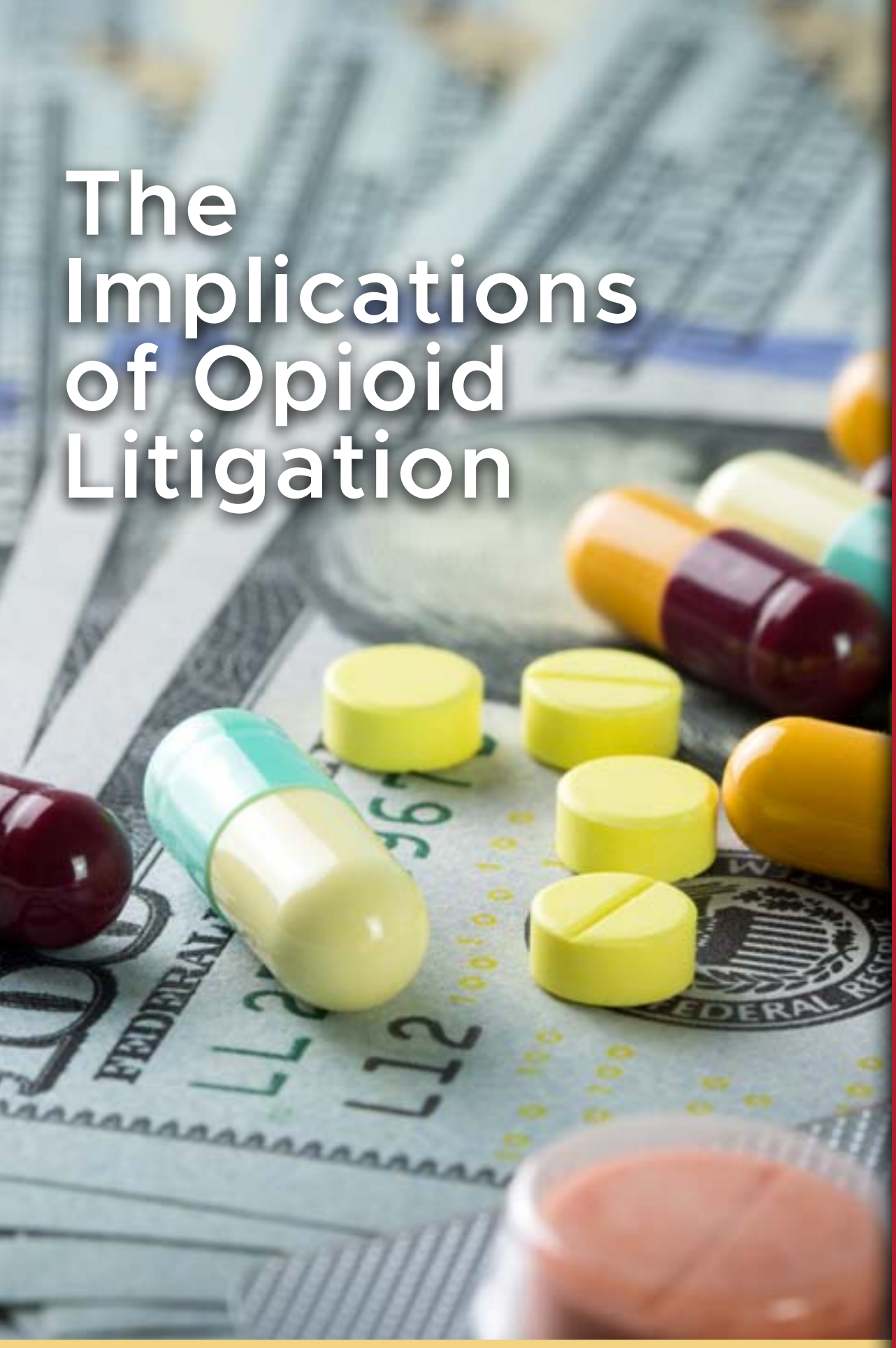

The Implications of Opioid Litigation

ARIAS US

QUARTERLY

ALSO IN THIS ISSUE

- *The* Functus Officio *Doctrine*
- *Promoting Sound Decisions*
- *What's Left of* Bellefonte?

Q1 · 2018

2018 ARIAS•U.S. Spring Conference

May 9 – 11, 2018
The Breakers Palm Beach, Florida

Mark Your Calendars!

ARIAS heads back to The Breakers this year. *"Once you stay, you'll understand"* is the Breakers motto and for many ARIAS members, you know the resort provides an unparalleled experience! Since our stay in 2016, The Breakers has undergone extensive updates to its restaurants, grounds, and accommodations. So make your plans now to join us in the spring for networking, education, and relaxation!

Hotel Accommodations & Reservations: ARIAS·U.S. has secured a block of rooms at a reduced rate at The Breakers. The room block rate ends on April 9, 2018. To make your room reservation, visit **https://aws.passkey.com/go/ARIAS18** to be taken to the reservation site or call 1-888-273-2537. Be sure to mention you are attending the 2018 ARIAS·U.S. Spring Conference to receive the reduced rate.
All accommodations are available on a first-come, first-served basis. Local taxes are not included. To hold your reservation, a one-night deposit is required. Check-in time is 4:00 p.m.

Registration opens on February 5th. Early bird registration ends on March 15th.

Details at www.arias-us.org

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EDITORIAL POLICY — ARIAS • U.S. welcomes manuscripts of original articles, book reviews, comments, and case notes from our members dealing with current and emerging issues in the field of insurance and reinsurance arbitration and dispute resolution. All contributions must be double-spaced electronic files in Microsoft Word or rich text format, with all references and footnotes numbered consecutively. The text supplied must contain all editorial revisions. Please include a brief biographical statement and a portrait style photograph in electronic form. The page limit for submissions is 5 single-spaced or 10 double-spaced pages. In the case of authors wishing to submit more lengthy articles, the *Quarterly* may require either a summary or an abridged version, which will be published in our hardcopy edition, with the entire article available online. Alternatively, the *Quarterly* may elect to publish as much of the article as can be contained in 5 printed pages, in which case the entire article will also be available on line. Manuscripts should be submitted as email attachments. Material accepted for publication becomes the property of ARIAS • U.S. No compensation is paid for published articles. Opinions and views expressed by the authors are not those of ARIAS • U.S., its Board of Directors, or its Editorial Board, nor should publication be deemed an endorsement of any views or positions contained therein.

Back in the mid-1990s, when ARIAS•U.S. was starting out, Dick Kennedy asked me to look at the first draft of the inaugural issue of the *Quarterly* and make any suggested revisions. Who knew that in 2018 I would become the editor of the *Quarterly*? Having come full circle, I want to thank my predecessor, Tom Stillman, for carrying the flag for the *Quarterly* for the past several years. Tom did a great job of encouraging arbitrators to contribute their thoughts to the magazine.

Editing the *Quarterly* comes with many challenges. First and foremost is living up to the expectations set by my predecessors, like Tom, Gene Wollan, and, of course, Dick Kennedy. Each prior editor had his or her own style. My style incudes a few pet peeves, but clarity and readability are primary. So when you submit an article for publication in the *Quarterly*, let's just say that legalese is not particularly welcome. And please don't start sentences with "however" or use "which" when you mean "that."

The news is moving quickly on the myriad cases that have been brought by various state and local officials seeking to hold pharmaceutical and other companies responsible for this crisis.

My goal is to continue the tradition of making the *Quarterly* a useful publication for ARIAS members. To do that, I will need your help. We have many thought leaders in ARIAS, and we need them to write articles. Who are these thought leaders? Just look in the mirror.

We want to hear from you. Each of you deals with important insurance and reinsurance issues every day. You speak and write about these issues—write for the *Quarterly*, too! Leverage your internal and external communications by turning them into articles.

This issue contains some great articles on a wide variety of subjects. Damon Vocke and Mark Bradford from Duane Morris LLP have written an excellent article on our Latin friend, the *functus officio* doctrine. Titled "*Functus Officio*: Because All Things Must Come to Pass, The Real Question Is on What Terms?" the article discusses the doctrine and describes the limited exceptions to it and how it applies to reinsurance disputes.

J.P. Jaillet and Rob Kole of Choate, Hall & Stewart LLP have put together an interesting article on the opioid crisis and the litigation arising from this scourge. The news is moving quickly on the myriad cases that have been brought by various state and local officials seeking to hold pharmaceutical and other companies responsible for this crisis. The article, titled "Opioid Litigation and Its Insurance and Reinsurance Implications," will be helpful for claims professionals faced with the defense and indemnification requests flowing from the various lawsuits.

On a less controversial note, longtime arbitrator Richard Waterman has prepared a very interesting article on arbitrator decision making. Titled "Making Good Arbitration Decisions: An Arbitrator's Viewpoint," Richard brings his insightful analysis to this most important arbitral task.

Amy Kline and Angella Middleton from Saul Ewing Arnstein & Lehr LLP, along with Jamie Scrimgeour of Travelers, have followed up on their presentation at the ARIAS 2017 Fall Conference with an article on the *Global v. Century* decision from the New York Court of Appeals. Titled "Global Domination? What's Left of the *Bellefonte* Rule Post-*Global Reinsurance Corp. of America v. Century Indemnity Co*.?" the article outlines the cases pending that involve the *Bellefonte* rule and discusses how these cases may be decided.

Of course, this issue also contains its regular features, including case summaries from the Law Committee. It also includes some interesting information about our venue for the 2018 Spring Conference, The Breakers in Palm Beach, Florida. Most of you know (or know about) The Breakers, one of the most famous beachside resorts on Florida's East coast. The Breakers has everything you can want in a conference venue and more, plus it's conveniently located in Palm Beach, with its outstanding shopping and restaurants. The Spring Conference will be held May 9-11, and by the time you read this, you should be able to register and make your hotel reservations. You really don't want to miss the Spring Conference, so register today.

Finally, I hope you enjoy this issue of the *Quarterly*, and I hope you consider contributing articles in the future. Whether you have published before or are a member who has never published, I welcome your participation and your thought leadership. If you have article ideas or ideas for additional content, give me a call or send me an e-mail.

— Larry P. Schiffer

EDITOR'S LETTER

OnDemand Webinars

All 2018 OnDemand webinars are available for purchase and count toward the 2018 recertification requirements until December 31. All 2017 and prior OnDemand webinars are available to view for free. You can find them on the ARIAS website for download and/or purchase!

2018 Webinars

January 25	What are the "CAT" Bonds and How do they Differ from Insurance and Reinsurance?
February 21	The Year in Review: A Discussion of Significant 2017 Cases Arbitrators Need to Know

2017 Webinars

February 8	The Increasing Relevance of Runoff
April 18	Avoiding the Trip-Wire: Current Issues in the Attorney-Client Privilege
June 8	Information Security and Social Media
September 26	After the Final Award: When is it permissible and appropriate for panels to retain jurisdiction?
October 26	Direct Insurance Arbitrations: What ARIAS Arbitrators Need to Know

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Functus Officio: Because All Things Must Come to Pass, the Real Question Is, on What Terms?

By Damon N. Vocke and Mark A. Bradford

Every reinsurance transaction, be it treaty or facultative business, must eventually come to an end no matter how long the tail or eye-popping the loss ratio (good or bad). Today's award engendered by yesterday's dispute eventually becomes tomorrow's tale, possibly shared as part of the industry's proverbial water cooler gossip (subject to maintaining appropriate confidentiality). The doctrine of *functus officio*, a Latin term translated as "a task performed," helps provide finality to arbitration so the proverbial next chapter can begin.[1]

One key distinction between arbitration and litigation is that, in arbitration, there is no appeal—hence the significant and important role of the doctrine of *functus officio*. The parties to an arbitration typically contract for finality, efficiency, and confidentiality throughout the arbitration process. These contractual aims are imperiled if a party turns to the courts, where litigation proceedings (unlike arbitration) take place in the public domain and may cause further uncertainty, expense, and delay.

This article briefly summarizes the legal doctrine of *functus officio*, i.e., the termination of an arbitration panel's authority once a "final" decision is rendered. It then explores how reinsurance executives, arbitrators, and legal practitioners might utilize the doctrine to their or their client's respective advantage.

The Doctrine

It is well recognized that once an arbitration panel renders a final decision, the panel becomes *functus officio* and lacks authority to re-examine or modify that decision absent certain exceptions or agreement of the parties.[2] That is not to say that an arbitration panel cannot continue its work following an interim decision[3] or issue an order "to correct obvious error in the translation of the [p]anel's own decision into an award-amount."[4] What is prohibited is another bite at the apple. The lack of an appeal in arbitration prohibits re-examination of the award, including the factual or legal underpinnings of the award. "[F]or there is no opportunity for redetermination on the merits of what has already been decided."[5]

The policy underlying the doctrine of *functus officio* arises from an "unwillingness to permit one who is not a judicial officer and who acts informally and sporadically, to re-examine a final decision which he has already rendered, because of the potential evil of outside communication and unilateral influence which might affect a new conclusion."[6] This makes sense, as arbitration serves the dual purposes of (1) resolving disputes efficiently before learned persons with subject matter expertise and experience, and (2) avoiding long, expensive, and protracted litigation.[7] On one hand, courts recognize that "[a] primary reason for the resolution of such disputes via arbitration is that judges . . . are inexpert in the arcana of reinsurance calculations."[8] On the other hand, arbitrators do not have the institutional protection or distance of judges and may explicitly or implicitly feel subject to industry pressures.[9] As a result, forcing a party to resubmit an issue to an arbitration panel may constitute irreparable harm, warranting the issuance of an injunction.[10]

Functus officio blossomed in what courts have called the "bad old days when judges were hostile to arbitration and ingenious in hamstringing it."[11] It addresses the concern that arbitrators not bound by the continuity of judicial office could be inundated with, and possibly impermissibly swayed by, demands from disappointed parties.[12] The limitation on arbitrators' jurisdictional authority under *functus officio* is similarly supported by principles of contract.[13] Panels may only resolve those disputes that the parties have agreed to submit to an arbitrator. Once the panel has finally resolved the issues before it, it lacks the authority to do more.

Exceptions to the Doctrine

Despite the best efforts of arbitration panels, some decisions will inevitably embody inaccurate, incomplete, or ambiguous results. To err is human, so arbitrators, like judges, will sometimes make mistakes, overlook contingencies, or lack clarity in rendering a decision and thus require clarification as to a final award already made.[14] Accordingly, courts generally recognize three exceptions to the doctrine of *functus officio*. Under these exceptions, arbitrators may: (1) correct a mistake apparent on the face of an award; (2) decide an issue that has been submitted but not completely adjudicated by the original award, as the arbitrators have not exhausted their authority; or (3) clarify or construe an arbitration award that seems complete but proves to be ambiguous in its scope and implementation.[15] The exceptions threaten to swallow the rule, such that the exact limitations imposed by *functus officio* are as clear as mud.

Any party wishing to utilize one of the exceptions—or a party seeking to oppose such an exception—should keep in mind that any correction or clarification must occur within a relatively short period of time. First, the Federal Arbitration Act, where applicable, provides a three-month period for challenging an arbitration award.[16] Second, courts generally limit an arbitration panel's power to clarify an award (when appropriate for the panel to exercise such authority) to a reasonable time after the final award.[17] One month[18] has been held to be a reasonable amount of time, but 8 years,[19] 18 months,[20] and, in one instance, more than 90 days[21] have been rejected as unreasonable and out of bounds.

The exceptions are limited "to prevent arbitrators from engaging in practices that might encourage them to change their reasoning about a decision, to redirect a distribution of an award, or to change a party's expectations about its rights and liabilities contained in an award."[22] While courts regularly recognize these exceptions, any arbitral correction or clarification must not modify or augment the substance of the award.[23] An "advisory opinion" from the panel is improper.[24] However, there is no bright line rule as to how or when to apply the following points:

1. The Mistake Exception. The mistake exception is confined to "clerical mistakes or obvious errors in arithmetic computation."[25] For example, in *Clarendon National Insurance Co. v. TIG*

Generally, reviewing courts will only approve the correction of mistakes and not modification of an award.

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FUNCTUS OFFICIO

Reinsurance Co., the panel issued an interim award on the first of three issues to be resolved concerning a portfolio reinsurance agreement in the amount of $4,836,000 to which pre-judgment and post-judgment interest were added as confirmed in a judgment.[26] The panel then reconvened to consider the second and third issues and, in the process, realized an arithmetical error that reduced the interim award on the first issue by $346,000, to $4,498,000.[27] The court held that "substantial justice" warranted modifying the award and confirmed judgment in light of the panel recognizing its mathematical mistake.[28]

Generally, reviewing courts will only approve the correction of mistakes and not modification of an award.[29] An award based on a mistaken understanding of fact or law should not later be corrected, as doing so would require the facts or law to be reconsidered, and a final arbitration award should be enforced despite disagreement on the merits by the confirming court so long as there is a barely colorable justification for the outcome reached.[30]

The decision in *Colonial Pennsylvania Insurance Co. v. Omaha Indemnity Co.*, is also instructive.[31] In that case, the arbitration panel ordered the release of any and all claims to certain reserves.[32] Thereafter, a majority of the panel issued a second order deleting the reference to the release of reserves and requiring the reinsurer to pay an additional $8,988,783 to represent its share of the reserves necessary to pay losses arising out of the original agreement.[33] The district court approved the amended award, but the Third Circuit reversed and remanded, finding the "application of the 'mistake on the face of the award' standard [could] not be sustained."[34] The court of review reasoned that arbitral awards must be regarded as final, and "in extending the limited exception for mistakes apparent on the face of the award to a situation where extraneous facts must be considered, the district court opened a Pandora's box which could subvert the policies on which the application of *functus officio* to arbitral decisions are predicated."

2. The Finality Exception. The so-called finality exception is more of a condition precedent than an exception. It merely provides that an award must be final for the doctrine of *functus officio* to apply.[35] Failure to obtain judicial confirmation is not determinative or fatal as to whether an arbitration award is final.[36] While an award cannot be final if significant issues remain for the panel to determine, an award does not have to be final in all aspects for *functus officio* to apply.[37] It is the scope of the arbitration agreement and the issues presented for consideration as framed by the parties that determine whether the panel has exhausted its grant of authority for purposes of finality.[38]

While an award cannot be final if significant issues remain for the panel to determine, an award does not have to be final in all aspects for functus officio to apply.

The completion exception provides arbitrators with authority to complete awards in which the final decision did not address all of the issues submitted for decision or where the panel expressly retained jurisdiction to resolve an issue.[39] However, a final interim award in a phased proceeding may be final for purposes of *functus officio* if nothing remains to be decided as to that issue.[40]

3. The Clarification Exception. The third exception to the doctrine of *functus officio* permits arbitrators to revisit an award that is incomplete or ambiguous.[41] While the merits of the controversy may not be revisited, a remand for clarification of the intended meaning of an arbitration award may be ordered when the remedy awarded by the arbitrator is ambiguous.[42] When a matter is remanded for clarification, the panel is limited to clarifying the issues raised by the court rather than broadly reconsidering the totality of its decision.[43] By way of example, one court went so far as to give detailed alternatives on how an award might be interpreted as regarding certain disputes over loss adjustment expenses.[44] That court considered the arguments of both parties and gave limiting instructions as to the scope of the panel's clarifying review.[45]

Permitting clarification "serves the practical need for the district court to ascertain the intention of the arbitrators so that the award can be enforced, [so] there is not even a theoretical inconsistency with the *functus officio* doctrine."[46] Where the court cannot ascertain the intent of the award, "[a] remand to the arbitrator avoids misinterpretation of the award by the court, and more likely results in the parties obtaining the award for which they bargained."[47]

Contracting around the Doctrine

Parties may want to consider drafting their arbitration agreements in a manner that avoids the sometimes harsh realities of *functus officio* and the attendant uncertainties that litigation over arbitrator authority engenders. Possible contractual solutions include: (1) either authorizing to seek—or, perhaps more appealing for purposes of true finality and cost efficiency, prohibiting the parties from seeking—post-award correction, reconsideration, clarification, or completion; (2) requiring the panel to circulate a draft award for review prior to issuing the final decision; and/or (3) providing for the panel to retain jurisdiction for a limited amount of time (e.g., 60 days) to handle any post-award issues. Obviously, the latter two suggestions likely protract the dispute and increase the expense, although perhaps this is more favorable than post-award litigation.[48]

As the doctrine only applies absent agreement of the parties, it is possible to address some of these issues when initially contracting.[49] The challenge, of course, lies in the uncertainty at the time of contract formation concerning: (1) whether there may be a dispute and, if so, the ultimate composition of the panel; (2) whether the dispute is arbitrated and not settled; and (3) whether the contracting party has the faith and confidence to rely on the "final" decision rendered or will assume the risk (or potential benefit) of a post-award judicial challenge on any one or more of the grounds summarized above.

When Only One Party Requests Modification or Clarification

It is also possible for parties to address *functus officio* on an ad hoc, post-award basis. While it may generally seem that only one party will want to seek clarification from the panel, it is important for industry personnel and practitioners to keep in mind that an opponent requesting an agreement to submit an issue (or issues) to the panel for reconsideration, modification, or clarification provides an opportune moment to negotiate over other points or obtain other concessions (or, as the "prevailing" party may see it, to take another bite at the apple and further prolong and delay final resolution for settlement leverage or otherwise).

This article opened by stating that every book of reinsurance must come to an end, as must every arbitration. That statement remains true, such that it may be important to consider the broader picture when faced with issues created by the doctrine of *functus officio*. In other words, do not win a battle to lose the war. The party now opposing further review by an arbitration panel may next time be the party asking the same counterparty that now wants further review (and may next time oppose it) for the same concession. While there is no right answer to these ques-

Parties may want to consider drafting their arbitration agreements in a manner that avoids the sometimes harsh realities of functus officio and the attendant uncertainties that litigation over arbitrator authority engenders.

tions, parties may obtain finality and avoid litigation costs by agreeing to some limited review by the panel—the scope of which can be negotiated and contractually defined by the parties—as compared to a court-ordered remand that could take a different tone if the issue is fully litigated. Once again, post-award litigation will inevitably undermine the essential purposes of arbitration: finality, efficiency, and confidentiality.

The party now opposing further review by an arbitration panel may next time be the party asking the same counterparty that now wants further review (and may next time oppose it) for the same concession.

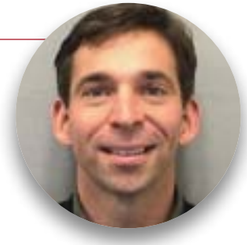
1. *Colonial Penn Insurance Co. v. Omaha Indemnity Co.*, 943 F.2d 327, 331 n.3 (3d Cir. 1991). ("*Functus officio* derives from the Latin meaning 'a task performed' and is defined by Black's as 'having fulfilled the function discharged the office or accomplished the purpose, and therefore of no further force or authority.' *Black's Law Dictionary,* 606, 5th ed., 1979.")
2. *RGA Reinsurance Co. v. Ulico Casualty Co.*, 355 F.3d 1136, 1139 (8th Cir. 2004) (affirming district court's confirmation of award on de novo review and holding that "proceedings were properly characterized as a confirmation rather than a modification."); *Arrowood Indemnity Co. v. Trustmark Insurance Co.*, 938 F. Supp. 2d 267, 274 (D. Conn. 2013) (recognizing "limited authority" to remand to a panel "to correct certain mistakes") (quoting *Trade & Tranp., Inc. v. National Petroleum Charterers Inc.*, 931 F.2d 191, 195 (2d Cir. 1991)).
3. *U.S. Life Insurance Co. v. Superior National Insurance Co.*, 591 F.3d 1167, 1177 n. 11 (9th Cir. 2010). In this decision, the Court of Appeals held that the panel's styling of an award as "Phase II Interim Final Award" "belie[d]" the reinsurer's argument that the Phase II award was final such that a subsequent award was not void under the doctrine of functus officio. Id.
4. *Global Reinsurance Corp. v. Argonaut Insurance Co.*, 548 F. Supp. 2d 104, 111 (S.D.N.Y. 2008).
5. *Hartford Steam Boiler Inspection & Insurance Co. v. Underwriters at Lloyd's & Companies Collective*, 857 A.2d 893, 901 (Conn. 2004) (quoting *La Vale Plaza, Inc. v. R.S. Noonan, Inc.*, 378 F.2d 569, 573 (3d Cir. 1967)).
6. *Colonial Penn Insurance Co.*, 943 F.2d at 331-32.
7. *Menorah Insurance Co., Ltd. v. INX Reinsurance Corp.*, 72 F.3d 218, 223 (1st Cir. 1995); *R&Q Reinsurance Co. v. Utica Mutual Insurance Co.*, 18 F. Supp.3d 389, 392-93 (S.D.N.Y. 2014).
8. *Unionamerica Insurance Co., Ltd. v. Allstate Insurance Co.*, 302 F. Supp. 2d 865, 868 (N.D. Ill. 2004).
9. *Koken v. Cologne Reinsurance* (Barbados) Ltd., No. 1:cv-98-678, 2006 WL 6577172 (M.D. Penn. Dec. 5, 2006); *Lanier v. Old Republic Insurance Co.*, 936 F. Supp. 839, 848 (M.D. Ala. 1996).
10. *Unionamerica Insurance Co.*, 302 F. Supp. 2d at 868.
11. *Clarendon National Insurance Co. v. TIG Reinsurance Co.*, 183 F.R.D. 112, 117 (S.D.N.Y. 1998) (quoting *Glass, Molders, Pottery, Plastics & Allied Workers International Union v. Excelsior Foundry Co.*, 56 F.3d 844, 846-47 (7th Cir. 1995)).
12. Id.
13. *Mutual Fire, Marine & Inland Insurance Co. v. Norad Reinsurance Co., Ltd.*, 868 F.2d 52, 58 (3d Cir. 1989); *Continental Cas. Co. v. Scandinavian Reinsurance Co.*, Ltd., No. 05-c-2349, 2005 WL 2171187 at *2 (N.D. Ill. Aug. 30, 2005); *Employers Insurance of Wausau v. Certain Underwriters at Lloyd's London*, 552 N.W.2d 420, 423, 425-26 (Wis. Ct. App. 1996).
14. *Cuna Mutual Insurance Soc. v. Office & Professional Employees International Union, Local 39*, 443 F.3d 556, 656 (7th Cir. 2006).
15. *Colonial Penn Insurance Co., 943* F.2d at 332; *Hartford Steam Boiler Inspection & Insurance Co.*, 857 A.2d at 900.
16. 9 U.S.C. §12; *Louisiana Health Serv. Indemnity Co. v. Gambro A B*, 756 F. Supp. 2d 760, 765-66 (W.D. La. 2010).
17. *Employers Insurance of Wausau v. El Banco Seguros Del Estado*, 357 F.3d 666, 670 (7th Cir. 2004).
18. *Clarendon National Insurance Co.*, 183 F.R.D. at 118.
19. *Employers Insurance of Wausau*, 357 at 670 ("Eight years is not a reasonable time.").
20. *Unionamerica Insurance Co., Ltd.*, 302 F. Supp. 2d at 868.
21. *R & Q Reinsurance Co.,* 18 F. Supp. 3d at 395. The court in *R & Q Reinsurance Co.* based its decision on the fact that the party requesting the remand did not do so until after the date that the panel had stated it would cease to exist in the award. In other words, the panel set a reasonable time (90 days after issuance of the award) for its dissolution and, therefore, set the outrebounds of the reasonable time for any challenges. Id.
22. *Teamsters Local 312 v. Matlack, Inc.*, 118 F.3d 985, 992 (3d Cir. 1997) (citing *Colonial Penn*, 943 F.2d 332, for proposition).
23. *Global Reinsurance Corp.*, 548 F. Supp. 2d at 111 (addressing order clarifying recovery on non-clash claims).
24. *Arrow Indemnity Co.*, 938 F. Supp. 2d at 274.
25. *Colonial Penn*, 943 F.2d at 332.
26. 183 F.R.D. 112, 114 (S.D.N.Y. 1998).
27. Id.
28. Id. at 118.
29. *Arrow Indemnity Co.*, 938 F. Supp. 2d at 273-74.
30. *R & Q Reinsurance Co.*, 18 F. Supp. 3d at 393.
31. 943 F.2d 327 (3d Cir. 1991).
32. Id. at 329.
33. Id. at 330.
34. Id. at 332.
35. *Legion Insurance Co. v. VCW, Inc.*, 198 F.3d 718, 720 (8th Cir. 1999).
36. *Federated Rural Elec. Inc. Exchange v. Nationwide Mutual Insurance Co.*, 134 F. Supp. 2d 923, 932 (S.D. Ohio 2001).
37. *Legion Insurance Co.*, 198 F.3d at 720.
38. *Mutual Fire, Marine & Inland Insurance Co.*, 868 F.2d at 58.
39. *National Indemnity Co. v. IRB Brasil Resseguros S.A.*, 164 F. Supp. 3d 457, 487 (S.D.N.Y. 2016).
40. *Employers' Surplus Lines Insurance Co. v. Global Reinsurance Corp.*-U.S. Branch, 07 Civ. 2521(HB), 2008 WL 337317 at *6 (S.D.N.Y. Feb. 6, 2008).
41. *Global Reinsurance Corp.*, 548 F. Supp. 2d at 111 n.50 (citing *Colonial Penn Insurance Co.*, 943 F.2d at 332).
42. *Hartford Steam Boiler Inspection & Insurance Co.*, 857 A.2d at 900-01.
43. Id. at 901.
44. Lanier, 936 F. Supp. at 851.
45. Id. at 849-50.
46. *Colonial Penn*, 943 F.2d at 334.
47. *General Accident Insurance Co. of Am. v. MSL Enterp., Inc.*, 547 s.E.2d 97, 101 (N.C. Ct. App. 2001).
48. Thomas A. Allen, Robyn D. Herman, Clarification, Reconsideration and the Doctrine of Funcus Officio, *ARIAS QUARTERLY*, Vol. XI No. 2 5, 8 (2004).
49. *Hartford Steam Boiler Inspection & Insurance Co.*, 857 A.2d at 900 n. 11 ("The doctrine of *functus officio* serves as a default rule, and it applies only in the absence of an agreement between the parties to the contrary.").

Global Domination? What's Left of the *Bellefonte* Rule after *Global Reinsurance Corp. of America v. Century Indemnity Co.*?

By Amy S. Kline, Angella N. Middleton, and James D. Scrimgeour[1]

Since the U.S. Court of Appeals for the Second Circuit decided *Bellefonte Reinsurance Co. v. Aetna Casualty & Surety Co.*[2] 28 years ago, the majority of courts that have considered whether reinsurers' losses are capped under facultative certificates at the stated amount on the face of a certificate have identified the decision as persuasive, if not dispositive, authority. For more than two decades, the so-called "*Bellefonte* Rule" was applied by courts consistently, without regard for differences in the language of the certificates being interpreted. As noted in this publication's Second Quarter 2015 issue, that trend slowed in recent years as courts began to more frequently consider contract wording variations and distinguish *Bellefonte*.

This momentum peaked most recently in the *sua sponte* decision by the Second Circuit in *Global Reinsurance Corp. of America v. Century Indemnity Co.*[3] to certify to the New York Court of Appeals the question of whether the court's decision in *Excess Insurance Co. v. Factory Mutual Insurance Co.*[4] imposed "either a rule of construction, or a strong presumption, that a per occurrence liability cap in a reinsurance contract limits the total reinsurance available under the contract to the amount of the cap regardless of whether the underlying policy is understood to cover expenses such as, for instance, defense costs."[5] The Court of Appeals answered this question in the negative, holding that "[u]nder New York law generally, and in *Excess* in particular, there is neither a rule of construction nor a presumption that a per occurrence liability limitation in a reinsurance contract caps all obligations of the reinsurer, such as



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payments made to reimburse the reinsured's defense costs."[6]

Although the New York Court of Appeals answered the Second Circuit's certified question, its answer—that there is no bright-line rule, or even a presumption, to be applied in interpreting reinsurance facultative certificates—leaves open myriad potential outcomes in *Global*, and for pending and future cases in which this issue is raised.[7]

This article addresses the potential impact of *Global II*, focusing on the future treatment of *Bellefonte*, *Unigard Security Insurance Co. v. North River Insurance Co.*,[8] and their progeny by courts in the Second Circuit and elsewhere.

Bellefonte in the Second Circuit and New York

There are several pending cases that will tell us how the Bellefonte Rule will be treated by the Second Circuit and under New York law.

There are several pending cases that will tell us how the *Bellefonte* Rule will be treated by the Second Circuit and under New York law, and whether it still has life. These cases may also result in a potential distinction between the law as interpreted by the Second Circuit and the law in state court.

The first is *Global* itself, of which, following *Global II*, the Second Circuit will now resume its consideration.[9] Another case to watch is *Utica Mutual Insurance Co. v. Clearwater Insurance Co.*, which is also pending before the Second Circuit.[10] The latter case is on appeal from the order of the Southern District of New York granting Clearwater's motion for summary judgment and holding that the reinsurance-accepted cap in the certificate was expense-inclusive.[11] A third is *Utica Mutual Insurance Co. v. Alfa Mutual Insurance Co.*, which is pending in the New York state courts.[12] There, the New York Appellate Division affirmed the decision of the New York Supreme Court granting partial summary judgment to Alfa. Relying on *Excess*, the court found that the reinsurer's liability for loss and expense is capped by the face amount of reinsurance accepted under each certificate.

What does *Global II* mean for these cases, and what can these cases tell us about the future of the *Bellefonte* Rule? The answers are many.

First, it appears unlikely that these issues will be resolved immediately by the Second Circuit. To be sure, in certifying the case to the New York Court of Appeals, the *Global I* court made comments that appear to be favorable to the cedent's position. As favorable as that language was, however, there is no mechanism by which that court would be likely to reverse the judgment of the District Court and enter judgment in favor of the cedents without first remanding.

The lack of a mechanism is unlikely to stop cedents with cases currently before the Second Circuit from trying; indeed, Utica has already asked the Second Circuit to reverse the District Court's decision and enter judgment in its favor. Utica reads *Global II* to create a principle of concurrency, which means that a follow-the-form clause requires a reinsurer, as a matter of law, to cover expenses in addition to limits where the certificate and the underlying policy are concurrent. While there is some non-binding Second Circuit case law affirming a Judge Rakoff decision endorsing that presumption in facultative certificates where there is a follow-the-form clause,[13] the safer course would certainly be to remand the matter to the District Court. Were the Second Circuit to adopt Utica's position and read *Global II* this way, the impact would be profound: whereas, previously, courts arguably applied a presumption that the reinsurance limit was expense-inclusive, such a holding would mean that where the certificate and underlying policy are concurrent via a follow-the-form clause, expenses are, necessarily, not subject to the limit and *Bellefonte*, as we know it, would be dead.

Such a result, however, seems improbable. The *Global II* court described its calling as a "narrow" one: to decide "whether *Excess* imposes either a rule of construction, or a strong presumption, that a per-occurrence liability cap in a reinsurance contract limits the total reinsurance available under the contract."[14] Further, the *Global II* court observed that *Excess* involved loss adjustment expenses and stated, specifically, that in *Excess*, "[w]hether a similar (or even identical) limitation clause would apply to third-party defense costs, in a certificate reinsuring a liability insurance policy, was never at issue. Consequently, the *Excess* court did not pass on whether a follow-the-form clause such as the one in that case . . . would require the reinsurers to cover third-party defense costs in excess of such a limit."[15]

Second, based on the language by the *Global I* court seeking certification, the Second Circuit summarily affirming in the reinsurers' favor in either *Global* or *Utica* is highly unlikely. In addressing whether *Bellefonte* and *Unigard* were wrongly decided, the court found this suggestion "not without force" and questioned, specifically, "the *Bellefonte* court's conclusion that the reinsurance certificate in that case unambiguously capped the reinsurer's liability for both loss and expenses," finding it "not entirely clear what exactly the 'Reinsurance Accepted' provision in *Bellefonte* meant."[16] Further, with respect to *Clearwater*, the *Global II* court identified it as a case in which the District Court read *Excess*, incorrectly, to say that third-party defense costs under any facultative reinsurance contract are unambiguously or presumptively capped by the liability limits in the certificate.[17]

While it can be reasonably expected that reinsurers will argue—notwithstanding this language from the *Global I* and *Global II* courts that their certificates are unambiguously expense-inclusive—it is difficult to imagine that courts applying New York law will, or can, continue to summarily agree. In this way, *Bellefonte*, applied this way, will not survive, and the so-called "*Bellefonte* Rule" appears to be dead.

The third and most likely scenario involves vacating the judgments entered by the District Courts, respectively, and remanding the matters for further proceedings consistent with direction from the *Global II* court.[18] In such a scenario, the District Courts' approach on remand is certain to be guided by any direction provided by the Second Circuit. In this guidance we may reasonably expect insight into the court's view on the continued viability of *Bellefonte*.

Instead of a rule or presumption, *Global II* makes explicit that each policy is to be construed solely in light of its specific language. Were the court inclined to overrule *Bellefonte*, such a ruling would have to be based on the conclusion that the *Bellefonte* court did not interpret the certificates pursuant to the New York rules of contract interpretation. Such a finding, however, is both (1) inconsistent with *Global I's* observation that in cases involving contract rights, "considerations favoring *stare decisis* are at their acme,"[19] and (2) unnecessary. Rather, using the requirement that each contract be interpreted individually according to its express terms and context, *Bellefonte* can be, effectively, limited to its facts. In that scenario, *Bellefonte* would not be overruled, but a limit to its precedential value would be expressly recognized.

Using the requirement that each contract be interpreted individually according to its express terms and context, Bellefonte can be, effectively, limited to its facts.

The practical result of *Global II* should be that reinsurers litigating in the Second Circuit will likely go back to life before *Excess* and *Bellefonte* and, absent unusual contract language or evidence of a specific intent, no longer deny expenses in addition to limits on otherwise payable claims involving policies with covered expenses in addition to

Global II *may be influential in persuading Illinois courts to interpret each contract according to its specific terms, rather than relying upon results involving "similar" language.*

limits.

In the New York state courts, however, it is less clear what effect *Global II* will have on *Bellefonte* cases. As of the time of this publication, in the *Utica Mutual v. Alfa Mutual litigation*,[20] Utica has withdrawn its motion for reconsideration of the Appellate Division's decision and motion for leave to appeal to the Court of Appeals, and the matter is instead headed back to the trial court. It is possible, based on *Global II*, that the court could find that the certificate language is ambiguous. It is a distinct possibility, however, that the court could issue a ruling reinforcing its initial analysis of the certificate as based on the contract interpretation principles articulated in *Global II*.[21] Of course, if that result occurs—or even if a reversal in favor of the cedent ensues under the same principles—we fully expect there to be further statements from the New York appellate courts on this issue.

The *Bellefonte* Rule in Illinois

The *Bellefonte* Rule spread not only through New York and the Second Circuit, but into Illinois as well. In *Continental Casualty Co. v. Midstates Reinsurance Corp.*,[22] the Illinois Court of Appeals held that the reinsurance certificate at issue was clear and unambiguous and that the "reinsurance assumed" provision created an overall limitation on the obligation to reinsure both losses and expenses.[23] The court observed that the contract terms in *Bellefonte* were "similar" to the provisions in *Midstates* and that "the *Bellefonte* case and following cases interpreting this same, or similar, language" were persuasive.[24] The court further held that the cedent's reliance on *Penn Re, Inc. v. Aetna Casualty & Surety Co.*[25] was misplaced. In *Penn Re*, the court found "the precise amount of coverage" under the reinsurance certificate "to be inherently ambiguous" and thus "decline[d] to construe the terms as a matter of law." The court in *Midstates* distinguished *Penn Re*, however, because it "was decided before *Bellefonte* and does not enjoy the same support in case law."[26]

From this, there are two potential takeaways. First, *Global II* may be influential in persuading Illinois courts to interpret each contract according to its specific terms, rather than relying upon results involving "similar" language. Second, to the extent that the "support" afforded by other courts to *Bellefonte* informs a court's decision, the criticism of *Bellefonte* by the *Global I* court and the guidance by the *Global II* court may be equally informative. It is likely that some reinsurers reviewing claims subject to Illinois law will continue to claim the presumption based on the "*Midstates* Rule" and deny expenses in addition to limits until there is a definitive statement from the Illinois Court of Appeals about the continued viability of *Midstates*.

The *Bellefonte* Rule in Pennsylvania

The seminal *Bellefonte* Rule case in Pennsylvania is *Century Indemnity Co. v. OneBeacon Insurance Co.*[27] There, OneBeacon filed a declaratory judgment action against Century on the ground that the "Reinsurance Accepted" limit in the certificates placed a total cap on its liability, including expenses. The trial court denied the motion for summary judgment.[28] In so doing, the court specifically considered and rejected *Bellefonte*, holding instead that *Bellefonte* did not establish a blanket rule that all limits of liability are presumptively expense-inclusive. Rather, applying general rules of contract interpretation, the court found that there were variations from the certificate in *Bellefonte* and that extrinsic evidence was necessary to construe the terms of the contract in its entirety.

The trial judge then held a three-day hearing and found in favor of Century. On appeal, the Pennsylvania Superior Court agreed with the trial court's conclusion that the certificate language was ambiguous as to whether defense expenses are limited by the "Reinsurance Accepted" amount, and held that the court properly denied OneBeacon's motion for summary judgment.[29]

Pennsylvania law respecting this issue should remain unchanged by *Global II*. In short, Pennsylvania law (as articulated in *Century*) and New York law (as articulated in *Global II*) are aligned insofar as, under both, there is no presumption of expense inclusivity, and facultative certificates are each to be construed under their own terms.

Conclusion

To the extent that the impact of *Global II* can be predicted, the following reminder from the New York Court of Appeals in reviewing certificate language may provide the most useful guidance: "Our cases in the insurance context confirm that even modest variations on the face of a written agreement can alter the meaning of a critical term."[30] It is in these "modest variations" and the acknowledgment that evidence of intent may, in certain cases, be necessary to interpret the certificates that *Global II* may have the most impact. Whereas courts may previously have felt constrained to inflexibly apply *Bellefonte*, *Global II* opens the door to differentiating based upon the examination of specific language of the certificate at issue and the holding of further mini-hearings involving extrinsic evidence (regarding premium, etc.) that may tend to show an intent of concurrency, as happened in Pennsylvania.

This individual case-by-case analysis certainly suggests that reinsurers must be very selective in the cases they bring if they wish to avoid additional cedent-friendly jurisprudence on the horizon. If reinsurers do in fact take that tack, it will finally align reinsurers' approach in litigation with their approach in arbitration, providing much-desired consistency to companies evaluating their facultative reinsurance books.

1. The views expressed in this article are those of the author(s) and do not necessarily represent the views of The Travelers Companies, Inc. or any of its subsidiary insurance companies. Nothing in this article constitutes legal advice.
2. 903 F.2d 910 (2d Cir. 1990).
3. 843 F.3d 120 (2d Cir. 2016) [hereinafter *Global I*].
4. 3 N.Y.3d 577 (2004).
5. *Global Reinsurance Corp. of America v. Century Indemnity Co.*, — N.E.3d —, No. 124, 2017 WL 6374281 at *1 (N.Y. Dec. 14, 2017) [hereinafter *Global II*].
6. *Global II*, 2017 WL 6374281 at *1.
7. While the *Global I* court, in certifying the question to the New York Court of Appeals, did not limit the issue to facultative certificates, the *Global II* court expressly limited its decision to facultative certificates.
8. 4 F.3d 1049 (2d Cir. 1993).
9. As of this writing, the Second Circuit has not taken any action post-*Global II*.
10. *Utica Mutual Insurance Co. v. Clearwater Insurance Co.*, No. 16-2824 (2d Cir.). The parties briefed the *Bellefonte* issue, among others, and argued the matter before the Second Circuit on October 18, 2017. Now, the panel in *Clearwater* has been called upon to consider the impact of *Global II*.
11. Utica Mutual Insurance Co. v. Clearwater Insurance Co., No. 6:13-cv-1178 (GLS/TWD), 2014 WL 6610915, at *3 (N.D.N.Y. Nov. 20, 2014).
12. *Utica Mutual Insurance Co. v. Alfa Mutual Insurance Co.*, No. 1001, 17-00305 (N.Y. App. Div.).
13. *Travelers Casualty & Surety Co. v. Ace American ReInsurance Co.*, 392 F. Supp. 2d 659 (S.D.N.Y. 2005).
14. *Utica Mutual Insurance*, 2014 WL 6610915 at *6. The *Global II* court discussed the impact of follow-the-form and follow-the-settlements clauses only insofar as it summarized the issue presented to, and holding by, the court in *Excess*. To that end, the *Global II* court stated that *Excess* "addressed whether a reinsurer's obligation to pay loss adjustment expenses arising from a 'follow-the-settlements' clause was subject to the stated indemnification limit in the reinsurance policy." Id. at *3. This was material because it was the *Excess* court's holding that the "LIMIT" clause imposes an expense-inclusive cap notwithstanding the follow-the-settlements clause that was interpreted by subsequent courts to create a rule or presumption that third-party defense costs are capped by the liability limits in the certificate.
15. Id. at *4.
16. 843 F.3d at 126. The Second Circuit further observed that "[t]he purpose of reinsurance is to enable the reinsured to 'spread the risk of loss among one or more reinsurers.' If the amount stated in the 'Reinsurance Accepted' provision is an absolute cap on the reinsurer's liability for both loss and expense, then *Century*'s payment of defense costs could be entirely unreinsured. This seems to be in tension with the purpose of reinsurance." Id.
17. *Global II*, 2017 WL 6374281, at *4.
18. Such a result would be consistent with the Second Circuit's treatment of *Utica Mutual Insurance Co. v. Munich Reinsurance America, Inc.*, 594 Fed. Appx. 700 (2014), where the court held that the certificate at issue was ambiguous and remanded the matter and directed the District Court to consider extrinsic evidence in construing the contract. In what may also prove to be predictive of how these cases will be treated by reinsurers, Munich Re withdrew the *Bellefonte* issue as one to be addressed during the scheduled trial of the dispute.
19. Id. at 126.
20. *Utica Mutual Insurance Co. v. Alfa Mutual Insurance Co.*, No. 1001, 17-00305 (N.Y. App. Div.).
21. These same principles—that each contract should be read based on its specific words and circumstances rather than any sort of presumption based on prior case law interpreting similar language—were also confirmed by the Court of Appeals in *In re Viking Pump*, 52 N.E.3d 1144 (N.Y. 2016).
22. 24 N.E.3d 122 (Ill. App. Ct. 2014).
23. Id. at 126.
24. Id. (emphasis added).
25. No. 85–385–CIV–5, 1987 WL 909519 (E.D.N.C. June 30, 1987).
26. 24 N.E.3d at 128
27. 173 A.3d 784 (Pa. Super. Ct. 2017).
28. No. 02928 (Pa. C.C.P., Phila. Cty. Mar. 27, 2015).
29. 173 A.3d at 801.
30. *Global II*, 2017 WL 6374281, at *5.

Making Good Arbitration Decisions: An Arbitrator's Viewpoint

By Richard G. Waterman

It seems straightforward: men and women who serve on an arbitration panel want to make a good decision that is fair and accurate. The problem is how to distinguish a good decision that leads to the best outcome balanced with all other decision options.

Generally, a good decision in arbitration is one that makes effective use of reliable information available to the arbitrators at the time a decision is made. In practice, arbitrators must evaluate complex claims, facts, and arguments where uncertainty is bound to exist without being misled by cognitive biases that would lead to a bad decision. Arbitrators usually do not verify their decisions with complex mathematical formulas; instead, it is assumed by those who evaluate arbitration decisions that individuals serving on arbitration panels think critically about the facts and arguments while carefully evaluating other information that is knowable to increase the probability of a good-quality decision.

The assumption that arbitration panels make good decisions is based in part on the arbitration setting. Three panel members, each with diverse backgrounds and extensive business experience—including, in recent times, a tendency to come from a legal background practicing law rather than the ranks of industry practitioners—work together in a deliberative process to resolve important business disputes that the contesting parties disagree about intensely. Similar to other small groups of individuals who share a common purpose, arbitration panels are likely to make better-quality decisions than individuals acting alone. The independence of each panel member to confirm or reject the opinions reached by other panel members seems to prevent the kind of groupthink that can bedevil good decision making.

To provide some understanding of how arbitrators collaborate and process information to help make the best decisions, psychological researchers have tried to examine panel deliberations to determine whether their collective conclusions are optimal decisions consistent with the available evidence, witness testimony, common industry practice, and legal guidance. The limited research reveals the difficulty in assessing arbitrator performance, primarily because there is no objective way to measure the nature of an optimal or best decision. The reasons for a judgment are complex—in many instances, arbitrators must decide complicated issues with a range of variable decision outcomes. Moreover, arbitration deliberations are held in a private setting; no one can listen in. Information does not emerge after the decision is announced because arbitrators have an obligation to maintain privacy about statements made during deliberations.

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PROMOTING SOUND DECISIONS

Arbitrators also have tremendous discretion in deciding cases. Reinsurance agreements often allow arbitrators to interpret the agreement as an honorable engagement and not merely a legal obligation. They are usually relieved of all judicial formalities and abstain from following the strict rules of law. Additionally, reinsurance agreements generally provide that arbitrators can make their award with a view to affecting the general purpose of the agreement in a reasonable manner rather than in accordance with a literal interpretation of the language. Given the intentionally broad language of most contractual provisions, arbitrators must balance competing interests and make decisions based on their judgment of the facts and understanding of industry practices, which inescapably are a product of their personal life experiences and business judgment.

The Arbitration Process Structure

Prior to an arbitration hearing, arbitrators usually assess information contained in the parties' pre-hearing briefs, including selected evidentiary document exhibits. When the hearing begins, lawyers and legal assistants descend on the hearing venue to champion their case. They come armed with laptops, projectors, and iPads, ready to battle over the boxes full of exhibits, deposition transcripts, and other evidence. It is remarkable how well the lawyers can recall the information contained in so many documents, and how quickly the legal assistants can retrieve any document on a moment's notice and project it on a screen for all to see.

During the arbitration hearing, arbitrators listen to each side's arguments, evaluate the evidence, claims, facts, and statistics, and often consider expert technical information. Their analysis requires a lot of reading, careful thought, and a skeptical eye to avoid being misled by unreliable arguments or cognitive biases that could result in a sub-optimal decision. Although most present-day arbitration venues provide panel members with electronic access to briefs, documents, witness testimony, and a daily transcript of the hearing proceeding, arbitrators often take copious notes during the hearing for future reference. In their deliberations, arbitrators may rely heavily on their notes and memory to quickly recall specific relevant evidence that aligns with their interpretation of the evidence and to reject argumentative information that does not.

Debriefing conversations with arbitrators after a ruling has been announced (including with mock arbitration panelists) suggest that arbitrators frequently establish a clear leaning to a dominant opinion about the merits of a case by reading the pre-hearing briefs and supporting exhibits and listening to the opening statements. Indeed, there is evidence supporting the proposition that some arbitrators may have substantially made up their minds about the merits of what happened once deliberations begin, but may change their minds during deliberations about how to shape a ruling that is consistent with their strongly favored conclusion. Like business people, doctors, lawyers, and nearly all other decision makers, arbitrators are believed to think in terms of probabilities by considering and

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Participating in a collaborative body requires a willingness to accommodate the views of other members, so putting off sharing thoughts and viewpoints until the end of the evidentiary hearing may lead to a lack of critical thinking that is needed for accurate decision making.

evaluating incoming facts and evidence at early stages of a process and continuing to update and re-evaluate new facts and evidence as they come in. It is expected, therefore, that arbitrators will review the merits of a case as it progresses and will adjust their preliminary views with more considered judgment.

Decision-Making Style Differences

Three-member arbitration panels create the opportunity for a diversity of shared views to balance compelling interests and arguments. Arbitrators are expected to work together in an atmosphere in which multiple views and alternative interpretations of the facts are considered. Although the role of party-appointed arbitrators is not assumed to be impartial, their function is not to ignore all evidence that contradicts their conclusion, cast a vote for their nominating party, and attempt to persuade other panel members to do the same. When there is a built-in bias and opinions do not come with reasons or explanations, voting is usually along party lines. Ideally, with adequate time to properly consider arguments and examine the evidence, the accumulated expertise and wisdom of all three decision makers can be shared with each other to improve decision outcomes.

Although there are distinct differences between them, jury trial decision making has implications similar to arbitration. Granted, jurors are not given briefs or evidence exhibits before the trial begins and are told not to talk about the case with one another until the judge sends them to commence deliberations. Jurors are also charged to keep an open mind during the presentation of evidence and to avoid forming any conclusion until all the evidence has been presented and they have received instructions from the judge. Nonetheless, jury trial research has confirmed that jurors commonly form an early opinion about a case and may change their minds as the case progresses. Remarkably, according to some studies, the position favored by the majority of jurors at the beginning of deliberations became the jury's verdict in approximately 90 percent of trials.[1]

In contrast with a jury trial, arbitrators often speak to one another about aspects of a case as the arbitration is progressing unless there has been an agreement to hold off on case-related discussions until the hearing concludes. Edna Sussman, a professor and distinguished ADR practitioner in residence at Fordham University School of Law, surveyed more than 400 arbitrators in 2012 and found that 63 percent believed that sharing views early in the hearing process and discussing reactions to testimony and the developing merits of a case throughout the proceeding helped ensure that all aspects of a case were being fully considered throughout the hearing and improved the likelihood of a fair outcome.[2] The surveyed arbitrators believed that the benefits of having three decision makers on the arbitration panel would be lost if their views and reactions could not be exchanged and debated during the course of the proceeding.

Interestingly, the survey also showed that 27 percent of the arbitrators who responded to the survey followed a protocol similar to a court proceeding by waiting until the conclusion of the evidentiary hearing before talking to their fellow arbitrators about the merits of a case. Participating in a collaborative body requires a willingness to accommodate the views of other members, so putting off sharing thoughts and viewpoints until the end of the evidentiary hearing may lead to a lack of critical thinking that is needed for accurate decision making. As with jury admonitions, this practice does not forestall arbitrators from forming a preliminary view of a case and tending to favor a particular outcome before deliberations begin. For instance, making an early mistake in interpreting particular items of evidence may lead to a wrong decision if a panelist cannot be swayed from his/her mistaken opinion when deliberations begin.

Neutral arbitration panels commonly experience the benefits of exchanging views about a case and testimony while the hearing is ongoing. In their article "All-Neutral Arbitration Panels," Fowler, Hall, and Monin, three highly accomplished arbitrators, commented that when arbitrators are not encumbered by a partisan obligation, the panel can begin their discussion of the case while the hearing is ongoing and the evidence is fresh in their minds.[3] The authors also pointed out that panel members' collective experience and intellect help them identify key areas of testimony that may need clarification while counsel is available to comment.

An inherent benefit of arbitration is the contribution of each panel member in determining a final decision after critically evaluating the evidence and carefully considering all decision options. Concern about the ambiguities created by party-appointed arbitrators or that an arbitrator may speak out in a partisan manner should not be a cause to restrict communications among panel members during a proceeding, which is an acknowledged fundamental benefit of collaborative decision making. Parties choose arbitration to obtain a fair resolution of their dispute by three knowledgeable industry professionals working together. Instead of avoiding the exchange of thoughts and opinions during the course of a proceeding, it would be far more productive to engage effective techniques to temper partisan enthusiasm and foster effective, deliberative decision making.

Sharing Views for Optimal Decisions

The decision-making strategies of jurors, as well as those of arbitration panels with three knowledgeable individuals, are consistent with research studies and practical experience. Most decision makers begin to consider and evaluate facts and evidence at early stages of their personal deliberations, then continue to update and re-evaluate their views as new evidence comes in. A strategy intended to bolster high-quality decision making by an arbitration panel would incorporate a practice that encourages all panel members to share their knowledge and thoughts about the developing merits of a case in private conversations throughout the proceeding. These informal exchanges can lead to improved decision outcomes by ensuring all three panelists have a prominent role in understanding every aspect of the case and a shared responsibility in the final decision outcome. Interactive discussion also may help panel members evaluate accurate information as the case develops, instead of waiting for deliberations to debate the recollections and navigate the arguments of advocates with a biased perspective.

However, despite the apparent benefits of sharing insights while evidence is being presented, experienced arbitration panels agree in some instances to adopt a protocol similar to a judicial trial, whereby the arbitrators avoid sharing their reactions to what they hear or observe about witness testimony until the hearing is complete and the deliberation room is closed. There are several plausible explanations for implementing this procedural style. The most common is the belief that if panel members exchange views before all of the evidence has been heard, the discussions may lead to an early conclusion and thereby prejudice a fair result. Others are of the opinion that although party arbitrators have leeway in showing a leaning toward the party that appointed them, an umpire must maintain the appearance of pristine neutrality until the panel has convened for deliberation. Some panel umpires simply want to avoid potential pressures caused by partisan infighting, fired-up emotions, or problematic arbitrator conduct.

While preliminary research and survey findings are not representative of the entire population of arbitrators, this information provides a useful benchmark. A significant finding indicates that a majority of active arbitrators believe that sharing views during the hearing related to the presentation of

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It is possible that not engaging party arbitrators throughout the proceeding and making them jointly accountable for the final decision may create an environment in which party arbitrators appear to be overly partisan.

evidence or witness testimony is not likely to prejudge a fair outcome. For the same reasons that jurors are not forestalled from reaching an early decision without benefit of communicating with other jurors, experienced arbitrators are equally likely to reach an early conclusion about a case even if the full panel does not interact by sharing views throughout the proceeding. Moreover, the belief that a panel umpire must create a mirage of absolute impartiality in an arbitration setting may not advance the panel's goal to make the best decision. Umpires should be encouraged to weigh in with their experience, judgment, and skills in a measured and nonpartisan fashion throughout the proceeding. The best decisions emerge when a multiplicity of viewpoints are openly shared and debated and alternative outcomes are considered.

Party arbitrators are presumably predisposed toward their appointing party, and they have the task of making sure their appointing party's position is understood. During a lengthy, hard-fought, complex arbitration with a high volume of documents and briefings, any member of the panel may fail to notice or not fully appreciate the relative importance of specific information. An interactive arbitration panel sharing their analysis as they work together while the hearing is in progress may result in more accurate decisions. Moreover, it is possible that not engaging party arbitrators throughout the proceeding and making them jointly accountable for the final decision may create an environment in which party arbitrators appear to be overly partisan. Finally, an experienced umpire can effectively discourage unacceptable partisan behavior by pointing out, in a private conversation, how that behavior could affect the individual's reputation for objectivity, credibility, and esteem with other panel members.

Experienced arbitrators have suggested several strategies for improving the efficiency and quality of arbitration decisions by tapping the backgrounds and experiences of each panel member throughout a proceeding. One suggestion an arbitration panel may find useful is to sum up the evidence at the end of each hearing day. Another approach is to ask the party-appointed arbitrators to take turns summing up the evidence each day or have them switch sides on several occasions in explaining their reactions to and perspectives on the presented evidence. More commonly, panel members exchange their views and understanding of events with each other on an informal basis and often with an agreement to avoid discussions about the case during dinner.

Given that a large percentage of arbitrators are inclined to develop a strong view of a case in the early stages of a proceeding, perhaps the time has come to consider an alternative practice strategy for arbitrators—to share their views early in the process and discuss their reactions to the testimony throughout the proceeding to encourage open-minded thinking and promote good decision making that is fair and accurate.

1. Waites, Richard C., and James E. Lawrence. 2010. "Psychological Dynamics in International Arbitration Advocacy." In *The Art of Advocacy in International Arbitration*, ed. R. Doak Bishop and Edward G. Kehoe, 69-120. Huntington, N.Y.: Juris Publishing.
2. Sussman, Edna. 2013. "Arbitrator Decision-Making: Unconscious Psychological Influences and What You Can Do About Them." *The American Review of International Arbitration*, 24(3): 487-514.
3. Fowler, Caleb, Robert M. Hall, and Lawrence O. Monin. 2005. "All-Neutral Arbitration Panels." In *Mealey's Reinsurance Report*, 15(24).

Opioid Litigation and Its Insurance and Reinsurance Implications

By J.P. Jaillet and Rob Kole

Opioid addiction is a public health epidemic of enormous scope. According to the National Institute on Drug Abuse, more than 115 Americans die every day—and more than 40,000 per year—from opioid overdoses. The Centers for Disease Control and Prevention has estimated the annual cost of prescription opioid abuse to exceed $75 billion.[1]

Where costs of that magnitude are involved, extensive litigation follows. With extensive litigation inevitably come insurance and reinsurance implications—and, often, disputes.

Over the last several years, government entities have filed a growing number of lawsuits seeking to recoup their expenses associated with the opioid epidemic.[2] These cases have targeted pharmaceutical manufacturers, prescription opioid distributors, and pharmacies and doctors (among others) as defendants. The government plaintiffs typically allege that the manufacturer defendants intentionally overstated the benefits and downplayed the risks of opioids through aggressive marketing efforts, for the purpose of achieving blockbuster profits. With regard to the distributor defendants, plaintiffs typically allege that they failed to detect, investigate, or report excessive orders of prescription opioids.

In the past year, the number of these lawsuits has exploded. For example, more than 300 opioid lawsuits brought by states, counties, cities, and other government entities are currently pending, for pre-trial purposes, in a multi-district litigation in the U.S. District Court for the Northern District of Ohio. Numerous additional cases are pending in state courts. In addition to cases brought by government entities, individuals, hospitals, pension funds, and third-party payers

J.P. Jaillet chairs the Insurance & Reinsurance Group of Choate Hall & Stewart LLP in Boston. **Rob Kole** is a partner in Choate's Insurance & Reinsurance Group and has argued insurance and reinsurance disputes before the First, Second, Fifth, Ninth, and Eleventh Circuits of the U.S. Court of Appeals.

have brought lawsuits against the same universe of defendants.

Many of the opioid manufacturers and distributors have turned to their insurers for defense and indemnification. In this article, we examine certain key direct-side coverage issues posed by the underlying opioid lawsuits. We then examine the potential reinsurance coverage issues related to these claims.

Direct-Side Coverage Issues

The opioid lawsuits have spawned a growing body of insurance coverage litigation. These cases, which principally have involved the duty to defend, have focused primarily on three coverage issues: (a) whether the allegations in the underlying lawsuits constitute an "occurrence," (b) whether the lawsuits seek amounts that the insured is legally obligated to pay as damages "because of" or "for" "bodily injury," and (c) whether a products exclusion excludes coverage. Although indemnity issues have yet to be litigated, a number of complex issues are likely to arise in that context as well.

Occurrence. In certain cases, insurers have denied a duty to defend on the ground that the underlying opioid complaint did not contain allegations sufficient to qualify as an "occurrence." More specifically, the insurers argued that the underlying complaint contained allegations that the defendants engaged in intentional conduct for profit, which does not qualify as accidental conduct sufficient to constitute an "occurrence" under a general liability insurance policy.

This argument has faced mixed results in the courts. One set of declaratory judgment cases arose from an underlying lawsuit brought by the state of West Virginia against various prescription opioid distributors (the "West Virginia State Court Action"). Three federal courts—applying South Carolina, Kentucky, and Illinois law, respectively—concluded that certain allegations in the underlying complaint sounded in negligence, including allegations that the defendants failed to implement sufficient controls to identify suspicious prescription drug orders. These courts ruled that the complaints' allegations were sufficient to qualify as an "occurrence" for duty-to-defend purposes.[3]

In contrast, the Court of Appeals of California rejected a pharmaceutical manufacturer's claim for coverage in connection with underlying cases brought by several California counties (the "California Action") and the city of Chicago (the "Chicago Action") alleging deceptive marketing and sales practices.[4] The court held that the allegations in the California and Chicago Actions did not constitute an "accident" or "occurrence" under California law, because the policyholder was accused of a deliberate course of conduct designed to increase sales of its opioids by intentionally misleading doctors and the public. The court emphasized that under California law, the fact that a policyholder engaged in allegedly intentional misconduct that resulted in unintended consequences—such as opioid or heroin abuse—does not transform the alleged misconduct into an "accident" giving rise to a duty to defend.

Bodily injury. In certain cases, insurers have denied coverage for underlying opioid lawsuits on the ground that the underlying complaints did not allege covered damages "because of" or "for" "bodily injury" as required under a commercial general liability policy. When litigated, this coverage defense has led to mixed results.

The Seventh Circuit Court of Appeals, applying Illinois law, concluded that a duty to defend was triggered because the underlying complaint in the West Virginia State Court Action alleged damages "because of" bodily injury.[5] The court reasoned that the "because of bodily injury" language in the operative insurance policies created wider coverage than the "for bodily injury" wording sometimes used in commercial general liability policies. The court also concluded that language in the policies that provided coverage for "damages claimed by any person or organization for care . . . resulting . . . from bodily injury" supported a duty to defend, because West Virginia had alleged, at least in part, that it incurred excessive costs relating to the care of its citizens suffering opioid addiction.

In contrast, two federal district courts concluded that there was no duty to defend government entity complaints because those complaints did not allege covered bodily injury.[6] Instead, the courts concluded that the state of West Virginia sought damages only for its own economic loss, and the state did not assert claims on behalf of its individual citizens for the physical harm they personally sustained.

Products exclusion. In certain cases, insurers have denied coverage related to underlying opioid lawsuits on the ground that a products exclusion contained in the policy barred coverage for "bodily injury" either "arising out of" or "resulting from" products manufactured, sold, handled, or distributed by the policyholder. When litigated, this coverage defense has fared well. The U.S. Court of Appeals for the Eleventh Circuit and the Court of Appeals of

OPIOID INSURANCE LITIGATION

California have both relied on a products exclusion to conclude that insurers have no duty to defend opioid lawsuits against pharmaceutical policyholders.[7] The courts concluded, in sum, that because "bodily injury" (if any) related to opioid addiction "arises out of" opioid products, the products exclusions were triggered.

Indemnity issues. The opioid coverage cases litigated to date principally have focused on the duty to defend, where courts have been asked to determine whether the underlying complaints allege a *possibility* of coverage, not whether coverage actually exists. For example, the Seventh Circuit, in *H.D. Smith*, held that it was possible that the complaint in the West Virginia State Court Action sought damages "because of bodily injury" due to allegations that the state provided certain types of care to its addicted citizens. The West Virginia complaint actually sought a variety of different types of economic losses, including the costs attendant to (a) building additional prisons, (b) hiring more police officers and judges, (c) providing opioid-related education, (d) paying for opioid prescriptions (which the state had to reimburse under its workers' compensation program), and (e) treating addicted citizens.

Even assuming, as the Seventh Circuit did, that the last category of damages could potentially qualify as "bodily injury" damages for purposes of triggering a duty to defend, some or all of the other categories likely do not. How are indemnity dollars, particularly in the context of a settlement, going to be allocated to each of those categories? With respect to indemnity dollars that are allocated to the treatment of individual citizens, can the policyholder or the government entities identify when each citizen suffered "bodily injury" and when costs were incurred in treating that citizen, for purposes of determining which policy or policies were triggered? What trigger of coverage will apply? These are just some of the issues that will have to be addressed if and when insurers are asked to pay indemnity costs.

Potential Reinsurance Coverage Issues

Follow the fortunes/settlements. A threshold issue that likely will undergird many future reinsurance disputes is the "follow the fortunes/settlements" concept ("follow"), under which the

cedent is afforded substantial, but not unfettered, discretion in settling coverage disputes. Due to the fact that indemnity issues largely have been unexplored in opioid litigation, that discretion may prove particularly helpful to cedents.

Deciding whether and how to apply the "follow" concept in the context of an opioid settlement and allocation is largely a two-step process. First, does the dispute involve a coverage decision under the cedent's own policies (to which "follow" typically applies) or application of the language of the governing reinsurance contracts (to which "follow" typically does not apply)? Second, if "follow" applies, was the cedent's decision grossly negligent, reckless, made in bad faith (the cedent's preferred formulation) or unreasonable (the reinsurer's preferred formulation)?

Opioid litigation is in its nascent stages, and as a result, many of the liability, coverage, and reinsurance issues have yet to play out.

By way of example, in the West Virginia State Court Action, the state sought more than $2 billion in damages from the distributors but settled (according to publicly disclosed reports) with individual defendants for much smaller dollar figures, ranging from less than $1 million to $20 million. According to public filings, at least some of the distributors are seeking to recover all or substantial portions of the settlement amount from their carriers, as well as defense costs incurred in the underlying litigation.[8] If an insurer ultimately settles with a distributor-policyholder, that insurer will be left to allocate the settlement dollars to different claims, years, and policies, in a context where both the underlying facts and the case law are underdeveloped. In that situation, cedents likely will attempt to rely heavily on the "follow" concept to insulate their settlement. How far that deference extends may be the subject of litigation/arbitration.

Allocation. One situation where the "follow" concept likely will come into play is in a cedent's allocation of opioid losses among potentially triggered policies and claims. Opioid losses can resemble traditional long-tail claims (such as asbestos) in certain respects, because the government plaintiffs allege wrongful conduct and injury that took place over the course of several decades. Yet there are also material differences between opioid claims and traditional long-tail claims, in that people know or should know that they are addicted to opioids soon after such addiction takes place, and governments should know that they have suffered a loss related to opioids as soon as they make a payment in connection with an addicted citizen. Courts have yet to explore trigger and allocation issues in the context of opioid claims, and it is unclear whether they will borrow more from long-tail claims or from more typical exposures in analyzing these losses.

A certain amount of uncertainty may also come into play in analyzing allocation and trigger issues from a factual standpoint. The underlying complaints provide little guidance on these issues, because they are typically vague concerning the timing of each specific defendant's allegedly wrongful conduct and the timing and nature of each underlying injury. In addition, it is unclear how much the factual record will be developed in the underlying lawsuits, most of which are in their early stages. To date, the government entity plaintiffs have focused on identifying large potential damages figures in a variety of broad categories, without assigning dollar figures or exposure periods to allegedly injured citizens. It is possible, and in fact likely, that some or all of the government entities may not have good records of precisely when they provided services to individual citizens.

Thus, the potential exists—as appears to have happened in the West Virginia State Court Action—that lump sum settlements will be reached without attributing settlement dollars to particular injuries. In addition, early indications are that policyholders may seek to resist or significantly limit discovery into the nature of their settlements in disputes with their insurers. If those efforts are successful (and they should not be), insurers may be faced with having to make payments via settlement or judgment while lacking significant detail concerning the nature of the underlying exposures.

Such uncertainty often leads to disputes with reinsurers. Reinsurers will want to investigate (1) whether cedents' allocations took into consideration when the policyholder manufactured or distributed its opioid products generally, (2) when the policyholder manufactured/distributed its products in the jurisdiction that brought the suit, (3) when individual citizens were injured, (4) when the government entity actually paid losses in connection with those injuries, and (5) what the governing trigger of coverage for the underlying policies is. Cedents will argue that, under the "follow" concept, reinsurers are not entitled to second-guess their decisions, especially if they were forced to make payments without that same information. These are precisely the circumstances that have led to reinsurance disputes in other contexts.

Aggregation. Opioid claims also may result in reinsurance aggregation disputes when cedents bundle loss and expense in their presentations. Depending on the nature of the applicable reinsurance contracts, cedents will attempt to aggregate losses arising within one policy year, losses arising from multiple policy years, or losses of multiple policyholders in one year or multiple years. If the governing reinsurance contacts and insurance policies contain the same or substantially similar contract language, cedents will argue that "follow" should govern these issues. If the wording in the insurance and reinsurance contracts is materially different, reinsurers will argue that the aggregation wording of the reinsurance contracts should govern.

For example, some reinsurance contracts define "loss occurrence" to include all losses arising from the same "event," which is typically viewed as a relatively narrow basis for aggregating losses. Other reinsurance contracts define "loss occurrence" to include all losses arising from the same "cause," which is generally considered to provide a broader basis on which to aggregate. Either way, disputes may result. For example, did a separate "event" or "cause" occur each time a pharmaceutical company downplayed the addictiveness of opioids, or is the manufacturer's conduct part of an overarching scheme that should be viewed as a single "event" or "cause"? In the context of distributor claims, is the "event" or "cause" the distribution of opioids generally, the distribution of a specific lot of opioids, or the use of opioids by each individual end user? The answer to these questions could be the difference between a substantial reinsurance recovery or none at all.

Defense without indemnity. In response to opioid claims, some insurers may pay a high percentage of their overall liability in defense costs; in some cases, insurers may pay all defense and no indemnity. These situations may lead to reinsurance disputes, especially under reinsurance contracts that require reinsurers to pay expenses in the same proportion that they pay the cedent's losses. In similar circumstances involving different types of pharmaceutical losses, some reinsurers have taken the position that if the cedent pays no indemnity, the reinsurer is not required to reimburse the cedent for any portion of its expenses. We have been unable to identify any reported decision in which these issues have been resolved.

Opioid litigation is in its nascent stages, and as a result, many of the liability, coverage, and reinsurance issues have yet to play out. Given the massive amount of dollars at risk, however, insurers and reinsurers should develop and implement a coordinated strategy for addressing these claims now.

1. The U.S. Department of Health and Human Services estimates that total economic costs from all opioid abuse in the U.S. in 2016 exceeded $500 billion. See "The Opioid Epidemic by the Numbers" at "About the Epidemic: The U.S. Opioid Epidemic," a web page hosted by the U.S. Department of Health and Human Services (citing *Mortality in the United States*, 2016 NCHS Data Brief No. 293, Dec. 2017).
2. See, e.g., *State of West Virginia ex rel. Darrell V. McGraw Jr. v. AmerisourceBergen Drug Corp., et al.*, No. 12-C-141 (W.Va. Cir. Ct., Boone County); *The People of the State of California, acting by and through Santa Clara County Counsel Orry P. Korb and Orange County District Attorney Tony Rackauckas v. Purdue Pharma L.P. et al.*, (Cal. Super. Ct. Orange County, 2014, No. 30-2014-00725287); *City of Chicago vs. Purdue Pharma L.P. et al.*, No. 14-cv-04361 (N.D. Ill.).
3. See *Liberty Mutual Insurance Co. v. J M Smith Corp.*, 602 F. App'x 115 (4th Cir. 2015); *Cincinnati Insurance Co. v. Richie Enterprises LLC*, 2014 U.S. Dist. LEXIS 27306 (W.D. Ken. March 4, 2014) (Richie I); *Cincinnati Insurance Co. v. H.D. Smith Wholesale Drug Co.*, 2015 U.S. Dist. LEXIS 100823 (C.D. Ill. Aug. 3, 2015).
4. See *Traveler's Property Casualty Co. of America v. Actavis, Inc.*, 2017 Cal. App. LEXIS 976, G053749 (Cal. Ct. App. Nov. 6, 2017). The authors of this article were counsel for Travelers in this appeal and the underlying action in California Superior Court.
5. *Cincinnati Insurance Co. v. H.D. Smith, LLC*, 2016 U.S. App. LEXIS 13175 (7th Cir. July 19, 2016).
6. *Travelers Property Casualty Co. of America v. Anda, Inc.*, 2015 U.S. Dist. LEXIS 31450 (S.D. Fla. Mar. 9, 2015) (applying California law) affirmed on other grounds 2016 U.S. App. LEXIS 15760 (11th Cir. Aug. 26, 2016); *Cincinnati Insurance Co. v. Richie Enterprises LLC*, 2014 U.S. Dist. LEXIS 96510, at *15 (W.D. Ken. July 16, 2014) (applying Kentucky law). The authors of this article were counsel for Travelers in the *Travelers v. Anda* case.
7. *Travelers Property Casualty Co. of America v. Anda, Inc.*, 2016 U.S. App. LEXIS 15760 (11th Cir. Aug. 26, 2016); *Traveler's Property Casualty Co. of America v. Actavis, Inc.*, 2017 Cal. App. LEXIS 976, G053749 (Cal. Ct. App. Nov. 6, 2017).
8. See *AmerisourceBergen Drug Corp. v. ACE American Insurance Co. et al.*, Case No. 17-C-36 (Cir. Ct. of Boone County, West Virginia).

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Reinsurance Limits and Scope of Arbitration

Since March 2006, in a section of the ARIAS•U.S. website titled "Law Committee Reports," the Law Committee has been publishing summaries of recent U.S. cases addressing arbitration- and reinsurance-related issues. Individual ARIAS•U.S. members are also invited to submit summaries of cases. Legislation, statutes, or regulations for potential publication by the committee. The committee encourages members to review the existing summaries and to routinely peruse this section for new additions.

Global Reinsurance Corp. of America v. Century Indemnity Co., 2017 WL 6374281, No. CTQ-2016, 005, (N.Y. Dec. 14, 2017)

Court: New York Court of Appeals

Date Decided: December 14, 2017

Issues Discussed: Reinsurance limits and defense costs

Issues Decided: Whether a liability limit in a facultative certificate caps a reinsurer's liability for both indemnity and expenses.

Submitted by: Ann E. Halden, special counsel at Mound Cotton Wollan & Greengrass LLP.

A reinsurer sought a declaration that the "Reinsurance Accepted" clause of its facultative certificates capped all obligations, including defense costs, at the limits provided. In considering the matter, the Second Circuit U.S. Court of Appeals certified a question to the New York Court of Appeals, asking whether the Court of Appeals' decision in *Excess Insurance Co. v. Factory Mutual Insurance Co.*, 3 N.Y.3d 577 (2004) imposes "either a rule of construction, or a strong presumption, that a per-occurrence liability cap in a reinsurance contract limits the total reinsurance available under the contract to the amount of the cap regardless of whether the underlying policy is understood to cover expenses such as, for instance, defense costs." The Second Circuit noted that if *Excess* did not provide a clear rule, it would then apply the "standard rules of contract interpretation."

On December 14, 2017, the New York Court of Appeals held that "[u]nder New York law generally, and in *Excess* in particular, there is neither a rule of construction nor a presumption that a per-occurrence liability limitation in a reinsurance contract caps all obligations of the reinsurer, such as payments made to reimburse the reinsured's defense costs." In reaching this conclusion, the Court of Appeals explained that its decision in *Excess* addressed whether a reinsurer's obligation to pay loss adjustment expenses was subject to the stated indemnification limit in the reinsurance policy. The court noted that given its review of the contract at issue in *Excess*, it concluded that the limit clause imposed an expense-inclusive cap on the reinsurer's liability. The court noted that while its decision in *Excess* did not rule that third-party defense costs are capped by the limits in a facultative certificate, various courts had interpreted the decision that way.

Thus, the court sought to clarify its decision, noting that, contrary to interpretations of its decision by other courts, the court in *Excess* did not consider third-party defense costs nor consider whether there was a "presumption" or "rule of construction" that the limitation of liability clause applied to all payments by a reinsurer. The court further distinguished the loss adjustment expenses at issue in *Excess*, which the reinsurer incurred in litigation between the insurer and its policyholder, from the third-party defense costs at issue in the matter before the Second Circuit, which it noted were costs that an insurer may be obligated to pay under the terms of the insurance policy.

Thus, the court stated that its decision in *Excess* did not address the issue before the Second Circuit and that "*Excess* did not supersede the 'standard rules of contract interpretation' . . . otherwise applicable to facultative reinsurance contracts."

Galilea, LLC v. AGCS Marine Insurance Co., No. 16-35474, 2018 WL 414108 (9th Cir. Jan. 16, 2018)

Court: United States Court of Appeals, Ninth Circuit

Date Decided: January 16, 2018

Issue Discussed: Arbitrability and scope of arbitration

Issue Decided: Whether the enforceability and scope of an arbitration provision in a maritime insurance policy is (1) governed by the FAA, notwithstanding state law to the contrary and the application of the McCarran-Ferguson Act, and (2) decided by a court or an arbitrator.

Submitted by: Aluyah I. Imoisili, partner, and H. Josh Ji, associate, at Greenberg Gross LLP.

Galilea, LLC applied for an insurance policy for a yacht it owned. In its application, Galilea agreed that the parties would settle disputes arising out of "the parties' relationship" through AAA arbitration and that New York law would govern. The insurance policy that AGCS Marine Insurance Company ultimately underwrote differed from the application in that it provided that the parties would settle disputes arising "under this policy" through AAA arbitration and that federal maritime law would govern.

When Galilea submitted a claim to AGCS after the yacht crashed in Panama, AGCS denied coverage and commenced AAA arbitration when Galilea sought reconsideration of the coverage denial. Galilea filed counterclaims in the arbitration based on alleged misrepresentations made by AGCS's broker during the application process. Subsequently, Galilea brought mostly the same counterclaims in an action in Montana federal court and sought to stay the arbitration while its court claims were pending.

The district court held that, notwithstanding Montana law that precluded arbitration in consumer contracts, the Federal Arbitration Act required enforcement of the arbitration provision in the insurance policy and that the court was the proper arbiter of the enforceability and scope of the arbitration provision. The district court then determined that only two of Galilea's counterclaims were subject to arbitration.

The Ninth Circuit agreed with the district court that the FAA governed the enforceability of the parties' arbitration provision. Notably, the Ninth Circuit rejected Galilea's argument that Montana law should prevail due to the application of the McCarran-Ferguson Act, which exempts state insurance laws from federal pre-emption. The Ninth Circuit explained that because the FAA governs the enforcement of arbitration provisions in maritime contracts, the FAA applied to maritime insurance policies and pre-empted state law.

With respect to the scope of the arbitration provision, however, the Ninth Circuit demurred, reasoning that a court could not decide the issue of arbitrability because, under the relevant AAA rules that the parties agreed to, the scope of arbitration is within the arbitrator's exclusive jurisdiction. Thus, the Ninth Circuit affirmed in part, and reversed in part, the district court's ruling: although McCarran-Ferguson does not insulate state insurance law from federal pre-emption with respect to the FAA, governing arbitration rules that require an arbitrator to determine the scope of an arbitration provision divest such jurisdiction from courts.

The Ninth Circuit rejected Galilea's argument that Montana law should prevail due to the application of the McCarran-Ferguson Act, which exempts state insurance laws from federal pre-emption.

Attention history buffs and trivia seekers!

Did you know that The Breakers Palm Beach was first named The Palm Beach Inn? Opened in 1896 by oil/real estate/railroad tycoon Henry Flagler to accommodate travelers on his Florida East Coast Railway, this historic hotel occupies the beachfront portion of the grounds of the Royal Poinciana Hotel, which Flagler had opened beside Lake Worth Lagoon in 1894, facing the inland waterway. Guests began requesting rooms "over by the breakers," so Flagler renamed it The Breakers Hotel in 1901.

Fires destroyed the hotel in 1903 and 1925; each time, it was rebuilt. After its reopening in December 1926, the resort hosted the "who's who" of early 20th-century America, including the Rockefellers, Vanderbilts, Astors, Andrew Carnegie, and J.P. Morgan. The names of today's illustrious guests are kept under wraps to ensure privacy, although I have spotted Luke Wilson and Drew Barrymore during ARIAS conferences over the years, and Sofia Vergara and Joe Manganiello were married at the hotel in 2015!

During World War II, the War Department took over The Breakers (as it did many other large facilities in the United States), using it as the U.S. Army's Ream General Hospital, complete with maternity ward. More than a dozen babies were born during this time at The Breakers; some of these "Breakers Babies" have even returned to visit the resort where they were born. Maybe we have a few "Breakers Babies" in the ARIAS crowd!

After the war, The Breakers was restored and reopened as a hotel. Today, $30 million is reinvested annually into the resort, which is still owned and operated by Flagler's descendants. The resort's grounds encompass 140 acres along the Atlantic Ocean and include four pools, two 18-hole golf courses (including the Ocean Course, created in 1896 by Alexander H. Findley, making it Florida's oldest golf course), a new indoor/outdoor fitness center, a new 20,000-square-foot spa, poolside bungalows, family and children's activities, a shopping arcade, and nine restaurants in which to dine.

The Breakers' compelling history and gorgeous landscaped grounds are inviting in their own right; as backdrops for our 2018 Spring Conference, they create a welcoming environment for you to learn from our lineup of expert speakers, network with colleagues, and enhance your career profile. Whatever entices you, we hope you plan to join us in Florida from May 9-11. Arrive earlier or stay longer—either way, the hotel will honor the fabulous ARIAS room rate for all of our guests.

See you in West Palm!

—Sara Meier

Members on the Move

John Nonna recently left his partnership at Squire Patton Boggs to enter public service, accepting an invitation to serve as county attorney of Westchester County (New York). In his new role, he will serve as the legal advisor to the county executive, county legislature, and county departments and lead a department of 50 lawyers that handles litigation for and against the county as well as county contracts and legislative issues. Nonna is not new to public service—he is a former county legislator and served as mayor of Pleasantville, New York, from 1995-2003. He is also a past member and chair of the Westchester Community College Board of Trustees and a former co-chair of the board of directors of the Lawyer's Committee for Civil Rights Under Law.

Deirdre Johnson and **Paul Kalish** recently joined Squire Patton Boggs LLP as partners on the litigation team in the firm's Washington, D.C., office. Johnson has nearly two decades of experience handling disputes in the U.S., Bermuda, London, and European markets in lawsuits and arbitration proceedings arising out of a broad range of claims and virtually all types of insurance and reinsurance agreements. Kalish has represented members of the insurance industry for more than 30 years and, since 2000, has served as counsel for the Coalition for Litigation Justice, Inc., a group formed by insurers to address abuses and inequities in the current mass tort litigation environment.

Clyde & Co. is expanding its presence in the United States, hiring 15 insurance and litigation partners from Sedgewick LLP, a California law firm. The new partners are insurance coverage, trial, and litigation lawyers and represent U.S. and international insurance carriers and corporate and public-sector bodies. They will be based in San Francisco, Los Angeles, Chicago, New York, Miami, and Orange County (Calif.).

Newly Certified Arbitrators

David Bradford is a vice president and senior assistant general counsel with the Zurich Insurance Group, where he provides counseling, regulatory, and contract wording advice in connection with complex reinsurance transactions concerning North American business. In addition, he manages all reinsurance arbitrations and litigation concerning the Zurich North America underwriting companies. Prior to joining Zurich, he practiced at the Chicago office of Lord, Bissell & Brook, where he concentrated his practice on the litigation and arbitration of disputes of interest to reinsurers. His practice included the representation of reinsurers in disputes involving a broad range of contracts including general liability, property/casualty and surety reinsurance agreements.

Michael Goldstein has been practicing insurance law since 1980 and reinsurance law since 1985 at Mound Cotton, where he worked closely with the late Gene Wollan in multiple arbitration hearings and then collaborated for over 20 years with Larry Greengrass as co-first chair at many hearings. He has been first chair/co-first chair in 50-plus arbitration hearings to award and has argued multiple appeals in the federal circuit courts of appeal. He has represented both cedants and reinsurers and has made law in many landmark decisions in the federal and state appellate courts. He also has obtained several recent significant discovery rulings in the federal courts concerning reinsurers' rights of access to cedants' claim files and cedants' reserving history. He also has authored multiple articles in insurance and reinsurance journals and has lectured on many insurance and reinsurance topics over the last 25 years.

Lawrence S. Greengrass, a former officer of Emerald Coast Reinsurance Co. Ltd., has 41-plus years of experience at Mound Cotton Wollan & Greengrass. During his years with the firm, he has litigated insurance and reinsurance disputes in state and federal courts and has acted as lead counsel in more than 150 arbitrations in the United States and abroad. His practice has encompassed a wide range of topics involving property/casualty, life/accident, health, and financial reinsurance; he has also been actively involved in the preparation of contract wordings. He has participated in various capacities in ARIAS and has presented at many industry conferences on numerous reinsurance topics, including asbestos, pollution, allocation, insolvency, catastrophe losses, reinsurance underwriting and claims handling, and reinsurance arbitrations.

Online membership application is available with a credit card through "Membership" at www.arias-us.org.

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Insurance/Reinsurance Companies (1 - 15)	$1,850
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SIGNATURE

AGREEMENT

By signing below, I agree that I have read the ARIAS•U.S. Code of Conduct and the Bylaws of ARIAS•U.S. and agree to abide and be bound by the *ARIAS•U.S. Code of Conduct* and the By-Laws of ARIAS•U.S. The Bylaws are available at www.arias-us.org under the "About ARIAS" menu. *The Code of Conduct* is available under the "Resources" menu.

SIGNATURE OF INDIVIDUAL
OR CORPORATE MEMBER APPLICANT

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BOARD OF DIRECTORS