

**HOW REINSURANCE ARBITRATIONS CAN BE
FASTER, CHEAPER AND BETTER (REVISED)**

By

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I. Introduction

This is an update of an article which first appeared in 2004¹ and was intended as an action plan for remedying some of the more significant problems with the reinsurance arbitration process. Unfortunately, this action plan has not progressed very far since then.

One of the reasons for this is identified in an article authored by noted commenter, Larry Schiffer, which is entitled, significantly, "Mirror, Mirror on the Wall."² In this article, he suggests that the problems may be less with the arbitration system itself but more with participants who find advantage in gaming the system.

In my opinion, this advantage may be a severe attenuation of the process by a party that is reluctant to pay or which hopes to find a reason not to pay in scorched earth discovery. This advantage may be to the law firm whose stock in trade is to make every dispute, regardless of importance or the merits, into an ordeal similar to crawling through broken glass for 20 miles on hands and knees. This advantage may be to the arbitrator who no longer wants to work hard, make difficult decisions or articulate them in writing to those paying the bills.

As Mr. Schiffer observes in his article, the three constituent parts of the arbitration process need to work together to improve, and reduce gaming of, the arbitration process. Remedies in several critical areas are suggested below.

II. Discovery Standards in Arbitrations

A major problem in arbitrations is discovery. While most counsel are responsible in terms of discovery, arbitration panels sometimes field requests for massive deposition and document discovery, some of which is not well targeted or would produce information largely tangential to a resolution of the dispute on the merits. Not only is this burdensome, costly and time consuming, it may be functionally impossible to execute (due in part to limitations on subpoena power) or when the discovery is sought from disbanded or disaffected third parties such as

agents. When a party is unable to convince an agent third party to cooperate, that party may be accused of playing hide the ball.

One of the hurdles with placing reasonable boundaries on discovery is acquiescence by panels in the views of counsel as to standards for discovery. The Federal Rules of Civil Procedures allow discovery of documents which may lead to admissible evidence. Since there is no standard for admissible evidence in arbitrations, this rule is not very meaningful in the arbitration context. Moreover, very broad discovery is less necessary for arbitrations than litigation since: (a) arbitration is supposed to be faster and less costly than litigation; (b) arbitrators are expert in the business and require less detail than a court to understand the transaction at issue and what went wrong; and (c) arbitration panels are familiar with the business records of insurance and reinsurance entities and can focus discovery on those locations most likely to contain probative evidence. “The test is whether the parties have had a fair opportunity within the context of due process to present their case.”³

In this light, perhaps arbitration panels should adopt a standard for discovery more appropriate for arbitrations: that which is likely to produce evidence probative to the issues in dispute. This would reduce high volume - low result discovery and the time and cost related to thereto and provide the panel with the information most useful to resolve the dispute which has caused non-performance.

III. Panel Involvement in Shaping Issues

In the typical arbitration, the parties define the issues to be placed in front of the panel. Often, the panel first becomes involved in shaping issues when discovery disputes arise. However, such involvement usually deals with the connection between the discovery desired with and a line of inquiry thought to be significant by counsel. The panel sometimes makes little effort during the discovery phase to connect the line of inquiry with the issues identified in the dispute.

Viewed historically, this passivity is understandable. Arbitration is the creature of the contract between the parties. The authority of the panel is limited to that granted in the arbitration clause. In addition, the partisan aspects of the party arbitrator process make it difficult to force counsel into an early definition of the issues. (*See* § VII on all-neutral panels.) However, a relatively passive role for the panel has significant disadvantages in large, complicated and hotly contested arbitrations. Counsel may have very different views of the case leading to a failure to meet squarely on the issues. This can lead to inefficient efforts of counsel and, occasionally, a tragic failure to grasp the panel’s priorities and inclinations. This, in turn, can lead to a lopsided result on a matter that could have been settled with more panel intervention.

While it may be hard for the panel, and painful to counsel, the speed and efficiency of the arbitration process may benefit from more panel involvement in shaping and prioritizing the issues in the dispute. This can start at the organizational meeting with counsel being required to reveal the substantive reasons for non-performance on either side. It can continue with a discovery plan that is tied to specific issues plus a conference call prior to filing the briefs to further define the issues. Finally, there should be a conference call after the briefs but before the

hearing so as to prioritize testimony to the issues most important to the panel and most in controversy. This would serve to better focus and shorten the hearing.

IV. Saving Time and Money Prior to the Hearing

There are a number of factors which influence the scheduling of an arbitration hearing. Many players must be available: counsel, arbitrators, witnesses and company representatives. They must be available for a block of time (one or more weeks for the hearing and a week before for preparation). Discovery must be completed (eight or more months) and briefs written and issued (one month). Therefore, twelve months is often the minimum lead time necessary to schedule a hearing.

Sometimes counsel believe that more lead time is necessary. This can result from their schedules or their view of necessary discovery i.e. audits can be cumbersome to arrange and time consuming. It can also result from intervening motion practice *i.e.* security, dispositive motions and discovery disputes. Some parties and their counsel are in no hurry to bring a dispute to resolution.

Slippage in the schedule prior to the hearing can have a disastrous result. If the hearing has to be rescheduled, this may add many months to the duration of the arbitration due to the necessity of juggling the schedules of all the relevant parties. Therefore, it is incumbent on the relevant players to achieve interim steps within the designed time periods. This can be done in several ways:

- Arbitrators need to identify issues of relationships with relevant parties prior to the organizational meeting so as to resolve them without disrupting the proceeding at a later time
- Telephonic organizational meetings to avoid the scheduling conundrum at the front end
- Counsel have to identify with some particularity the reason for non-performance early on so as to focus discovery e.g. general statements of misrepresentation, concealment and breach of contract are not useful
- Firm dates for the interim discovery and briefing must be established at the organizational meeting with consequences for failure to meet them without good cause
- Periodic status reports from counsel to detect slippage in the schedule and identify emerging problems
- Meet and confer requirements for counsel before bringing disputes to the panel in order to avoid piecemeal and confusing presentations of such disputes to the panel
- Deciding interim issues on written submissions and/or argument by conference call to reduce scheduling problems
- Dealing with dispositive issues first (*see Section V., infra.*)

One the best ways in which pre-hearing delays can be avoided is for parties to be very involved in the discovery requested by counsel in order to focus on important witnesses and documents and to be efficient in the way that information is sought. Parties know how to focus requests to get maximum result from modest amounts of information. For instance, if the issue is the reason for entering and exiting a line of business, focusing on the business plans for the years in question will reveal more concise and useful information than a vague request for all documents

related to a company's involvement in a line of business (every piece of paper and electronic file?).

V. Saving Time and Money at the Hearing

Hearings are very expensive. Teams of lawyers and arbitrators are billing by the hour. Executives are taken away from other duties to testify. Hotels charge considerable amounts to provide space, room, board and equipment for the event.⁴ To the extent that a hearing cannot be completed within the time allowed, more expenses are incurred. Therefore, a reduction in hearing time is directly responsive to common criticisms of reinsurance arbitrations.

Sometimes, on the opening day of a hearing, the panel is faced with a number of motions and arguments over use of hearing time, or other matters, that seriously delay the taking of testimony putting the arbitration behind schedule from the outset. These issues are best addressed by means of a conference call after the final briefs are submitted and before the hearing starts. This allows the panel to resolve these issues with some time for reflection and without a courtroom full of lawyers, witnesses and company representative waiting for testimony to start.

In some disputes, there are threshold issues which might be decided on a summary basis in that they have no or few disputed facts.⁵ For instance, a common defense of reinsurers is that the cedent misrepresented the program on placement so as to justify rescission and administered the program so poorly as to violate the duty of utmost good faith. The placement defense involves limited players and documents and if successful, will obviate the rest of the hearing. The administration defense involves many players, many transactions and time-consuming audits. Panels and counsel should consider bifurcating such a dispute to focus on the placement issue first and to allow the administration issue to follow on at its naturally slower pace. If the cedent is found to have misrepresented the business in material fashion, discovery on administration can stop and a time-consuming hearing thereon is avoided. If no material misrepresentation is found, the dispute is in a better posture for settlement.

Another means by which hearing time can be saved is for the panel, after it has reviewed the briefs, to give counsel direction as to the issues and witnesses of most interest to the panel. Counsel are often grateful for this because it helps them prioritize their efforts and decide which witnesses are needed for live testimony. While panel consensus on point may be difficult to achieve absent an all-neutral panel (*see* Section VII., *infra.*), it is a worthwhile tactic in an effort to achieve an efficient and focused hearing.

For major witnesses at the hearing, considerable time can be saved by the use of British-style direct testimony i.e. written statements submitted to the panel prior to the hearing. Cross and re-direct is handled live. In this fashion, direct testimony is more organized and concise and does not take up hearing time. The panel has already absorbed the written testimony and opposing counsel are better prepared for cross.

For minor witnesses, deposition designations, rather than live testimony, can save considerable hearing time. They can be prepared by counsel and read offline by the panel. This may require

somewhat more complete depositions of minor witnesses by both sides as would ordinarily be the case. However, it saves hearing time where the aggregate costs are much higher.

Technology has added a new dimension to the arbitration process; however, technology can add costs without real benefit. Written deposition designations can obviate segments of videotaped depositions of minor witnesses. Demeanor evidence, which the primary benefit of videotaped depositions, is seldom a significant factor. The businessmen and businesswomen who are the subject of the depositions are used to presenting themselves well so the benefit of viewing them as they give their testimony is often marginal. The panel can read the testimony much faster than it can be given on videotape and they can read it offline, thus saving considerable hearing time.

Certain technology is very helpful to the panel to the panel before, during and after the hearing. Briefs, exhibits and attachments provided electronically allow the panel to be productive even while traveling. LiveNotes or similar technology provides the panel a live feed to testimony as it is given. This helps the panel to absorb it better and to annotate it so that the panel can more easily find it later and use it in their deliberations.

VI. Awarding Costs in Reinsurance Arbitrations

Absent a contractual provision to the contrary, it is clear that an arbitration panel can award costs (e.g. attorneys' fees and other costs of the arbitration) to the prevailing party.⁶ Until recently, there has been considerable reluctance on the part of arbitration panels to do so.

This reluctance may have several sources. One may be the American rule in litigation that each party must pay its own costs, absent extraordinary circumstances. The American rule is in contrast to the rule in other jurisdictions (*e.g.* England) where costs are granted routinely to the prevailing party as a means of deterring marginal litigation.

Traditionally, reinsurance arbitrations were largely good faith disputes between business partners which could be resolved relatively quickly and cheaply with the aid of some market practitioners. There were few costs to award and the dispute was something the parties wished to put behind them so they could continue trading. This is no longer the case.

Finally, the party arbitrator system creates a certain degree of partisanship which may deter a panel from awarding costs even when deserved. While a panel, or a majority thereof, may be willing to rule on all issues for one party, they know that awarding costs may subject the losing party arbitrator to the considerable disappointment of the party and its counsel who may believe that their arbitrator has failed in his or her partisan responsibility.

Obviously, the arbitration process has changed in recent years. It is no longer a low cost, expeditious resolution of good faith disputes between trading partners. All too often, it has become a scorched-earth proceeding involving parties in runoff or with discontinued operations and with no interest in a future trading relationship.

With a low probability of costs being awarded, there is little disincentive to taking novel if not outrageous positions. Sometimes arbitrators encounter highly skilled advocates making earnest

arguments in favor of the most unlikely positions in support of totally unacceptable behavior by their clients. Fortunately, a growing number of panels are willing to grant costs under such circumstances. This trend would accelerate with a move to all-neutral panels which will eliminate partisanship in arbitration proceedings. It has become evident that granting costs in appropriate circumstances is a tool that must be wielded to combat legitimate criticisms concerning the length and costliness of the arbitration process.

VII. All-Neutral Panels

Reinsurance arbitrations in the United States traditionally have used two arbitrators appointed by the parties and a neutral umpire. To most, the role of the party arbitrator is to make sure his or her party's position is articulated and fully considered by the panel and then to seek a just result. To a minority, the role of the party arbitrator is simply to advocate the position of the party. Others have a view of their role somewhere in between.

Regardless of where party arbitrators fall within this spectrum, their role is difficult and conflicted. Only with a struggle can a party arbitrator put behind him or her the appointment process, discussions with counsel prior to the termination of ex parte communications and the effort to assure balance to the proceeding. The result often is a partisan element to the proceeding which can impact virtually all phases: (1) umpire selection; (2) timing of the hearing; (3) scope and nature of discovery; (4) length and focus of the hearing; (5) the nature of panel deliberations; and (6) the nature and clarity of panel rulings.⁷

The impact of this partisan element takes several forms. Debate within the panel is elongated to little purpose. Negotiations tend to be distributive in nature *i.e.* working toward the middle from outer parameters determined by the positions of the parties. Unfortunately, this tends to reward the party which takes the most extreme position and tends not to consider that the proper answer may be within entirely different parameters. Hearings may be longer than necessary to assure that each counsel can present their arguments in full, regardless of whether the panel finds all of such arguments useful. The reasoning behind the panel's ruling on the merits may be mushy and poorly articulated. Common denominator approaches to findings and remedies are easier to cobble together than creative ones.

All-neutral panels would increase the efficiency and quality of the arbitration process significantly by eliminating the partisan element. Without party identification, arbitrators can focus on obtaining the right answer rather than positioning themselves with respect to other arbitrators. Panels can act more decisively and efficiently with less debate and face-saving compromise. The varying areas of expertise of the individual panelists can be better utilized. The panel can give more effective direction to counsel as to witnesses and the focus of issues at the hearing which can result in a better hearing in less time and with less cost. Finally, panelists are better able to produce clear and decisive answers which proceed from the evidence rather than an internal negotiation process.

Several groups have given thought to methods of selecting all-neutral panels. ARIAS•U.S. has developed a system for selecting neutral panels. In addition, the Dispute Resolution Task Force, consisting of individuals from a cross section of interested parties, has devised its own method.

While there does not seem to be a groundswell to utilize these devices, it may be too soon to evaluate their success.

VIII. Reasoned Awards

British arbitrators regularly issue rulings of 20 or more pages, notwithstanding the ability to appeal the arbitration tribunal's decision on the law pursuant to the Arbitration Act of 1996. There is no right to appeal the decision of a US arbitration panel although its ruling may be vacated on very limited grounds focused on conflict of interest and lack of due process. One might conclude that US arbitrators would be more inclined to issue "reasoned awards" as final rulings on the merits but this is not the case. Some have a sincere, if mistaken, belief that "reasoned awards" may prolong the dispute, by providing fodder for a motion to vacate, rather than conclude it.

For purposes of this discussion, I will define a "reasoned award" as 2 - 3 pages of findings of fact and conclusions of law. No more is necessary to tell parties and their counsel why they won or lost.

Reasoned awards contribute to better arbitrations for several reasons. First, composing a reasoned opinion requires clarity of thought concerning what the panel decided and why. Mushy reasoning and "split the difference" approaches to damages can seldom survive this process. Panels often render awards which do not match the reasoning or damages claimed by either party and there is absolutely nothing wrong with this. It is important, however, for the panel to have a logical reason for doing so and be able to express it in writing. This will provide better rulings by arbitration panels.

The second reason why reasoned awards produce better arbitrations is feedback to the parties and their counsel. Arbitrated disputes are becoming very large in size and considerable legal and other expenses are associated. If the parties choose to have their dispute resolved by experienced senior members of the insurance community, they have a right to know the basis upon which the panel decided. This is not merely a matter of idle curiosity. An adverse decision by a panel may cause a party to re-examine its position on similar disputes. The decision may cause the party may re-examine its decision making process when problems with clients and markets arise so as to make better evaluations as to which matters to compromise and which to pursue to an adversarial conclusion.

To lose an arbitration and not know why causes parties and their counsel to disrespect the arbitration process itself. When the process is disrespected, parties and their counsel either turn away from it or engage in some of the negative behavior cited in earlier sections. Either is detrimental to the arbitration process.

Finally, case law suggests that a court is less likely to find that a panel exceeded its authority if a motion to vacate is filed.⁸ With a reasoned award, it is easier for the court, which is unfamiliar with the business, to understand creative solutions to arcane business problems.

IX Conclusion

The reinsurance arbitration process is legitimately criticized as having become too long, costly and contentious. In part, this results from marketplace changes *i.e.* larger disputes between parties with no continuing business relationship. However the relevant players (arbitrators, parties and their counsel), must look in the mirror and accept a share of the responsibility for this situation. These players must be willing to adopt techniques to promote efficiency and clarity, such as those described above, if arbitration is to remain a viable alternative to litigation.

ENDNOTES

¹ XI ARIAS•U.S. Quarterly No. 2 at 33 (2004).

² XVII ARIAS•U.S. Quarterly No. 4 at 10 (2010) (hereinafter *Schiffer*).

³ *Schiffer* at 13.

⁴ Today, a number of court reporters have office space available for arbitrations and make such space available for free if they are used as the court reporters for the hearing.

⁵ See generally, Robert M. Hall, *Are Formal Hearings Necessary for Interim Issues in Reinsurance Arbitrations?*, TIPS Alternative Dispute Resolution Committee Newsletter, Spring 2010 at 5, also available at the author's website: robertmhall.com.

⁶ See generally Robert M. Hall, *"Inherent Authority" of Arbitration Panels to Grant Attorneys' Fees and Costs*, XVI ARIAS-US Quarterly No. 2 at 9 (2009).

⁷ See generally, Caleb Fowler, Robert M. Hall and Lawrence O. Monin, *All-Neutral Arbitration Panels*, XV Mealey's Reins. Rpt. No. 24 at 23 (2005).

⁸ See generally, Robert M. Hall, *Are "Unreasoned" Arbitration Awards "Irrational?"*, ARIAS-US Quarterly No. 4 at 7 (2009).