# THE BERMUDA FORM

## Interpretation and Dispute Resolution of Excess Liability Insurance


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# 1

# INTRODUCTION TO THE BERMUDA MARKET

**1.01** This chapter is a very brief discussion of the environment in which the 'new' Bermuda-based international insurers created in the mid-1980s, and the policy forms they chose to implement, initially took root and grew. The story of how that took place has been told at length by others.[1] The authors of this work do not propose to duplicate those efforts. By the same token, the continued development of the international Bermuda insurance market represents a much longer story, to be told by others. This chapter represents only a brief overview and context for the introduction of the Bermuda Form between 1985 and 1986.

**1.02** The founding of the new companies was in reaction to changed conditions in the market for liability coverage available to US buyers. The sea change spurring the birth and development of the Bermuda international insurance market occurred in 1984, when the US- and European-based insurance environment for large corporate commercial liability risks changed radically. Prices rose and capacity diminished for all insurance buyers, but for difficult-to-place corporate risks[2] in 1984, premium rates had tripled, and available excess limits of liability had plummeted. Many insurers had simply withdrawn from the liability arena; others had drastically reduced their exposure, still others had gone insolvent.[3]

**1.03** Many factors contributed to this situation. Long dormant, but newly emerging and massive long-tail liabilities plagued industrial America. The two best-known examples of these liabilities, asbestos and pollution, were each the result of operations commenced in the long distant past, causing toxic exposures silently developing over the intervening decades. The bill for the injuries and damage caused by these exposures began to come due for payment in the litigation explosion commencing in the late 1970s, and continuing unabated since.

**1.04** The corporate defendants ultimately held responsible[4] for compensating the multitude of injured parties not surprisingly looked to their contemporary and historic insurers for indemnity and defence, the costs of which often proved to be well in excess of the total limits of liability of their current policies. Accordingly, the corporate defendants looked to all

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[1] See, for example, Duffy *Held Captive. A History of International Insurance in Bermuda* (Oakwell Boulton, 2004); Jacobs, Masters and Stanley *Liability Insurance in International Arbitration* (Hart, 2011) Chapter 1.

[2] Chemical, pharmaceutical, and energy companies, for example.

[3] See Kim, Anderson, Amburgey and Hickman 'The Use of Event History Analysis to Examine Insurer Insolvencies' (1995) 62(1) *Journal of Risk and Insurance* 94–110.

[4] Typically, these were corporate successors responsible for long discontinued or abandoned operations.

insurers on the risk during any part of the development of these problems, from the first occasion of toxic discharge or exposure, to the time of recognition of the ensuing injuries, illnesses and damage, and including all intervening years. For the most part, in the onslaught of coverage litigation that accompanied the underlying tort litigation, policyholders found a sympathetic reception in courts in the United States.

**1.05** The most often cited example of this warm reception was the decision in *Keene Corp v. Insurance Co. of N. America*.[5] This decision, addressing coverage under occurrence-based policies responding to liabilities for asbestos-related illness, held that policies in force at any point in time beginning with claimant's first exposure, through and including the time of injury or death, were 'triggered', and responsible for the compensation for the entirety of the injury. Accordingly, a single injured worker whose exposure to asbestos began in 1940, and whose injury was recognized only in 1985, could trigger some 45 years of coverage.

**1.06** Thus, insurers using versions of the liability policy forms most commonly in use faced massive liabilities for which they were unprepared. With regard to the older, historic policies, where the insurers had long since 'closed the books' and to which no reserves were attached, the companies faced newly recognized financial exposures that could not be paired with current premium income streams. With regard to the newer policies, bearing larger limits of liability consistent with contemporary insurance, insurers now faced liabilities for the consequence of toxic exposures that commenced years or decades prior to their current policies' inception. Further, and usually in the cases of older policies, including a duty of defence, the insurers' liabilities were often not subject to any aggregate limit of liability, such that claims could be presented perpetually,[6] and the insurer's response would be limited only by any per accident, per occurrence or per person limit of liability that was stated in the policy.

**1.07** Other factors also contributed to the capacity crisis, which not coincidentally emerged on the heels of historic lows in premiums for liability coverages. This premium nadir accompanied a period of very high inflation, motivating some insurers to balance unrealistically high loss ratios against short-term, high returns on investments. The high inflation rates also, however, resulted in inflated verdicts. Other factors were at work here as well, and economists and other experts do not agree on exactly what caused the crisis, but there was no doubt about the result: massively higher premiums, and substantially reduced capacity.

**1.08** Responding to this shrinkage of capacity, but recognizing a continuing need for coverage, the insurance broker Marsh McLennan, led by Robert Clements, organized new alternative markets domiciled in Bermuda,[7] beginning with ACE Limited[8] in 1985 and XL Capital Ltd[9] in 1986. In each case, these companies were organized for the purpose of providing high-limit excess coverage for major commercial risks, regardless of industrial class, and these new companies were owned and financed by their founding insureds.

**1.09** The Bermuda insurance community in 1984 was by no means moribund, but had not yet developed into the international insurance market it is now. It served as home to a domestic

[5] 607 F 2d 1034 (DC Cir 1981).
[6] Or as long as claimants continued to emerge.
[7] But incorporated elsewhere.
[8] Then American Casualty Excess.
[9] Then EXEL Ltd.

insurer market serving the needs of its 60,000 residents, and it was the domicile of hundreds of 'captive' insurers. These insurers, typically, wholly owned subsidiaries of their typically Fortune 500 creators, were formed to serve the needs of their corporate parents, and usually only wrote policies for those companies within the corporate family of the parent. Similarly, the island spawned 'industry captives', organized for the benefit of designated industries, which shared common needs and interests. In each case, the driving force behind the formation of these entities was the perception that the commercial insurance market was not adequately serving the needs of these companies and industries, and Bermuda tax and regulatory policies created an attractive domicile for alternative ways to address these risks. Bermuda-based insurers participated in international, non-captive placements, but only to a limited degree.

**1.10** The remaining problem was designing a form to be used by the new companies that would permit them to provide the high excess coverages desired by corporate buyers, while avoiding the very problems that were visited on the historic insurers of US risks. Primarily, the goals were to avoid 'legacy' exposures such as long-term gradual pollution and asbestos, and provide increased certainty of response. That is, the new insurers, while prepared to commit large limits, required advance knowledge that those limits would be required to respond to any one occurrence only once. The Bermuda Form, designed to alleviate these problems, while filling an urgent and continuing market need, was the result.

**1.11** It is appropriate here to explain what we mean by the 'Bermuda Form'. While the policy form, introduced in 1985, has gone through numerous evolutions by those insurers routinely using the form, and has been modified and hybridized extensively by others, by 'Bermuda Form' we refer to a form that is at least generally similar to those historically issued by ACE Bermuda Insurance Ltd, and XL Insurance (Bermuda) Ltd, on their 'Occurrence Reported' forms, and which include the following characteristics:

(1) a trigger of coverage, or linkage of loss to policy period and terms that is accomplished solely via the policyholder's affirmative act of providing written notice to the insurer;
(2) a continuous policy—regardless of how long the insurer–insured relationship continues, it will generally be documented in a single, annually extended contract;
(3) a bifurcated definition of 'occurrence'—treating injuries and damage derived from products liability exposures differently from those derived from premises and other non-products exposures;
(4) integrated occurrence—a definition of 'occurrence' which permits policyholders to consider multiple instances of personal injury or property damage to be considered as falling within one occurrence (for purposes of eroding retentions and underlying insurance) where all resulted from a common cause;
(5) 'maintenance deductible', a term undefined in any policy seen by the authors, but which, in industry practice, has colloquially become known as representative of that component of loss that is not covered because not 'vastly greater in order of magnitude' than what had been previously expected or experienced;[10]
(6) an express statement of principles governing interpretation of the policy, including designation of which forum's law applies to construction of the policy;

[10] The 'maintenance deductible' feature, while included in the large majority of the Bermuda Forms, is not in all. Chartis Excess, successor to Starr Excess, does not include this feature in its version of the form.

(7) dispute resolution by means of binding, mandatory, non-US arbitration; and
(8) an absolute exclusion of 'long-tail' exposures preceding the policies.

**1.12** There are other distinguishing features, but for the most part, the remaining components of the Bermuda Form have much in common with those of contemporary US insurers. The significantly different features are discussed at some length in the next chapter.