SQUIRE PATTON BOGGS

REINSURANCE NEWSLETTER

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In this Issue

Congratulations to John Nonna and Larry Schiffer, who were named to *Who's Who Legal 100* 2014 for Insurance & Reinsurance.

Congratulations to John Nonna, who was elected to serve as Co-Chair of the Board of Directors and Trustees of the Lawyers' Committee for Civil Rights Under Law.

Recent Case Summaries

Seventh Circuit Holds FSIA Overrides State Statute Requiring Pre-Answer Security from Foreign Government-Owned Reinsurer and Rejects Right to Arbitrate

Pine Top Receivables of Ill., LLC v. Banco de Seguros del Estado, Nos. 13-1364 & 13-2331, 2014 U.S. App. LEXIS 2129 (7th Cir. Nov. 7, 2014).

This dispute arose over the assignee of a cedent's rights to collect debts against a foreign reinsurer wholly owned by the government of Uruguay. When the assignee was unable to collect amounts it claimed were due under the reinsurance contracts, it sued the reinsurer in federal court. The reinsurer failed to post prejudgment security with its answer as required by Illinois law. The reinsurer argued, and the district court held, that the Federal Sovereign Immunities Act's ("FSIA") prohibition on attaching a foreign state's property prevented application of the Illinois security requirement.

The Seventh Circuit affirmed, holding that a law requiring a foreign state to deposit money in a court pending the outcome of a case falls squarely within the definition of "attachment" under FSIA, because the requirement would totally prevent the foreign state from using those funds for the duration of the litigation. It further rejected arguments that the reinsurer had waived FSIA's protections by conducting business in Illinois and because of a reserves clause in the contract, concluding that prejudgment security differed from any contractual requirement and that the reinsurer may have conducted business in Illinois unaware of the Illinois requirement or believing FSIA would protect it.

The assignee also attempted to argue that the McCarran–Ferguson Act (a statute requiring generic federal laws to give way to state insurance statutes) required FSIA, not an insurance specific statute, to give way to the Illinois requirement. The Seventh Circuit did not reach the merits of that argument because it concluded the assignee had waived the argument.

Finally, the court considered whether the assignee had acquired the right to compel arbitration under arbitration clauses in the reinsurance contracts between the cedent and reinsurer. The Seventh Circuit affirmed the district court's conclusion that the assignment agreement did not convey that right. It reasoned that because the clause concerning enforcement of the debts in the assignment agreement was narrower than a preceding provision concerning obtaining information about the debts, which conveyed the power to obtain information "to the same extent" that the assignor could, the enforcement provision did not include the contractual right to compel arbitration. Instead, the court concluded the assignee obtained only those rights included in the narrower provision: to demand, sue, compromise, or recover the debts owed under the contract.

Second Circuit Affirms Ruling that Interest on a Judgment is Not a Covered Loss Under the Terms of the Reinsurance Contract

Seneca Ins. Co. v. Everest Reins. Co., No. 13-4201-cv, 2014 U.S. App. LEXIS 19929 (2d Cir. Oct. 16, 2014) (Summary Order).

In a case that was discussed in our December 2013 Reinsurance Newsletter, the Second Circuit Court of Appeals, in an unpublished Summary Order, has affirmed the district court's ruling that interest amounts included in the judgments entered against the insured were properly considered "interest on a judgment," which under the reinsurance agreement is not a covered loss. Because interest was not part of the covered loss, the US$5 million loss trigger to reach the reinsurance coverage was not met and the reinsurer had no obligation to pay.

Massachusetts Federal Court Grants Motion to Compel Arbitration of Reinsurance Dispute, Vacates Previous Arbitral Clarification

Nationwide Mut. Ins. Co. v. Liberty Mut. Ins. Co., Nos. 13-cv-12910-PBS and 14-cv-12046-PBS, 2014 U.S. Dist. LEXIS 157595 (D. Mass. Nov. 6, 2014).

A Massachusetts federal court granted in part and denied in part a reinsurer's motion to compel arbitration of "new" claims under a series of excess-of-loss treaties between the parties, and granted the reinsurer's motion to vacate a clarification issued by a previous arbitration panel. The motions concerned whether the arbitration panel's award applied to six previously billed, but unresolved, claims not raised as part of the original proceedings.

The reinsurer filed a petition to compel arbitration as to those claims in Massachusetts federal court under the Federal Arbitration Act (9 U.S.C. § 4). In a proceeding before the Massachusetts state court, an order had issued partially enforcing the prior arbitration award on the six "new" claims, but the court stated that it had neither considered nor relied on a clarification of the original award issued by the arbitration panel.

The court first examined the reinsurer's claim that the arbitration panel did not address all of the parties' prospective rights and obligations. The cedent argued that the award resolved the entire scope of the parties' relationship. The court first analyzed the state court's decision, noting that it had declined to interpret the term "future claims" as included in the award, or to decide whether the resubmitted claims so qualified. The state court based its enforcement of the award on alternate grounds not raised in the federal court. The court declined to revisit aspects of state court decision on the grounds of issue preclusion. Instead, it granted the reinsurer's motion to compel arbitration as to the six claims, but not insofar as it would require relitigation of the original award.

The reinsurer further argued that the clarification was both untimely and that the panel lacked authority to issue the clarification. The court agreed, noting that under the applicable Massachusetts law, application for modification of an arbitration award must be made within twenty days after issuance. The cedent argued that the clarification did not fall within the state statute's terms for a modification, and so the time limit did not apply. The court rejected the cedent's arguments, finding that the language of the statute, as further interpreted by courts, itself states that a modification or amendment of an award may be "for the purpose of clarifying the award." The court found that the cedent's request for clarification was made outside of the require time limit, and thus granted the reinsurer's motion to vacate the clarification.

New York Federal Court Confirms an Interim Security Award Against Reinsurer and Rejects Motion to Disqualify Panel

Companion Prop. & Cas. v. Allied Provident, No. 12-cv-7865, 2014 U.S. Dist. LEXIS 136473 (S.D.N.Y. Sept. 26, 2014).

The cedent petitioned a New York federal court to confirm an interim arbitration award that required the reinsurer to post security and the reinsurer sought to vacate the interim award and replace the arbitration panel. The court found that it had the authority to confirm the interim arbitration award due to extenuating circumstances and thus the award was confirmed.

The dispute arose out of a fronted private passenger automobile program produced by a managing agency, written on the cedent's paper and reinsured by a non-US reinsurer. A dispute arose when the reinsurer failed to pay amounts due under the quota share reinsurance agreement. The treaty contained an arbitration clause and the cedent demanded arbitration along with collateral for the reinsurer's obligations. The cedent moved for an interim security award sometime after the panel was constituted. Apparently, the reinsurer's party-appointed arbitrator became ill at around the same time. The parties dispute how much the reinsurer's party-appointed arbitrator was involved in panel decisions, but ultimately the panel issued an interim award directing that security be provided by depositing funds in escrow with the panel or by providing a letter of credit.

As the court found, more than a month after the interim award issued by the arbitration panel, the reinsurer had not complied with the panel's interim award to post the required security. Because, according to the court, the reinsurer did not seek reconsideration of the interim award or seek to vacate the award, but instead appeared to ignore the ruling, the court found that cedent was left with no choice but to petition the federal court to confirm the award. The court held that there was no basis to vacate the interim award, reasoning that reinsurer did not establish that the award was fundamentally unfair or that the arbitrators exhibited evident partiality. The court ultimately directed the reinsurer to appoint a new arbitrator because its arbitrator ultimately resigned because of his health issues.

The case provides a fascinating and detailed recitation of the communications between the panel and the parties over both the security issue as year-end approached and concerning scheduling the hearing on the merits where a panel member has a medical condition.

New York Federal Court Allows Attorney Disqualification Discovery

Utica Mut. Ins. Co. v. Emplrs. Ins. Co., No. 6:12-CV-1293, 2014 U.S. Dist. LEXIS 132271 (N.D.N.Y. Sept. 22, 2014).

A New York federal court was asked to address disqualification of counsel in a reinsurance dispute that is subject to arbitration. After the arbitration demand was served, the reinsurer demanded that the cedent's counsel withdraw based on counsel's prior representation of the cedent and, allegedly, the reinsurer in the underlying claim. The cedent responded by going to court seeking an order declaring that its counsel should not be disqualified. The reinsurer counterclaimed seeking disqualification.

The cedent moved for summary judgment and the reinsurers moved for discovery. The cedent's motion was denied and the reinsurers' motion was granted. The court concluded that inquiry into the potential conflict was warranted because the reinsurers sufficiently alleged a relationship with cedent's counsel. The relationship, while admittedly not a formal attorney-client relationship, allegedly arose during the underlying coverage case where the cedent's counsel represented the cedent in the coverage matter against the insured and allegedly represented the reinsurers' interests as well as part of a joint defense agreement.

This is an important issue because the ultimate decision after discovery, assuming it goes that far, will add to the jurisprudence of attorney disqualification in the context of counsel representing a cedent and also providing information to a reinsurer. Whether and what information a cedent should provide to a reinsurer about a claim is already under pressure because of the myriad court decisions allowing for the discovery of reinsurance information by policyholder counsel. This case has the potential to exacerbate that already existing tension between cedents and reinsurers on the disclosure of privileged analyses.

Massachusetts Federal Court Dismisses Petition to Confirm Interim Arbitration Award

First State Ins. Co. v. Nationwide Mut. Ins. Co., No. 13-cv-11322-IT, 2014 U.S. Dist. LEXIS 149649 (D. Mass. Oct. 21, 2014).

A Massachusetts federal court granted a reinsurer's motion to dismiss a petition to confirm an interim arbitration award concerning contract interpretation and application of the contract. As the court stated, an award was issued after initial briefing on a threshold issue raised by the cedent at the organizational meeting. The award was labeled a final award on the motion for an award on contract interpretation. Thereafter, other interim awards were issued and ultimately the panel issued a final award and payment order on the merits.

After the 90-days to petition to vacate an award expired, on the 100th day the cedent petitioned the court to confirm the interim award. The reinsurer moved to dismiss the petition, which the court granted.

In granting the reinsurer's motion to dismiss the cedent's petition to confirm the interim award, the court indicated that even though the award was labeled a final award, the panel expressed no intention to resolve all claims submitted in the demands for arbitration. In fact, said the court, the award directed the parties to report back on a schedule for the remaining matters. Because, according to the court, both parties did not agree to bifurcation, the evidence showed no understanding that the parties agreed to resolve a separate, independent claim. The court also noted that what the arbitration panel called the award is immaterial to the court's decision. Thus, said the court, although it is true to that an interim award maybe final in some circumstances, those circumstances did not exist here.

When and how an interim award can be confirmed has been subject to much commentary. Security awards are typically confirmed. Here, however, the court found that because the parties did not agree to treat this interim contract interpretation as a separate, independent issue, the award was not "final" and was not subject to confirmation.

Michigan Federal Court Grants in Part and Denies in Part Request to Seal on Motion to Confirm Arbitration Award

Amerisure Mut. Ins. Co. v. Everest Reins. Co., No. 14-cv-13060, 2014 U.S. Dist. LEXIS 153013 (E.D. Mich. Oct. 29, 2014).

As is quite common, a Michigan federal court was faced with a request by a cedent to allow it to file its motion to confirm a final arbitration award under seal. In this case, the reinsurer opposed the motion to seal in part.

In granting the motion in part, the court relied on well-established precedents in the Sixth Circuit and found that neither party had provided any cognizable basis to file the final award under seal in its entirety. The court advised that it would transmit to the parties a highlighted version of the final award showing the parts that will be sealed.

From the decision, it appears that references to non-parties to the arbitration likely will be sealed, but the substantive rulings of the arbitration panel will likely not be sealed. The court made it clear that sealing cannot be used to prevent unhelpful portions of a final award from being public in an effort to avoid future use in other legal proceedings. Essentially, the court took the view consistent with precedent that a corporation's interest in shielding prejudicial information from the public's view, standing alone, cannot justify the sealing of that information.

This decision is consistent with other recent decisions where requests to seal reinsurance arbitration awards and related papers have been denied.

New York Federal Court Decides Rare Cat Bond Case

Mariah Re Ltd. v. Am. Family Mut. Ins. Co., No. 13-cv-4657 (RJS), 2014 U.S. Dist. LEXIS 140859 (S.D.N.Y. Sept. 30, 2014)

We don't see many Cat Bond cases, but a few are starting to appear. The most recent decision involves a dispute in New York federal court about whether the Property Claims Service could issue a supplement to its original bulletin on a weather event and whether the calculation of the event and its effect on the reinsurance agreement should have considered the supplemental information.

The supplemental information concerned whether the losses arising from the severe weather event were properly categorized as metro or non-metro. The characterization made a difference as to whether the cedent received the proceeds of the Cat Bond or whether the investors would not have to pay. The special purpose vehicle reinsurer argued that the changes to the original bulletin via the supplement violated the terms of the agreements and could not be considered. Essentially, according to the court, the reinsurer argued that once the bulletin was sent, it could not be altered even if the actual facts were different upon subsequent analysis.

The court essentially found that there was no breach of any duties or contract and that the supplemental information added to the original bulletin was not prohibited by the terms of the agreement. These non-traditional alternative risk transfer transactions are very complicated and the triggers are equally complicated. The court in this case found that the documents were unambiguous and that no relief was available to the reinsurer. The cedent's recovery under the Cat Bond was upheld. This case is on appeal so we will see if the Second Circuit agrees with the district court's analysis.

New York Federal Court Decides Another "Bellefonte" Case in Favor of the Reinsurer

Utica Mut. Ins. Co. v. Clearwater Ins. Co., No. 6:13-cv-1178, 2014 U.S. Dist. LEXIS 162645 (N.D.N.Y. Nov. 20, 2014).

A New York federal court has ruled for the reinsurer in yet another dispute involving the limits of a facultative reinsurance certificate, this time in the context of underlying asbestos losses arising from Goulds Pumps.

Consistent with the many "*Bellefonte*" progeny, here the facultative certificates reinsuring underlying umbrella policies contained a preamble noting the statements contained in the declarations and terms and conditions of the certificates. The certificates had a liability and basis of acceptance clause, which identified the exposure reinsured.

This dispute concerns the reinsurer's motion for partial summary judgment that its liability is capped at US$5 million and US$2.5 million, respectively, under the facultative certificates. As the court noted, the sole issue is whether the cedent can recover defense costs or other expenses in excess of the sums stated in the liability clauses in the certificates. Unremarkably, the reinsurer relied on Second Circuit precedent on this issue. Even more unremarkably, the court, in granting the motion, relied on *Bellefonte Reins. Co. v. Aetna Cas. & Sur. Co.*, 903 F.2d 910 (1990), and the cases that followed it.

In finding for the reinsurer, the court agreed with the reinsurer that the holdings of these cases were directly applicable to the language in the reinsurer's facultative certificates. The court was not persuaded by the cedent's argument that the lack of the word "limit" in the facultative certificates was a distinguishing factor. The court also rejected the cedent's arguments concerning the follow-the-forms and claims clauses. Finally, the court rejected the cedent's request for further discovery and the introduction of custom and practice evidence. The court held that the facultative certificates were unambiguous and, therefore, consideration of extrinsic evidence would not be considered.

Illinois Appellate Court Finds for Reinsurer on Facultative Certificate Limits

Cont'l Cas. Co. v. Midstates Reins. Corp., No. 1-13-3090, 2014 Ill. App. Unpub. LEXIS 2456 (Ill. App. 1st Dist. Nov. 4, 2014).

In yet another "Bellefonte" case, an Illinois appeals court has found for the reinsurer where the facultative certificates clearly and unambiguously provided an aggregate policy limit on the reinsurance assumed. In this case the cedent sought a declaratory judgment of its rights under multiple facultative certificates. The underlying claims were environmental liabilities. The reinsurer paid the claims up to the total amount of the reinsurance limits under the certificates. The motion court granted the reinsurer's motion for judgment finding that the facultative certificates were not ambiguous and limited both loss and expense. The appellate court affirmed.

In affirming the motion court, the appellate court followed the "four corners" approach to contract construction. The court agreed with the motion court's reliance on *Bellefonte* and held that the facultative certificates provided a clear policy limit, inclusive of expenses. As in the case discussed above, the court adopted and relied upon the holding *Bellefonte* and subsequent cases as being widely accepted. The court found that none of the provisions of the facultative certificates removed expenses from the overall liability cap provided. The court held that the certificates clearly and unambiguously provided for an aggregate policy limit that included both losses and expenses.

New York State Court Addresses Various Late Notice and Discovery Issues

Lexington Ins. Co. v. Sirius Am. Ins. Co., No. 651208/2012, 2014 N.Y. Misc. LEXIS 4138 (N.Y. Sup. Ct. Sept. 15, 2014).

A New York state court was faced with multiple motions in a dispute over the bulk settlement of asbestos bodily injury claims. The cedent sought damages and a declaratory judgment against the reinsurer under a series of facultative reinsurance certificates reinsuring the excess umbrella exposure to Foster Wheeler.

Ultimately, the cedent settled the massive asbestos claims against Foster Wheeler and billed the reinsurer for its share of the settlement. The reinsurer defended based on failure to provide prompt notice and sought discovery on allegations of bad faith. The cedent countered by relying on the follow-the-fortunes doctrine and the following clauses in the facultative certificates.

In analyzing each of the certificates, the court noted that one of the certificates had a condition precedent that the cedent must provide promptly a definitive statement of loss for claims involving death, serious injury or a lawsuit. The court also noted that notices of loss provided by an affiliate do not fulfill the cedent's obligation to provide notice by the actual entity itself. Accordingly, the court found that under that facultative certificate, the cedent failed to provide timely notice as a matter of law. Because the certificate required prompt notice as a condition precedent, the reinsurer did not have to demonstrate prejudice to rely on the defense of late notice.

Nevertheless, the court found that the evidence demonstrated that the reinsurer waived its contractual right and coverage defenses, including the right to prompt notice, on a November 2011 billing because the reinsurer paid that billing. The court ruled, however, that the waiver did not apply to later billings.

In a second set of facultative certificates, the court found that prompt notice was not a condition precedent and that the reinsurer is required to demonstrate prejudice to avoid its obligations. The court held that because the reinsurer could not demonstrate prejudice, the cedent was entitled to summary judgment on those facultative certificates.

What makes this case interesting is the court's useful analysis of the distinction between notice provisions that are conditions precedent and are not conditions precedent and how that changes the way a late notice defense is reviewed.

Pennsylvania State Appeals Court Finds Non-Commercial Insurance Company Entered Into a Reinsurance Agreement for Claims Priority Purposes

Ala. Ins. Guar. Ass'n v. Reliance Ins. Co., No. 6 REL, 2012, Pa. Commw. LEXIS 10758 (Sept. 12, 2014).

By a split panel decision, a Pennsylvania state intermediate appellate court found that a liquidator had not erred in deeming the guaranty association a reinsurer, or in characterizing the benefits paid by the guaranty association as arising from a reinsurance contract.

The dispute concerned whether a distribution claim against the estate of an insolvent insurance company should be regarded as one arising from direct insurance—which would confer a higher distribution priority level—or whether it arose from reinsurance. The guaranty association asserted the distribution claim for reimbursement of payment that had been made only under the Alabama Supreme Court's mandate.

That collateral Alabama case challenged the guaranty association's refusal to pay claimed benefits. The guaranty association's refusal was based on the ground that the benefits were reinsurance benefits, and therefore not covered under the Alabama Guaranty Association Act. Disagreeing, the Alabama Supreme Court ruled that the relevant policy could not be deemed a true reinsurance contract. Among other reasons, the Alabama Supreme Court maintained that the buyer of the policy was not a commercial insurance company engaged in the business of selling insurance. The guaranty association was required to pay the claim.

Notwithstanding this Alabama Supreme Court decision, the liquidator denied the guaranty association the "b" priority level accorded direct insurance claims. Instead, the distribution claim was assigned priority level "e." The guaranty association sought review of this determination in the Commonwealth Court. The Commonwealth Court affirmed the liquidator's determination.

Applying the reasoning of a prior opinion, *CSAC Excess Ins. Auth. v. Reliance Ins. Co.*, No. 1 REL 2007 (Pa. Cmwlth), the majority concluded that, if both parties understand coverage to be reinsurance and their agreement operates as reinsurance, then any claim arising from that agreement is entitled to the priority level of reinsurance policy claims—level "e"—regardless of whether both parties are commercial insurance companies that sell insurance.

The dissent found that the role of the trust purchasing the policy was to provide coverage, not to pay for coverage. In so doing, the trust did not act as a reinsurer, but as an entity entering the marketplace to purchase excess coverage for members. Unable to find any other decisions where a state rejected the payment of a claim made in accordance with another state's law, the dissent observed that the decision controverted the Alabama Supreme Court and, "set[] a worrisome precedent" by creating "unnecessary uncertainty in the insurance solvency system that requires cooperation among the several states."

Priority of distribution is a critical factor in insurance insolvency. By relegating the claim to priority level "e," which applies to reinsurance claims, it is unlikely that the claim will ever be paid.

New York Appellate Court Dismisses All Claims Against Reinsurer and Claims Adjuster

OneBeacon Am. Ins. Co. v. Colgate-Palmolive Co., No. 651193/11, 2014 N.Y. App. Div. LEXIS 7255 (N.Y. App. Div. 1st Dep't Oct. 28, 2014).

A New York appellate court was asked to address whether a reinsurer could be joined as a counterclaim defendant in a contract dispute between the insured and its insurer. The court held that based on the total absence of a contractual relationship between the insured and the reinsurer and its affiliated claims adjuster all claims against the reinsurer and its claims adjuster should be dismissed.

The underlying dispute was about the right to control the insured's defense against a series of asbestos bodily injury cases. The cedent/insurer claimed that the insured did not allow the insurer to control the defense. The insured counterclaimed against the insurer and joined the reinsurer and its affiliated claims adjuster. The reinsurer and claims adjuster moved to dismiss all the counterclaims. The motion court dismissed some, but not all of the counterclaims and the reinsurer appealed.

On appeal, the insured argued that the insurer's contractual relationship with the reinsurer and its claims adjuster created a conflict of interest because of the dual role as both the reinsurer of the cedent's liability and the claims adjuster under the reinsured policies. Essentially, according to the court, the insured wants to vigorously defend the asbestos cases and the reinsurer and its claims adjuster want to settle.

In finding for the reinsurer on appeal, the court held that none of the counterclaims stated a cause of action. The court found that the reinsurer's and the claims adjuster's "dual role" does not give rise to any liability to the insured because the insured lacks contractual privity with the reinsurer and claims adjuster. There can be no claim for breach of contract, held the court, if there is no privity. The court found that the reinsurance agreement is a separate and distinct contract from the underlying insurance policies. Moreover, held the court, nothing in the reinsurance agreement suggested an assignment or assumption of the obligations of the underlying policies. The court found no special circumstances that would allow for a direct right of action against the reinsurer.

The remaining claims, in addition to breach of contract, all filed because there is no contract. The claim for tortious interference failed, said the court, because the claims adjuster acted as a designated agent and no action for tortious interference can be brought against an agent acting within the scope of its duties on behalf of a principal.

New York Federal Court Holds Cedent and Reinsurer Have Identity of Interest Concerning Recovery from Third Party

Wells Fargo Bank, N.A. v. Wales LLC, No. 13 Civ. 6781 (PGG), 2014 U.S. Dist. LEXIS 132192 (S.D.N.Y. Sept. 19, 2014).

A New York federal court denied a reinsurer's attempt to intervene in a suit involving a dispute among the cedent, the administrator of a residential mortgage-backed securitization trust, and certain certificate holders under the trust (whom the cedent insured). The dispute between the cedent and the certificate holders concerned a disputed interpretation of the trust documents. The cedent contended it was entitled to an independent right of reimbursement from the trust proceeds for paid insurance claims. The certificate holders, however, contended the cedent was entitled only to subrogation of their rights.

The trust administrator had adopted the cedent's interpretation of the trust documents for two years, distributing in excess of US$47 million of trust proceeds to the cedent. At the objection of the certificate holders to this interpretation, the trust administrator instituted a suit against the cedent and the certificate holders, seeking a declaration of their rights under the trust documents. The reinsurer sought to intervene in this suit, arguing that because of its agreement with the cedent, it had an 85% stake in the trust's proceeds regardless of the outcome.

The certificate holders objected to the reinsurer's attempted intervention, arguing that the cedent adequately represented the reinsurer's interests. The court agreed and denied the reinsurer's motion to intervene, finding that the cedent shared an identity of interest with the reinsurer in seeking a declaration that the trust documents should be interpreted in such a way so as to maximize the cedent's recovery from the trust proceeds. In so ruling, the court found that even though the reinsurer might be entitled to 85% of whatever the cedent recovered, the cedent's interest was still identical to the reinsurer's because the more the trust distributed to the cedent, the more the reinsurer also would recover.

The court also rejected the reinsurer's argument that the reinsurer and cedent might have divergent interests if the cedent were required to pay back the US$47 million it already had received due to differing interpretations of the reinsurance agreement. That dispute, the court ruled, would be more properly handled by a subsequent proceeding between the cedent and reinsurer and would unnecessarily complicate this litigation involving interpretation of the trust documents.

Iowa Federal Court Affirms Holding that Risk Management Communications Between Cedent and Reinsurer Are Not Privileged and Non-Party Reinsurer Must Produce Documents Pursuant to Subpoena

Progressive Cas. Ins. Co. v. FDIC, No. C 12-4041 (MWB), 2014 U.S. Dist. LEXIS 140709 (N.D. Iowa Sept. 3, 2014).

An Iowa federal court reviewed two components of a magistrate's discovery order after the cedent and non-party reinsurer filed objections. In the course of discovery, the cedent produced documents that contained communications between the cedent and reinsurer, but which were redacted based upon the attorney-client privilege and work product doctrine. The magistrate's discovery order required disclosure of the redacted portions of the communications and also required the reinsurer, who was not party to the underlying suit, to produce documents pursuant to plaintiff's subpoena.

Concerning the issue of work product privilege, the cedent argued that the question was not whether the information was prepared in the ordinary course of business, but whether the information contained within it work product information regarding the case by plaintiffs that was ultimately filed. In affirming the magistrate's order, the court noted that prior Eighth Circuit precedent rejected claims that the work product privilege covers "risk management documents," which had been "generated in an attempt to keep track of, control, and anticipate the costs of … litigation." The court further concluded that work product privilege did not protect even portions of the documents.

Concerning the issue of attorney-client privilege, the court affirmed the finding that the privilege had been waived due to cedent's voluntary disclosure of the documents to the reinsurer. The court rejected the cedent's argument that the common interest doctrine applied as between it and the reinsurer, reasoning that in order for the common interest doctrine to apply, held that what is required is evidence of an agreement (although not necessarily a written agreement) between an insurer and its reinsurer that establishes a "'cooperative and common enterprise towards an identical legal strategy." The court held that a contractual right on behalf of the reinsurer to participate in the litigation did not alone meet this standard.

Finally, the court also adopted a broad definition of relevancy and held that the non-party reinsurer, which had not reinsured the specific claim at issue in the underlying litigation, had to produce documents in response to a subpoena despite the potential burden on reinsurer.

Reinsurance Contracts Are Relevant to Assist in Discovering Financial Status

Smith v. ComputerTraining.com, Inc., No. 10-11490, 2014 U.S. Dist. LEXIS 135904 (E.D. Mich. Sept. 26, 2014).

A Michigan federal court entered a default judgment in a class action against a policyholder for injuries stemming from its abrupt termination of a computer training program in which the plaintiffs had enrolled. In post-judgment proceedings, plaintiffs learned that the policyholder had a general liability insurance policy. Plaintiff then sought discovery from the non-party cedent for, among other things, information regarding the insurance policy and any reinsurance contracts the cedent had concerning the policyholder's policy. The cedent objected to the relevance of the document requests.

In allowing the non-party discovery, the district court held that the insurance policies, any reinsurance policies, loss run information, and any other information regarding the policyholder that the cedent held, was relevant and had to be produced to plaintiffs. The court theorized that although the reinsurance policies and other information might not directly involve or be "directly relevant," disclosure could lead to the discovery of admissible evidence, including the financial status of the policyholder. As such, the court required production of the insurance and reinsurance information, or if the information did not exist, then to provide an affidavit to that effect.

Reinsurance Contracts Are Discoverable if They Relate to Coverage Dispute

Harleysville Lake States Ins. Co. v. Lancor Equities, Ltd., No. 13 C 6391, 2014 U.S. Dist. LEXIS 154685 (N.D. Ill. Oct. 31, 2014).

Cedent sought a declaratory judgment that its commercial property insurance policy did not cover losses and damages stemming from a fire at insured's property. In discovery, the insured requested all documents and correspondence relating to cedent's reinsurance coverage for first-party property claims for the previous six years on the basis that this information could lead to the discovery of relevant information. The cedent objected to the discovery requests, and in response to a subsequent motion to compel, objected on the grounds that reinsurance information was not relevant and that any communications between insurers were protected by the common interest doctrine.

The Illinois federal court, in allowing some of the discovery requested, noted that federal courts disagreed whether reinsurance information was discoverable in insurance coverage declaratory judgment actions. The court pointed out the tension between federal rules that required disclosure of insurance agreements that could satisfy judgment, and case law from Illinois that distinguished reinsurance agreements from direct insurance policies because of substantive differences in both type and form. The court ultimately resolved this tension by looking to previous decisions in the district that required the disclosure of reinsurance agreements.

The court reduced the scope of discovery, holding that the cedent had to disclose any reinsurance agreement that might indemnify reinsured for the claim at issue. Additionally, the district court only required the production of any relevant reinsurance policies, agreeing with the cedent that communications with reinsurers might be privileged or subject to the common interest extension of attorney-client privilege.

Michigan Federal Court Addresses Document Production Dispute and Grants in Part Fees and Costs Against Cedent

Mich. Millers Mut. Ins. Co. v. Westport Ins. Corp., No. 1:14-cv-00151-PLM (W.D. Mich. Nov. 7, 2014).

In a reinsurance dispute arising from coverage for multiple deaths from a gas explosion on a farm, a reinsurer sought fees and expenses following a motion to compel discovery. In granting the motion in part, the court noted that the cedent had promised disclosure of certain documents and had not complied with its promise. The court found that a three-month delay in producing the documents was a sufficient basis to award reasonable attorney fees and expenses. The court held that the cedent's actions were both unjustified and unreasonable under the circumstances. The court ultimately limited the attorney fees based on the parties' agreement, but nevertheless ordered the sanctions.

Second Circuit Dismisses Appeal on Breach of Reinsurance Underwriting Agreement Dispute

Acumen Re Mgt. Corp. v. Gen. Sec. Nat'l Ins. Co., 769 F.3d 135 (2d Cir. 2014).

In a contentious dispute over the breach of a reinsurance underwriting agreement, the Second Circuit dismissed an appeal by the underwriting agent of the district court's partial summary judgment order in favor of the reinsurer. We discussed the summary judgment decision in our March 2013 Reinsurance Newsletter.

The dispute was over alleged contingent commissions claimed due by an underwriting manager against its principal, a specialty reinsurer. The district court granted summary judgment in favor of the reinsurer on four out of five breach of contract theories and held that only nominal damages would be available for the remaining theory that was not dismissed. The agent appealed and the reinsurer argued, in part, that the Second Circuit had no jurisdiction to hear the appeal because the partial summary judgment order was not appealable.

In a reasonably lengthy opinion, the Second Circuit agreed and held that the underlying order was not amenable to certification under Rule 54(b) and the court lacked jurisdiction to hear the appeal. Essentially, the court agreed with the district court that the five theories of breach of contract did not qualify as separate claims, but were so untied and mutually referential as to not be separate claims.

Oklahoma Federal Court Dismisses Bad Faith Claim, But Denies Summary Judgment on Contract Claim on Assumption Reinsurance Agreement

Evans v. Liberty Nat'l Life Ins. Co., No. 13-CV-0390-CVE-PJC, 2014 U.S. Dist. LEXIS 159507 (N.D. Okla. Nov. 12, 2014).

An Oklahoma federal court was faced with interpreting the effect of an assumption reinsurance agreement in a dispute between a policyholder and the original policy issuing company for breach of contract and bad faith. The policyholder purchases a cancer treatment policy from the original insurer and some years later the original insurer entered into an assumption reinsurance contract with the assuming insurer. The policyholder made a claim after being diagnosed with cancer and presented that claim to the assuming insurer. The amount paid was not satisfactory and the policyholder sued both insurers for bad faith and breach of contract. The original insurer moved for summary judgment based on the assumption reinsurance agreement.

In granting the motion on the bad faith claim and denying the motion on the breach of contract claim, the court had the opportunity to explore the nature of assumption reinsurance. The court noted that assumption reinsurance is distinguishable from indemnity reinsurance because assumption reinsurance is the sale of the underlying policies and not the purchase of reinsurance protection. The court correctly pointed out that while assumption reinsurance transfers direct liability under the policy, the ceding company remains liable unless there has been a novation substituting the reinsurer for the ceding company. Thus, said the court, it could only grant summary judgment to the original insurer if the agreement was assumption reinsurance and there was an effective novation. While finding that the contract was one of assumption reinsurance, the court found that there was not sufficient evidence presented to show that a novation occurred.

The court, however, granted summary judgment on the bad faith claim because the policyholder failed to present any evidence that the original insurer dealt with the underlying claim in a tortious or unreasonable manner.

Recent Regulatory Developments

On November 6, 2015, the Financial Stability Board (FSB) and the International Association of Insurance Supervisors (IAIS) published an updated list of Global Systemically Important Insurers (G-SIIs). The **list** includes the same G-SIIs previously identified as such in 2013. Of note, in the release, the FSB and IAIS stated that they would postpone a decision on the G-SII status of reinsurers, pending further development of the G-SII assessment methodology.

More recently, at a hearing held by the House Financial Services Subcommittee on Housing and Insurance, lawmakers discussed (1) developments related to capital standards for insurers; (2) transparency at the IAIS; and (3) concerns regarding the impact of IAIS determinations on the ability of US regulators to make independent decisions regarding systemically important financial institution (SIFI) designations and capital standards for insurers. Absent from their discussion, however, was any mention of the FSB and IAIS's recent updates on G-SII designations or their decision to postpone any designations of systemically important reinsurers.

In the next Congress, we expect the House Financial Services Committee and the Senate Banking, Housing, and Urban Affairs Committee to continue its increased oversight of FSB and IAIS developments, and the systemically important designations of insurers and reinsurers in the US and abroad.

Recent Speeches and Publications

- Micah Green, Norma Krayem, Larry Schiffer and Ellen Shapiro spoke on a webinar entitled "The Terrorism Risk Insurance Act (TRIA) Reauthorization Update, The Insurance Industry Perspective," on September 9, 2014.
- John Nonna spoke on "A Focus on Allocation of Toxic Tort, Asbestos and Other Long Tail Claims," at the American Conference Institute's National Forum on Insurance Allocation on October 29, 2014, in New York.
- John Nonna co-chaired the ARIAS•U.S. Fall Conference, "The Arbitrators Speak: Insight and Perspective from the Arbitrators Themselves," on November 13-14, 2014, in New York. Suman Chakraborty participated as a discussion break-out leader at the same conference.
- Suman Chakraborty is speaking on *"Attorney Disqualification in Reinsurance Disputes: Where Do We Draw The Line?,"* at the IRU/ Reinsurance Networking Group meeting on December 9, 2015, in New York City.
- Larry Schiffer, Eridania Perez, Suman Chakraborty, Kate Woodall, Caroline Billet and Zachary Novetsky authored a free e-book summarizing the most influential reinsurance cases litigated in the United States. Entitled "50 Reinsurance Cases Every Risk Professional Should Know," the e-book was published by the International Risk Management Institute, Inc. (IRMI) and provides a detailed description of each case as well as its implications on important reinsurance coverage issues. The 130-page e-book is available for free here.
- Larry Schiffer and Alexandra Chopin authored "Best Practices for Cost Effective and Compliant E-Discovery in Runoff," in *AIRROC Matters*, Vol. 10, No. 3, Fall 2014, the magazine of the Association of Insurance and Reinsurance Run-off Companies.
- Larry Schiffer authored, "When Is a Reinsurance Treaty Not a Reinsurance Treaty?," an Expert Commentary on Reinsurance for IRMI.com, the website of the IRMI, in September 2014.

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