

Reinsurance

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The redux on developments in the law of reinsurance

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Contacts:



Amy S. Kline
215.972.8567
akline@saul.com



Caitlin M. Piccarello
215.972.7153
cpiccarello@saul.com



Braden A. Borger
215.972.7176
bborger@saul.com



Sean T. O'Neill
215.972.7159
soneill@saul.com



Andrea P. Brockway
215.972.7114
abrockway@saul.com

Southern District of New York Refuses to Disqualify Arbitrator or Consolidate Proceedings in Reinsurance Dispute

The Southern District of New York held that the Federal Arbitration Act does not permit the court to disqualify an arbitrator chosen in accordance with the procedures established in the parties' arbitration agreement and further held that the decision of whether to consolidate two arbitrations was for the arbitrators and not the court to decide. *IRB-Brasil Resseguros S.A. v. Nat'l Indemnity Co.*, No. 11-CV-1965 (S.D.N.Y. Oct. 5, 2011).

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United States Supreme Court Holds Court Must Compel Arbitration of Arbitrable Claims Even if Doing So Leads to Piecemeal Litigation

The Supreme Court vacated a state court decision that refused to compel arbitration under the Federal Arbitration Act merely on the grounds that some of the claims could be resolved by the court without arbitration. *KPMG LLP v. Cocchi*, 2011 WL 5299457 (U.S. Nov. 7, 2011).

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Delaware Chancery Court Holds Delaware Law Permits Enforcement of Arbitration Clause in Reinsurance Agreement Against Receiver

The Delaware Chancery Court held that Delaware law does not vest the court with exclusive jurisdiction over all claims against an insolvent insurer and that the receiver, who steps into the place of the insolvent insurer, is required to honor the contractual arbitration obligations of the insurer. *In the Matter of the Rehabilitation of Manhattan Re-Insurance Co.*, 2011 WL 4553482 (Del. Ch. Oct. 4, 2011).

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Southern District of New York Refuses to Disqualify Arbitrator or Consolidate Proceedings in Reinsurance Dispute

IRB-Brasil Resseguros S.A. v. Nat'l Indemnity Co., No. 11-CV-1965 (S.D.N.Y. Oct. 5, 2011).

This case involves a dispute concerning reinsurance policies issued to IRB-Brasil Resseguros S.A. (IRB) by National Indemnity Company (NIC). IRB instituted three arbitration proceedings against IRB: one arbitration in London (Arbitration 1) and two arbitrations in New York (Arbitration 2 and Arbitration 3). Arbitration 1 concerned a 2008 reinsurance policy and Arbitration 2 concerned a 2009 reinsurance policy. Both the 2008 and 2009 reinsurance policies contained arbitration clauses that provided a procedure for the selection of arbitrators.

The parties followed these procedures in selecting the arbitrators for Arbitration 1. The arbitration panel then determined that they lacked jurisdiction and dismissed the arbitration. IRB promptly commenced Arbitration 3 in New York, involving the same 2008 policy that was at issue in Arbitration 1. Meanwhile, IRB selected James White as its party-appointed arbitrator in Arbitration 2 and nominated Jonathan Rosen as the neutral arbitrator. The parties postponed selection of the neutral arbitrator in Arbitration 2 while the parties attempted to settle the matter. Ultimately, Arbitration 2 was not settled. NIC then sought to appoint Jonathan Rosen as its party-appointed arbitrator in Arbitration 3. IRB objected and filed a petition in the Southern District of New York seeking to disqualify Rosen and to consolidate Arbitrations 2 and 3.

The court denied IRB's petition, reasoning that the Federal Arbitration Act (FAA) does not permit the court to disqualify an arbitrator chosen in accordance with the procedures established in the parties' arbitra-

tion agreement. The court distinguished *Excelsior 57th Corp. v. Kern*, 218 630 N.Y.S.2d 492 (1st Dep't 1995) because that case involved the disqualification of an arbitrator when it had previously been determined that the arbitrator engaged in conduct that gave rise to an appearance of impropriety. The court held that even if it was permitted to disqualify Rosen, the fact that he was proposed as a neutral arbitrator in Arbitration 2 did not raise any concerns about his ability to serve as NIC's party-appointed arbitrator in Arbitration 3.

The court also declined to consolidate Arbitrations 2 and 3, noting that this decision should be made by the arbitrators in Arbitration 2. The court cited the Supreme Court decision in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444, 452-53 (2003), for the proposition that "the kind of arbitration proceeding the parties agreed to" is "for the arbitrator, not the courts, to decide."

REDUX IN CONTEXT:

- The FAA does not permit the court to interfere with the selection of arbitrators when the parties' have followed the selection procedures outlined in their arbitration agreement;
- Procedural matters, such as whether to consolidate two arbitrations, are matters best left to the arbitrators, not courts, to decide.

Supreme Court Holds Court Must Compel Arbitration of Arbitrable Claims Even if Doing So Leads to Piecemeal Litigation

KPMG LLP v. Cocchi, 2011 WL 5299457 (U.S. Nov. 7, 2011).

In this case, KPMG argued that investment funds affiliated with Bernie Madoff should be required to arbitrate their claims against KPMG pursuant to the arbitration clause contained in the audit serv-

ices agreement the funds entered into with KPMG. The investment funds asserted four claims against KPMG: negligent misrepresentation, violation of the Florida Deceptive and Unfair Trade Practices Act

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(FDUTPA), professional malpractice and aiding and abetting a breach of fiduciary duty. The state court held that the funds were only required to arbitrate claims that were derivative of the auditing services agreement. The funds' claims for negligent misrepresentation and violation of the FDUTPA, however, were direct, not derivative claims. Because two of the four claims set forth in the complaint were non-arbitrable, the court refused to compel arbitration of any of the claims. This decision was affirmed by the Florida Court of Appeals.

The Supreme Court reversed, relying on its prior decision in *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985). In *Dean Witter*, the court held that under the Federal Arbitration Act (FAA), courts are required to "compel arbitration of pendant arbitrable claims when one of the parties files a motion to compel, even where the result would be the possibility of inefficient maintenance of separate proceedings in different forums." In order to comply with *Dean Witter*,

the Supreme Court held in *KPMG* that the lower court must "examine a complaint with care to assess whether any individual claim must be arbitrated. The failure to do so is subject to immediate review." The court remanded the matter to the state court to determine whether the remaining two claims were subject to arbitration.

REDUX IN CONTEXT

- On a motion to compel arbitration under the FAA, the court must determine whether each claim is subject to arbitration and cannot simply deny arbitration because some claims are not arbitrable;
- Pendant arbitrable claims must be arbitrated, notwithstanding the nature of other claims alleged in the same action.

Delaware Chancery Court Holds Delaware Law Permits Enforcement of Arbitration Clause in Reinsurance Agreement Against Receiver

In the Matter of the Rehabilitation of Manhattan Re-Insurance Co., 2011 WL 4553482 (Del. Ch. Oct. 4, 2011).

Manhattan Re-Insurance Company (Manhattan Re) and American Motorists Insurance Company (AMICO) entered into a series of reinsurance contracts pursuant to which AMICO was required to provide a letter of credit as security for its obligations to Manhattan Re. In 2003, AMICO notified Manhattan Re that it would not be able to obtain an extension on its line of credit. Pursuant to the agreement of the parties, Manhattan Re drew down the full amount of the \$7.3 million line of credit. In 2007, Manhattan Re experienced financial difficulties and was placed into receivership. In 2010, the Receiver petitioned the Delaware Court of Chancery to approve a rehabilitation plan for Manhattan Re which included a request to allow the Receiver to use the \$7.3 million line of credit to satisfy Manhattan Re's general obligations as well as any administrative fees and expenses incurred by the Receiver. AMICO objected to the proposed plan's

treatment of the \$7.3 million and moved to have the dispute referred to arbitration.

The court first determined that Delaware law vests exclusive jurisdiction for all disputes related to insurance rehabilitation proceedings in the Court of Chancery. The Delaware statute at issue includes Delaware's codification of the Uniform Insurers Liquidation Act (the Act). The court further held that although the Act grants the Court of Chancery exclusive *in rem* jurisdiction over the "rehabilitation of an insurer," the Act does not grant the court with exclusive jurisdiction over *all claims* brought against the insurer during the pendency of a rehabilitation. Considering Delaware's strong policy in favor of arbitration, the court held that the arbitration agreement between Manhattan Re and AMICO should be honored. "The Receiver who

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has assumed the place of Manhattan Re, should be required to honor the contractual provision.” Because both the Receiver and AMICO are “sophisticated parties,” there is no reason to believe either party would be prejudiced by having an arbitration panel, rather than the court, decide their dispute.

Additionally, the court declined to determine whether the Receiver’s statute of limitations defense applied. The court reasoned that, pursuant to the Federal Arbitration Act, “procedural arbitrability” issues, such as statute of limitations defenses, should be determined by the arbitration panel.

REDUX IN CONTEXT

- Notwithstanding the broad jurisdiction that state courts enjoy over insurance company insolvency proceedings, that jurisdiction does not extend to claims that are subject to valid arbitration clauses;
- Procedural arbitrability issues, such as statute of limitations defenses, are appropriately decided by arbitration panels, not the courts.

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