

**PROCEDURES FOR THE RESOLUTION OF U.S. INSURANCE  
AND REINSURANCE DISPUTES**

**By**

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**I. Introduction**

**A. Background to the Procedures**

The Procedures for the Resolution of U.S. Insurance and Reinsurance Disputes (hereinafter “Procedures”) were drafted by representatives of primary insurers and reinsurers, domestic and foreign, as well as their trade associations and practicing arbitrators.<sup>1</sup> These are the only procedures currently in use that were designed specifically for insurance and reinsurance arbitrations.<sup>2</sup> Currently, the Procedures are incorporated by reference in at least some of the contracts of a number of major insurers (e.g. AIG, Fireman’s Fund and The Hartford). Intermediary Guy Carpenter is suggesting that its clients consider doing the same.

**B. Need for Procedures**

Highly experienced arbitration practitioners, both arbitrators and counsel, are aware of a number of informal but well-understood practices and procedures that have developed in the reinsurance arbitration field over the years. Nonetheless, there are gaps –and, the process can be difficult for less experienced practitioners given the lack of detail in arbitration clauses and the confidentiality of the proceedings. To a large extent, the Procedures codify the existing “best practices,” provide specific authority in gray areas and suggest a resolution to some of the more controversial ones.

The target market for the Procedures are the insurance and reinsurance companies that may either incorporate the Procedures into their contracts by reference or agree to their use after the fact. While there are many arbitrations ongoing, individual companies may have few disputes which reach the arbitration or litigation stage. Those setting policy for contract drafting may have little experience with the arbitration process and balk at an alternative dispute resolution process which has no rules of evidence, no fixed procedures and no right to appeal panel orders (although there are

limited bases to vacate orders). The Procedures can assist company personnel in achieving an appropriate level of comfort with the predictability of the process.

### **III. Qualifications of the Panel**

Reinsurance contracts generally require that arbitrators have experience as insurance or reinsurance company executives but the particular terms used to describe qualifications are variable and sometimes murky. Contracts sometimes require panelists to be “impartial” or “disinterested” without defining these terms. Sometimes, underwriters at Lloyd’s are inadvertently excluded by a reference to service with insurance or reinsurance companies. Other times, a reference to “active or retired executives” calls into question the eligibility of an individual who otherwise qualifies but who has not formally “retired.”

Paragraphs 6.1 and 6.2 of the Procedures resolve these issues by requiring the arbitrator to be “disinterested” and the umpire “neutral” and by defining these terms in Paragraphs 2.3 and 2.4. The language is crafted to avoid the Lloyd’s and “retired” problems. In addition, there is an alternative that allows those who have not been officers of insurers or reinsurers to serve as arbitrators as long as they have a minimum of ten years experience in or service to the industry. The latter provision would allow very experienced members of law, accounting and actuarial firms as well as trade association officials to serve as arbitrators.

### **III. Selection of the Panel**

Some contracts do not anticipate a failure of cooperation in appointing an opposing party arbitrator or the umpire. For instance, some contracts do not allow one party to appoint both party arbitrators if the opposing party declines to appoint an arbitrator within a designated period of time. This can lead to stasis or a time consuming proceeding to obtain a court order to require the recalcitrant party to proceed with the arbitration process. In addition, questions have arisen as to the proper procedure when a panelist resigns for ill-health or other reasons - need the entire panel be replaced or just the individual who resigned?

However, the primary concern with panel selection is the process of selecting the umpire. Some believe that the outcome of the dispute is determined once the umpire is selected. While this is very seldom the case, the process is sufficiently important to merit close scrutiny. Usually, both sides propose three qualified candidates, strike two of the other side’s candidates and select the umpire by lot *e.g.* an odd or even digit in the Dow Jones Industrial Average for a particular day. While this process works well generally, there is concern about the ability to “game” the process by a party which proposes three weak or partisan candidates and then gets lucky in the selection by lot. When this occurs, the result is a one-sided proceeding or one in which the umpire is over his or her head in terms of both procedure and substance. Either is both painful to experience and detrimental to the integrity of the arbitration process.

Paragraphs 6.3 through 6.9 of the Procedures provide a remedy for these problems. Arbitrators are appointed within a fixed time schedule. If the respondent fails to appoint its party arbitrator, the moving party may do so and the arbitrators so selected choose an umpire. If a panelist resigns, that individual is replaced using the same procedure as for the initial appointment *i.e.* the

entire panel is not reappointed.

Paragraph 6.7 of the Procedures applies to appointment of the umpire when the party arbitrators cannot agree. Each side proposes eight individuals from a designated group of candidates (e.g. ARIAS - US list of certified umpires, RAA Arbitrator's Directory, the American Arbitration Association's list of reinsurance arbitrators<sup>3</sup>). Each side then selects three candidates from the other side's list. If there is a common candidate on each list, he or she is the umpire. If there are two common candidates, the umpire is chosen between those two individuals by lot. If there are no common candidates, each of the six candidates is ranked by the parties with the lowest numerical ranking candidate being appointed umpire. If the ranking results in a tie, the umpire is chosen from those tied candidates. The theory is that the number of candidates originally proposed plus the selection / ranking procedure will prevent a party from "gaming" the process. Although the selection may involve some element of drawing lots, the candidates among whom the lots are drawn are theoretically among the most favored by both parties.

#### **IV. All Neutral Panel Alternative**

It is well understood that the use of party appointed arbitrators results in something less than a totally neutral panel. How much less depends largely on the attitude of the party arbitrators. A few act simply as advocates of the party by which they were appointed. Most make sure their party's position is well-articulated but in the final analysis, try to make their decisions based on the merits. Perhaps the threshold issue is whether the party arbitrator system is a contributing element to problems identified with the arbitration process e.g. arbitrations which are too long and expensive with too much discovery and contentiousness. Does some degree of identification with a party by party arbitrators prevent a panel from acting decisively to avoid these problems? A growing number of experienced practitioners advocate all neutral panels as a better alternative.

Paragraphs 6.1 through 6.5 of the all-neutral alternative to the Procedures provide a process for selection of an all-neutral panel. It begins with the submission by the parties of ten individuals from a designated group of candidates with a selection procedure used to reduce the candidates to three on each side, similar to that described above. If there is a common individual on each list, that person is the umpire (referred to as "chair"). Each party then selects one panel member from the other party's list. If there are two common individuals on each list, both are panelists, the chair is chosen by lot, and the remaining arbitrator is chosen by lot. If there are three common individuals on each list, all are panelists and the chair is chosen by lot. If there are no common individuals on each list, each party selects one from the other's list and the third panelist is chosen by lot with the chair chosen by lot from the first two panelists. It is believed that the number of candidates originally proposed plus the selection process will produce a neutral panel. The parties are prohibited from revealing to the panel members which party proposed them. Likewise, ex parte communications are prohibited.

#### **V. Confidentiality**

Very few arbitration clauses require the process to be confidential but most consider

confidentiality to be an implied assumption in the arbitration process. Some oppose confidentiality for “sunshine” or precedential reasons. Others oppose confidentiality so that they can share their briefs and testimony with other similarly situated parties. Many parties choose the arbitration process, in part, because of their expectation of confidentiality. Panels, almost universally, prefer a confidential proceeding but in the event of opposition from one party, may struggle with the lack of specific contractual authorization.

Paragraphs 7.1 and 7.2 of the Procedures impose confidentiality with certain well-recognized exceptions *e.g.* retrocessionaires, judicial proceedings, independent audit and laws and regulations. These exceptions are largely reflective of the exceptions contained in the ARIAS - US recommended Confidentiality Agreement<sup>4</sup> and the forms provided in the RAA Manual for the Resolution of Reinsurance Disputes.<sup>5</sup>

## **VI. Interim Relief and Sanctions**

There is little doubt that arbitration panels can issue interim rulings, such as those related to pre-answer security and discovery. However, there is greater doubt as to what sanctions are available to a panel for failure to comply. Doubt as to available sanctions makes panels hesitant to act decisively to control the arbitration.

Paragraph 8.1 of the Procedures specifically authorizes interim rulings. Sanctions for failure to comply are found in Paragraph 8.2 which include but are not limited to: “striking a claim or defense; barring evidence on an issue; drawing an adverse inference against a Party; and imposing costs, including attorneys fees, associated with such abuse or failure to comply.”

## **VII. Organizational Meeting**

Matters to be addressed at organizational meetings are well understood generally and the ARIAS - US guidelines provide a checklist and commentary thereon. Paragraph 10 of the Procedures specify the usual items to be discussed plus some which are somewhat less usual:

- revelation of the fact of *ex parte* communication plus identification of documents exchanged
- continuing obligation of disclosures by the panelists
- desire by the parties for a written rationale from the panel for the ruling on the merits

## **VIII. Summary Disposition**

Some arbitrators are hesitant to summarily dispose of issues because they are unfamiliar with the procedure, the bases therefore or the authority of the panel to make such a ruling prior to a full hearing on the merits. Nonetheless, it can be helpful to rule on issues when the material facts are not at issue so as to better focus the hearing on the merits and avoid unnecessary costs.

Paragraph 13.1 of the Procedures specifically authorizes summary disposition. In addition, Paragraph 13.2 allows ex parte summary proceedings when one side is aware of them but chooses not to participate.

## **IX. Hearing on the Merits**

Paragraph 14 of the Procedures provides a structure for the hearing. Much of this section codifies current procedure but there are some departures.

### **A. Honorable Engagement**

Paragraph 14.3 provides that the reinsurance contract is to be viewed as an honorable engagement subject to custom and practice and not to be interpreted by strict rules of law or evidence. While this is traditional language, it is not contained in all contracts. Given the increasingly legal tone of arbitrations, this provision preserves a business-oriented approach to resolution of the dispute.

### **B. Nature of Testimony**

Paragraph 14.6 allows testimony by telephone, affidavit, transcript, videotape and by other means. However, testimony that is not subject to cross examination may be permitted by the Panel only for good cause shown. This gives the panel broad discretion to consider available evidence but that discretion is balanced by the need of each party to confront adverse witnesses.

### **C. Proposed Orders**

Panels sometimes ask counsel to provide proposed orders, usually as a means of avoiding inadvertent failure to rule on a relevant issue. The proposed orders are sometimes overstated both in terms of rhetoric and findings of fact and rulings of law. Nonetheless, ¶ 14.9 requires counsel to provide proposed orders at the end of a hearing.

## **X. Award**

### **A. Types of Award Available**

Panels routinely award consequential damages for breach of contract and interest on sums due. Less routinely, they order rescission for more outrageous behavior. Some question the right to order attorneys' fees and costs as well as punitive damages. Panels are often unfamiliar with injunctive relief.

Paragraph 15.3 of the Procedures grants panels the authority to grant any remedy or sanction allowed by applicable law, in the absence of a contractual provision to the contrary. This provision specifically includes monetary damages, interest, costs, attorneys' fees and equitable relief. It

implicitly includes punitive damages where authorized by applicable law.

### **B. Reasoned Opinions**

There is considerable disagreement in the arbitration community concerning the wisdom of “reasoned opinions” *i.e.* final orders that contain a rationale for the result such as findings of fact and conclusions of law. Some believe that providing a rationale for an award provides fodder for efforts to vacate them. Others believe that the bases for vacation are so limited and the need for feedback so significant that reasoned opinions should be the rule rather than the exception. With tens of millions sometimes at stake, some rationale for a ruling can provide guidance with respect to other disputes and future behavior.

Paragraph 15.4 deals with this issue by requiring the panel to provide a rationale for its ruling only if both parties agree.

### **C. Post Hearing Communications**

Often, after a final order is handed down by the panel, counsel will seek feedback from their party arbitrator as to the basis for the award and for qualitative comments on the efforts and tactics of counsel. Commonly, the feedback is provided in general terms which do not reveal the detail of deliberations.

Paragraph 15.5 is notable in that it prohibits this communication until the parties waive their rights to challenge the award or the period to challenge the award expires. The obvious intent is to restrict challenges to an award on the merits. As noted above, the bases for challenging an award are few. Absent a written rationale for the panel’s order, this severely restricts the ability of counsel to obtain timely feedback to evaluate their own performance and the panel’s rationale for its rulings.

## **XI. Streamlined Procedures**

Some disputes are of such modest size that the costs of an arbitration pursuant to the usual procedure is prohibitive. In addition, there are some preliminary issues arbitrated (*i.e.* whether a reinsurer must pay balances before auditing or whether the cedent must allow the audit before the reinsurer is required to pay) that do not justify the time and cost involved in the standard procedures.

Paragraph 16 of the Procedures contain streamlined procedures for such matters, incorporating:

- single neutral arbitrator
- no discovery
- no evidentiary hearing - submission on briefs and documents only

· very limited time frames

## **XII. Conclusion**

The Procedures described herein are the first such to be designed specifically for insurance and reinsurance arbitrations. The major stakeholders in the process, insurers and reinsurers, domestic and foreign, their trade associations and practicing arbitrators, drafted them. To a large extent, the Procedures codify the “best practices” already in use. However, they also clarify procedures in gray areas and establish policy in some controversial ones. Perhaps most important, the Procedures provide a structure which allows the arbitration process to be more logical, more transparent and therefore more acceptable to those it means to serve.

## **ENDNOTES**

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1. A copy of the Procedures as well as guidelines for their use can be obtained from the Arbitration Task Force’s website at [www.ArbitrationTaskForce.org](http://www.ArbitrationTaskForce.org). While the Reinsurance Association of America (hereinafter “RAA”) staffed the process of creating the Procedures and participated in the drafting process, they are not “RAA Procedures.”
  2. ARIAS - US offers a very useful “Practical Guide to Reinsurance Arbitration Procedures” on its website [www.arias-us.org](http://www.arias-us.org). This guide discusses procedural issues but does not provide procedures appropriate for incorporation into reinsurance contracts.
  3. The AAA has made efforts in recent years to update their reinsurance arbitrator list. When citing this list in contract language, care should be taken to ensure that the specific reinsurance arbitrator list is used as opposed to the AAA’s general lists of arbitrators. The reinsurance arbitrator list is maintained through staff based in the AAA’s Atlanta office.
  4. *See* recommended forms at [www.arias-us.org](http://www.arias-us.org).
  5. *See* the RAA’s website for information on purchasing RAA materials at [www.reinsurance.org](http://www.reinsurance.org).