A I D A REINSURANCE & INSURANCE ARBITRATION SOCIETY

ARIAS • U.S.

ARIAS•U.S. Quarterly

Volume 3 No. 3

EX AEQUO

3rd Quarter, 1996

DON'T MISS IT!

Baltimore Seminar Set for November 1-2, 1996

Details... see page 9

Reinsurance: Statute of Limitations

New York's Six Year Statute of Limitations Does Not Bar Cedant's Recoveries

Contributed by Mound, Cotton & Wollan from their Winter 1996 Newsletter

The Second Circuit holds that New York's six-year statute of limitations for contract actions begins to run only after the cedant reports the loss and the reinsurer denies coverage. MC&W represented Continental in the case discussed below.

In our Winter 1995 issue we reported on a District Court case in which the trial court rejected reinsurers' argument that New York's six-year statute of limitations barred a cedant's action for breach of contract. Continental v. Stronghold, 866 F. Supp. 143, 145-46 (S.D.N.Y. 1995). The reinsurers appealed, but the Second Circuit affirmed. Continental v. Stronghold, 77 F.3d 16 (2d Cir. 1996).

Stronghold arose out of liability policies that Continental issued to hospitals and hospital associations, many of which were located in the New York City area. In the 1980s Continental settled and paid a series of medical malpractice claims against the hospitals but waited several years before it notified the reinsurers of these payments.

On various dates between 1987 and 1991 reinsurers refused

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Vertical Integration of U.S.Reinsurers, Means New Opportunities-Means More Competition

by Andrew Barile, CPCU

Foreign reinsurers from countries Such as Germany, Switzerland, France, United Kingdom, Japan, Australia, and Bermuda are becoming aware of vertical integration in the U.S. reinsurance business. The large American-owned reinsurance companies are all using primary owned insurers to capture more reinsurance market share. In addition, U.S. reinsurers are going global, therefore creating more competition in the world reinsurance market. This article is written with respect to the impact of vertical integration by reinsurers, i.e., new profit opportunities for specialty program agents, and more competition for existing, traditional property and casualty insurance companies.

Some foreign-owned U.S. reinsurers have been told that they cannot acquire a primary insurer, whereas others have been encouraged to form surplus lines insurance companies.

Consolidation in Reinsurance Market

Consolidation in the reinsurance market, simply stated, is whereby Christiana General Insurance Corporation of New York is merged into Folksamerica Re, also of New York, thereby reducing the number of reinsurers on the treaty reinsurance agreement. The number of reinsurers in the United States reinsurance market continues to decline based on several factors, all of which focus on the needs and philosophies of the reinsurance buyer. The buyer has demanded highly capitalized reinsurers, and, consequently, the surplus requirements continue to go higher, i.e., $10 million, $50 million, $100 million, $250 million over a 10-year time frame.

The buyer wants more than just a reinsurance program from the reinsurance market. In some instances, the buyer wants capital, and not in the form of a reinsurance product (treaty agreement). The buyer wants the capital in the form of senior subordinated debt, mezzanine financing, preferred stock—all of the terms that are familiar to investment banking firms, not reinsurance underwriters.

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Letter from E.F. Rondepierre

1996 Annual Meeting

The 1996 Annual Meeting of ARIAS US is planned for November 1st 1996. It will be held in Baltimore in conjuction with a one day seminar to be conducted on November 2nd.

At the annual meeting, there will be reports on the activities and accomplishments of the Association to date, and the work which is in progress. More importantly, this will be an opportunity for the board to hear directly from you, and for you to discuss matters of common interest with other members. We very much need your views and suggestions to carry out our plan to function as a membership association. We're hoping for a big turnout.

At this meeting, the terms of three of our nine directors will expire and their successors will be elected. As provided in the Bylaws, there will be one each representing ceding insurers, professional reinsurers, and lawyers in private practice. The Board has appointed a nominating committee, which will propose a slate of candidates. The committee is chaired by Charlie Foss, and he will welcome your suggestions. Of course, any member may nominate a candidate directly from the floor of the meeting, or by writing to the Secretary in advance of the meeting.

The November 2nd seminar will also be designed to emphasize member participation. Unlike previous ARIAS seminars, there will not be a mock arbitration. Instead, we will have experienced arbitrators, umpires, and party counsel present brief summaries of their suggestions for improving the arbitration process from their respective points of view. That will be followed by discussion groups and an open forum to provide an exchange of views and experiences of attendees. We expect to develop suggestions which can be published, or referred to existing or new committees for further study and development by ARIAS.

I look forward to seeing you in Baltimore.

E.F. Rondepierre

President

Vertical Integration of U.S.Reinsurers...

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Consolidation in Reinsurance

Fosters New Reinsurance Products

The consolidation in the reinsurance market is continuing, as buyers of reinsurance are fostering this to happen. Many ceding companies are looking to deal with fewer reinsurers who have larger reinsurance capacity and provide technical underwriting capabilities and other services. The rating agencies have also helped in fostering the consolidation on the basis of their comments that smaller reinsurers cannot survive in the future. Rating agencies, based on their financial data, have concluded that the reinsurance market will be made up of a handful of direct-writing reinsurers, and a group of highly capitalized broker market reinsurers.

Larger, well-capitalized reinsurers are now in a position to analyze the reinsurance requirements of the ceding insurance company. The traditional reinsurance products of (1) quota share, (2) surplus share, (3) per risk excess, (4) catastrophe cover, and (5) aggregate excess are still valued today, and are used as a starting point in describing an insurance company's reinsurance program. In fact, insurance agents and brokers have learned dramatically that their very agency appointment becomes predicated on their insurers' ability to purchase reinsurance. Agents should understand how insurers buy reinsurance.

From the traditional reinsurance products, there have emerged new reinsurance products. Quota Share treaties, with the introduction of franchise loss deductibles, loss corridors, and occurrence caps have been transferred into finite risk types of quota share agreements. Catastrophe reinsurance agreements, that were also very traditional, have been expanded from one-year to five-year covers, from no profit sharing to profit contingents, from fixed retentions to moving retentions, from one reinstatement to unlimited reinstatements, from open limits of protection, to a finite dollar limit of catastrophe reinsurance. Some of the latest reinsurance products are created by the reinsurance buyer who starts with the necessary reinsurance problem. More reinsurers are focused on what are the specific problems of the ceding insurance company, and what types of new reinsurance products have been created to solve these problems.

Reinsurance buyers are looking at actuarial projections, catastrophe modeling, three-year proformas, earthquake zones, how to better manage the purchase and implementation of their reinsurance program. Reinsurance buying has become a team effort within a ceding insurance company. More reinsurance buyers will act like corporate risk buyers in the future. The larger reinsurer will be in a better position to take advantage of this changing buying philosophy.

Vertical Integration in Reinsurance

Almost all of the large professional reinsurance groups now have within their financial holding company family an admitted and a non-admitted primary insurer. The initial thrust of these primary insurers, owned by reinsurers, was to write direct excess workers' compensation. Then they branched out into surplus lines insurance. Today, they have expanded into the alternative risk transfer market, such as using primary insurers to "front" captive insurance companies or risk purchasing groups. Primary insurers, owned by reinsurers, are now expanding into specialty niche programs and search for controlled books of business, making sure that they are not competing with their ceding insurance company clients.

Reinsurers are cross training their traditional treaty reinsurance underwriter to be able to select and underwrite a potentially profitable specialty insurance program. Vertical integration has helped reinsurance underwriters to better understand their clients' problems since reinsurers now see, first hand, the problems of getting a rate filing approved by state regulators, or how much time and effort goes into changing policy forms.

Who will have access to the reinsurance opportunities created by the primary insurer of the reinsurance group? Will the primary insurer be able to negotiate its own reinsurance program, or will its reinsurance program be written by the group's reinsurer? How does that affect the brokers and agents, program administrators, and general agents doing business with the primary insurer owned by the reinsurer?

Another form of vertical integration occurring in reinsurance involves reinsurers providing capital funds to their ceding insurance company clients, risk retention groups, agent-owned captives, etc. Better capitalized reinsurers have the funds to invest. What about the new development?

Impact on Intermediaries

Despite the consolidation in the number of reinsurance broker company markets, reinsurance brokerage revenues have not declined, nor has profitability. The reinsurance intermediary ownership is still under the guise of large primary insurance brokerage firms. The selection process for the appropriate reinsurance intermediary to serve the Florida JUA is common to what is going on in the industry. Reinsurance intermediaries, in this case were selected on the basis of (1) financial strength of the reinsurance intermediary, (2) intermediary company size, (3) the diversity of their client base, (4) reinsurance company market access, and (5) intermediary's experience with the kinds of risk the Florida JUA is looking to reinsure.

Greater Selectivity

Many reinsurance intermediaries have now started consulting firms and have had to expand their services to ceding insurance companies to include catastrophe modeling, reinsurance program design, tax preparation, and actuarial services. Some of the larger intermediaries that have access to capital are now offering capital to their client insurance companies.

In regard to vertical integration by reinsurers, reinsurance intermediaries will also seek out specialty niche insurance programs for the primary insurers owned by reinsurers. Many of these insurance programs are reinsured within the same reinsurance group. Therefore, reinsurers are creating their own reinsurance opportunities.

In the future, reinsurance intermediaries will provide their ceding insurance company clients with various types of strategies to help their clients enhance profitability, i.e. human resource search, technological development, marketing strategies, investment advice, and merger and acquisition techniques.

Impact on Specialty Niche Program Administrators

Retail insurance agents and brokers, wholesalers, general agents, and managing general agents, having created

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The Role of Foreign Insurers in Transition Economies and Developing Countries

(Remarks by Harold D. Skipper, Jr., Professor of Risk Management and Insurance, Georgia State University, Atlanta, Georgia/USA, for the 13 November 1995 meeting of the Standing Committee on Developing Services Sectors of the United Nations Conference on Trade and Development, Geneva, Switzerland)

Mr. Chairman, distinguished delegates, ladies and gentlemen. I am pleased to have the opportunity to speak with you on "The Role of Foreign Insurers in Transition Economies and Developing Countries." My remarks are personal and should not be ascribed either to the UNCTAD or to Georgia State University. They are extracted from a study underway at GSU in Atlanta which examines the economic arguments for and against greater foreign participation in insurance markets.

My remarks are oriented primarily towards the direct insurance market and towards foreign insurer involvement via foreign direct investment as contrasted with cross-border trade. I will not address cross-border trade issues. My use of the term, "foreign insurer," therefore, is technically and legally incorrect in most instances, but it is useful shorthand. A foreign-owned, locally incorporated insurance company, after all, is a domestic insurer. It must comply fully with all domestic laws and regulations. It must pay taxes as any other insurer. The only substantive difference between it and any other domestic insurer is its ownership. A national insurance market composed mostly of foreign-owned insurers is no less national than one without foreign-owned insurers.

As many in this room know, some policymakers believe that foreign insurers should play but a limited, if any, role within their markets. This opinion once was shared by the great majority of states. The number of its proponents today continues to shrink as policymakers increasingly embrace the liberal market model as offering better opportunities for economic growth.

Of course, all countries acknowledge that foreign reinsurers have an essential role to play in their markets, although some governments limit this role in various ways. And policymakers generally recognize the need for some foreign involvement, either directly or indirectly, in insuring complex industrial MAT and infra structural risks. Beyond these areas, however, some governments prohibit foreign insurer establishment altogether, limit ownership shares, or inhibit market access through other means. Even governments with officially liberal market access rules may tolerate national treatment inconsistencies.

In 1964, the UNCTAD pronounced that "a sound national insurance and reinsurance market is an essential characteristic of economic growth." This 31-year-old quote probably is the only formal acknowledgment by the UN that insurance is important, and even it fails to do justice to the role of insurance in economic development. Insurance is not merely a "characteristic of economic growth." It is a necessity for the great majority of today's economies. Regrettably, the precise linkages between insurance and economic development are poorly understood. In-depth research on this issue is sparse and largely anecdotal, unlike the situation with banks which enjoy by comparison a substantial body of supportive research. Not surprisingly, therefore, the role and importance of insurance in economic development goes largely unappreciated by policymakers, and, I fear, increasingly so within the UN family.

In thinking about the role of foreign insurers in domestic insurance markets, it is useful to examine the role of financial intermediaries generally to economic development and to inquire whether foreign insurers could contribute. For if they cannot or will not contribute in some way to economic development, we may legitimately question their relevance for transition economies and developing countries. The converse also

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Reprinted from the International Insurance Monitor, 2nd Quarter, 1996

Vertical Integration of U.S.Reinsurers...

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efit from seeking out these new insurance company markets. Reinsurers not obtaining enough opportunities to provide reinsurance in these areas of the business have capitalized primary insurers to seek out new niche programs, whether they be in personal lines or commercial lines. For the future this is a very important change occurring in the distribution system whereby agents access reinsurers without the need for an agency captive.

Conclusion

As the competitive market continues, there wilt be more consolidations in reinsurance so that in the future buyers of reinsurance will have fewer options when searching for a reinsurer. Reinsurance intermediaries also will have fewer reinsurers on a treaty.

Vertical integration will continue with more reinsurers accessing primary insurance companies when looking to expand. All reinsurers will own specifically admitted and non-admitted insurance companies. Specialty niche insurance program administrators will be in a good position to access these new primary insurers and provide them with complete niche insurance program concepts, production, underwriting, policy issuance, accounting, and statistical reporting, including claims handling.

The Role of Foreign Insurers...

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applies.

Insurance aids economic development through its financial intermediation function in at least four ways.

First and most obvious, insurance facilitates trade and commerce. Modern economies are built on specialization and its inherent productivity improvements. Greater trade and commercial specialization demand, in turn, greater financial specialization and flexibility. Without a wide insurance product choice and without constant service and pricing innovations, insurance inadequacies can stifle both trade and commerce. Multinational insurers often enjoy a reputation as market innovators.

Second, insurance mobilizes national savings. Countries that save more tend to grow faster. Of the world's 20 fastest growing economies over the preceding 10 years, 14 had savings rates greater than 25 percent of GDP, and none had a saving rate of less than 18 percent. By contrast, 14 of the 20 slowest growing countries had savings rates below 15 percent.

Insurers offer the same advantages as other financial intermediaries in channeling domestic savings into domestic investment. The nationality of the owners of domestic insurers is largely irrelevant to this channeling function. Life insurers and other contractual savings institutions can be especially important for developing countries. In contrast with commercial banks which specialize in collecting short-term deposits and extending short-term credit, contractual savings institutions take a longer-term view. Their long-term liabilities and stable cash flow are ideal sources of term finance for government and business.

Locally incorporated foreign-owned insurers could bring additional and possibly innovative marketing and product competition to the national market. This can deepen and broaden the domestic financial services marketplace. Research on the determinants of national savings suggests that such market strengthening is associated with higher saving rates and, hence, greater economic development.

Third, insurers provide risk management services. By this, I am not limiting myself to that which insurance executives typically think of as risk management. Rather, I refer to the functions of risk pricing, risk transformation, risk pooling and risk reduction performed by all financial intermediaries. These functions are too seldom discussed in an insurance context but appear often in the banking literature. I mention each briefly.

A competitive market's success depends on pricing. Insurers price risk through their underwriting and investment activities. Business owners and managers, potential investors, creditors, employees, and other stakeholders can use these risk pricing signals to make better informed decisions, thus enhancing national economic efficiency. Foreign insurers often are particularly good at risk pricing.

Insurance also permits businesses and individuals to transform many of their property, liability, loss of income and other risk exposures to suit their own needs better. Moreover, life insurers help individuals and businesses transform the characteristics of their savings to the liquidity, security and other risk profiles desired. To the extent that foreign insurers bring additional capacity to a market, they facilitate this risk transformation activity.

The third risk management function performed by insurers is risk pooling. It lies at the heart of the insurance mechanism. Pooling occurs both in underwriting and in investment. Pooling reduces volatility. By reducing volatility, a smaller "risk premium" can be assessed insureds and borrowers. As foreign-owned insurers often are part of much larger multinational insurance groups, their risk pooling activities might be particularly helpful, thus offering the potential for greater pricing and investment stability.

Risk reduction, the fourth risk management element, occurs because insurers have economic incentives to help insureds reduce losses. Foreign insurers sometimes can bring state-of-the-art loss mitigation services to markets.

Locally incorporated foreign-owned insurers could bring additional and possibly innovative marketing and product competition to the national market.

The fourth benefit of insurance to economic development is that insurers foster a more efficient allocation of a country's capital. They gather substantial information to conduct their evaluations of firms, projects and mangers both in deciding whether to issue insurance and in their roles as lenders and investors. Individual savers and investors typically do not have the time, resources or ability to undertake this information gathering and processing. Financial intermediaries, including insurers, have an advantage in this regard.

In making such investment and insurance decisions, insurers tangibly signal the market's approval of promising, well-managed firms and projects and thereby foster a more efficient allocation of a country's scarce financial capital and insurance bearing capacity. Foreign insurers often can bring innovative and more efficient means of gathering and evaluating information, thus aiding in capital allocation.

Therefore, based on the means by which insurance underpins economic development, the conclusion is that foreign insurers have a potentially constructive role to play in the insurance market of transition economies and developing countries.

In our study, we examine the means by which foreign insurers might actualize their contributions to economic development. We also examine the arguments as to why countries might be wise either to go slow in market liberalization or to limit foreign involvement in their insurance markets. Briefly, the specific arguments favoring greater foreign insurer participation are that countries could realize one or more of the following benefits:

- improvements in customer service and value

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The Role of Foreign Insurers...

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- increased domestic savings
- transfers of technological and managerial knowhow
- additional external financial capital
- improvements in the quality of insurance regulation
- beneficial domestic spillovers, including the addition of more and higher quality jobs, quality enhancing backward and forward linkages, and societal loss reductions.

Each of these arguments was examined, relying primarily on existing banking and related research and on available anecdotal evidence. Except for one argument, they were assessed as constituting reasonable expectations for transition economies and developing countries. The FDI accompanying foreign insurer establishment was assessed as being less important to development than the other items.

Policymakers have expressed numerous reservations about foreign insurer participation in their domestic markets. We classified all reservations around seven common themes. We could find no factual basis for five of the themes or believe that the associated issues can be addressed more adequately and with less consumer loss through alternative means. The validity and importance of a sixth theme cannot be established a priori. The seventh reservation theme we judged to warrant policymaker concern.

The five classes of reservations either lacking factual justification or for which more efficient, viable alternatives exist are as follows:

• First, foreign insurers might dominate the domestic market and thereby precipitate adverse microeconomic (less consumer choice and value) or macroeconomic (failure to contribute adequately to economic development) effects. If a market offers great potential and if domestic insurers are inadequate and unsophisticated, market liberalization could lead to foreign domination. In such a case, however, no rational basis exists to support a parallel belief that the nation's consumers and businesses will suffer harm or that the national economy will be harmed. On the contrary, that the market offered great potential, was unsophisticated, and had an inadequate capacity suggests that the status quo was stifling microeconomic and macroeconomic improvements.

• The second reservation class for which factual justification is lacking or for which more efficient means exist to address the concern than denial of market access is that foreign insurers might market insurance selectively, thereby leading to adverse microeconomic or macroeconomic effects. (This selectivity may be because of concern that foreign insurers will market insurance only to the most profitable segments, only to multinational corporations or only to the commercial sector, ignoring the retail market.) Governmental efforts to discourage selective marketing can be harmful. Specialization and market segmentation lead to efficiency improvements, as suggested earlier. It is true that segmentation could cause some market segments to be under served. If it does and if these under served segments are judged critical, government policymakers would be wise first to examine whether repressive regulation (such as price suppression) was at fault. If not, insurers can be enticed into neglected segments through less distorting subsidies or other positive means.

• The third class of reservations is that foreign insurers might fail to make lasting contributions to the local economy. We could find no reasonable factual basis to support this belief.

• The fourth class of arguments for limiting foreign insurer market access is that the domestic market is already well-served by locally owned insurers or through reinsurance. We could find no reasonable factual basis to support this belief.

• The fifth reservation category is that the national industry should remain locally owned for strategic reasons, such as national security concerns or because of the desire for economic diversification. To the extent that these goals are valid and not driven by special interests less market-distorting means exist for accomplishing them than limits on foreign insurer participation.

The sixth reservation class is that foreign insurers may provoke a greater foreign exchange outflow. The validity of this concern cannot be ascertained a priori. Over the short-term, of course, foreign exchange would flow into the country. But more importantly, as an UNCTAD study noted: "(any) loss of foreign exchange may not be substantial enough to justify the opportunity cost involved in running and upgrading national insurance corporations."

The final reservation relates to the belief that full market liberalization should await insurance and possible macroeconomic regulatory reforms so as to minimize the chances of micro- or macroeconomic disruptions. This concern is valid in certain situations, particularly regarding adequate prudential supervision. Reasonable insurance laws and regulation are essential. Ideally, they should exist prior to full market liberalization to avoid abuse by the unscrupulous. At the same time, we acknowledge that if market access could somehow be limited to those multinational insurers that enjoy reputations for honesty and integrity, the issue would be less critical. The challenge for regulators, of course, is determining how and where they should draw the line between acceptable and unacceptable insurers.

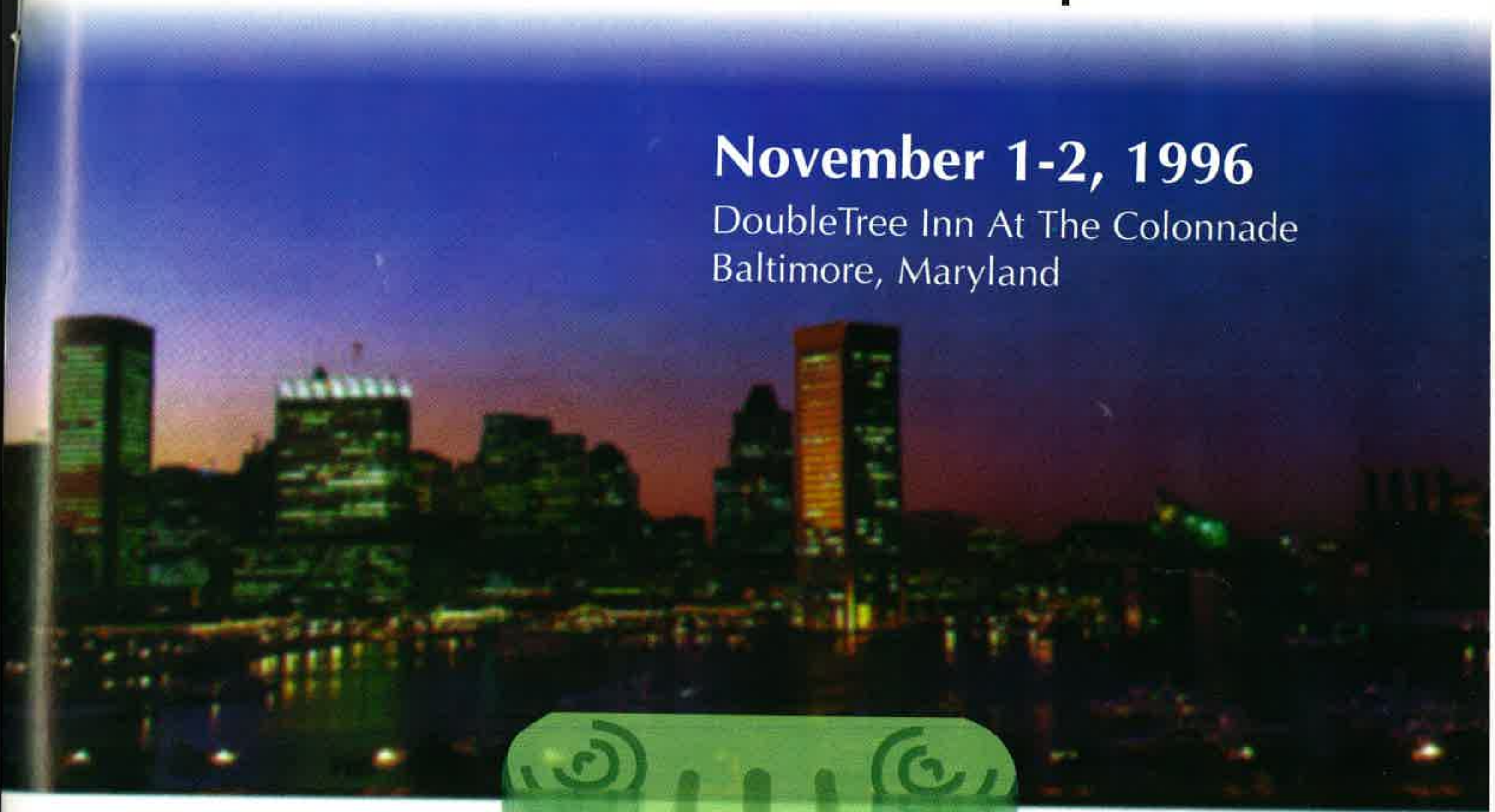
This then has been an overview of the key areas of our study. On balance, we conclude that opening insurance markets to appropriate foreign insurers is likely to aid economic development, enhance overall social welfare, and carry few unresolvable negative possibilities. Countries that maintain unjustifiable market access barriers and that fail to extend national treatment to foreign-owned insurers likely are doing their citizens, businesses and national economy a disservice.

Thank you, Mr. Chairman.

13 November 1995
Geneva, Switzerland

ARIAS • U.S.
5th Seminar

ARIAS • U.S. Reinsurance Arbitration Workshop



November 1-2, 1996

DoubleTree Inn At The Colonnade
Baltimore, Maryland

AIDA Reinsurance & Insurance Arbitration Society
PO Box 9001 ▲ Mt. Vernon, NY 10552
1▲800▲951▲2020

ARIAS · U.S.

An Invitation

ARIAS•US will hold its fifth arbitration workshop on November 1-2, 1996 at the elegant DoubleTree Inn at the Colonnade in Baltimore, Maryland.

The November 2nd seminar is designed to emphasize member participation. Unlike previous ARIAS seminars, there will **not** be a mock arbitration. Instead, we will have experienced arbitrators, umpires, and party counsel present brief summaries of their suggestions for improving the arbitration process from their respective points of view. That will be followed by discussion groups and an open forum to provide an exchange of views and experiences of attendees. We expect that to develop suggestions which can be published, or referred to existing or new committees for further study and development by ARIAS•U.S.

ARIAS U.S., this workshop's sponsoring organization, is a non-partisan, not-for-profit corporation, dedicated to the improvement of reinsurance arbitration in both the domestic and international markets. Its sister organizations, ARIAS (U.K.) and C.A.R.E.A. in France, have been active in training and certifying qualified reinsurance arbitrators and umpires. Like its counterparts, ARIAS U.S. aims to provide a service to the reinsurance industry by certifying a pool of insurance/reinsurance arbitrators and umpires.

Preliminary criteria established by the Board of Directors for merit evaluation of candidates for certification include experience in the insurance and/or reinsurance industry or as a private lawyer in the field of insurance and reinsurance law; letters of reference attesting to the individual's personal and professional character and fitness, and participation in ARIAS U.S. sponsored workshops/training sessions.

While the November, 1996 seminar is one of the integral parts of the certification process, the Board of Directors of ARIAS U.S. also welcomes the attendance of those individuals who wish to learn more about arbitration, but who do not necessarily wish to attain certification.

Please return the enclosed application at your earliest convenience.

We look forward to seeing you in Baltimore.

Charles W. Havens, III ▲ Program Chair

ARIAS·U.S.

ARIAS•US Objectives

The following are the objectives of ARIAS • U.S.

1. To promote the integrity of the arbitration process in insurance and reinsurance disputes.

2. To promote just awards in accordance with industry practices and procedures.

3. To certify objectively qualified and experienced individuals to serve as arbitrators.

4. To provide required training sessions for those persons certified as arbitrators.

5. To propose model rules of arbitration proceedings and model arbitration clauses.

6. To foster the development of arbitration law and practice
as a means of resolving national and international insurance and reinsurance disputes in an efficient, economical and just manner.

Panel Presentation

A panel presentation by four distinguished arbitrators on a series of questions on the hottest topics.

Each panelist will respond and then take questions from the audience. The panel will draw on the experience of the panelists while involving the audience in the key elements of an arbitration, e.g., selection of the umpire, the first meeting, appropriate discovery, the hearing, power and discretion of the panel, and "does the panel look over its shoulder in anticipation of the parties actions" or "how a court will look at their decision."

Certification

Ed Rondepierre and *Charles Foss* will review the process for Certification by ARIAS with q's and a's.

Forms & Procedures

Mark Gurevitz will present "What ARIAS Can Do in Proposing Suggested Forms and Procedures to be Used in Arbitrations."

Judicial Involvement

"The Proper Role of Judicial Involvement in a Reinsurance Arbitration from Judicial Review of Interlocutory Panel Actions to Confirming or Vacating Final Awards."

Featured Speaker

The Luncheon speaker is the *Honorable Fred Lacy*, formerly U.S. Attorney for New Jersey, formerly U.S. District Court Judge in New Jersey and now in private practice as a partner in the Newark office of LeBoeuf, Lamb, Greene & Macrae. *Judge Lacy* will present another view of arbitration from the perspective of a former judge, now an arbitrator.

Friday, November 1, 1996

Afternoon Session

1:30 - 6:00	Arrival/Registration
2:00	ARIAS•US Annual Meeting
4:00	ARIAS•US Board Meeting (members invited)
6:00 - 7:30	Cocktail Reception

Dinner on Own

Saturday, November 2, 1996

Morning Session

7:30 - 8:00	Continental Breakfast / Registration
8:00 - 8:30	Program Overview: Mr. Havens
9:00 - 10:15	**Panel:** Mr. William Gilmartin, Mr. Caleb Fowler and others
10:15- 10:30	Refreshment Break
10:30 - 11:00:	**Certifications by ARIAS•US** Q&A: Mr. Rondepierre, Mr. Foss
11:00 - 11:30	**Forms & Procedures:** Mr. Gurevitz
11:30 - Noon	"The Proper Role of **Judicial Involvement** in a Reinsurance Arbitration from Judicial Review of Interlocutory Panel Actions to Confirming or Vacating Final Awards."
10:45 - 12:00	Q&A re: selection process
12:00 - 1:30	Luncheon: **Featured Presentation** Hon. Fred Lacy

ARIAS·U.S.

General Information

ARIAS•U.S. Reinsurance Arbitration Workshop
DoubleTree Inn, November 1-2, 1996

Hotel:

ARIAS•US has made special arrangements for attendees with the DoubleTree Inn At The Colonnade, Baltimore.

Call the DoubleTree Inn at 410•235-5400 and refer to ARIAS•U.S. in making your reservation.

Fees:

Registration fees (see below) include all materials, cocktail reception on Friday, November 1st, continental breakfasts, lunch and all coffee breaks on Saturday.

Spousal fee is $50, and includes cocktail reception, breakfast and luncheon.

Not included: Travel, Lodging, Dinner Friday evening.

Certificates of attendance will be provided two weeks after completion of the sessions.

Reservation Form

Name ______________________________

Name for Badge ______________________________

Firm ______________________________

Address ______________________________

City ______________________ State ____________ Zip ____________

Phone ______________________ Fax ______________________

Spouse Name ______________________________

Please send registration fee by October 18, 1996.
▲ Members: $265.
▲ Non Members: $350.

❑ Non Member Registration Fee of $350 is enclosed.

❑ Member Registration Fee of $265 is enclosed.

❑ Spousal Fee of $50 is enclosed.

❑ I will be attending the luncheon on Saturday (Reservations strictly required)

❑ I am a member of ARIAS•US ❑ Individual ❑ Corporate

❑ Please send me a membership application.

Total Amount Enclosed: $ ______________________________

phone: 800-951-2020

Mail with your check for registration to:
AIDA Reinsurance & Insurance Arbitration Society
ARIAS•U.S. Arbitration Seminar
c/o Chase Communications ▲ PO Box 9001 ▲ Mt. Vernon, NY 10552

ARIAS·U.S.

Six Year Statute... *Continued from page 1*

to pay and denied liability. In November 1991 Continental brought suit against them in the Southern District of New York. The reinsurers filed answers, denied the allegations, and raised a late notice defense.

In 1992 the New York Court of Appeals held in an unrelated case that in order to succeed on a late notice defense a reinsurer must establish that it has been prejudiced by any delay in reporting the underlying loss. Unigard Sec. Ins. Co. v North River Ins. Co., 584 N.Y.S.2d 290 (1992); MC&W Newsletter, Fall 1993. As Circuit Judge McLaughlin put it in the Stronghold case, "undermine[d]" the reinsurers' late notice defense. 77 F.3d at 18. The reinsurers would have to prove that they were in fact harmed in some way by Continental's delay in reporting the losses.

After Unigard was decided, the parties entered into a stipulation. The reinsurers agreed that they would move in the district court for summary judgment on the ground that Continental's suit was time-barred. The reinsurers waived all other defenses, including late notice. The parties also agreed on the amounts due Continental and further agreed that if the district court held that the claims were timely, the reinsurers would pay these amounts.

The district court rejected the reinsurers' argument that the New York statute of limitations began to run when Continental first paid its policyholders. The trial court held instead that the six-year limitations period began to run "at the moment the reinsurers declined to pay the insurer's' claim under the reinsurance contract." Continental v. Stronghold, 866 F.Supp. 143, 145-46 (S.D.N.Y. 1995).

By the time the District Court rendered its decision, three of Continental's reinsurers were insolvent. The insolvent U.K. reinsurers obtained stays of all litigation against them in the U.S. pursuant to Section 304 of the Bankruptcy Code. The remaining reinsurers moved for entry of final judgment and then appealed the District Court decision to the Second Circuit.

Second Circuit

On appeal the reinsurers argued again that New York's six-year statute of limitations for contract actions, N.Y. CPLR 213(2), began to run when Continental settled and paid the malpractice claims covered by its underlying policies. Continental responded that a contract cause of action could not arise until its reinsurance contracts were breached. Continental insisted that the breach could not occur, and Continental could not commence an action against its reinsurers, until the reinsurers told Continental they would not indemnify it.

Judge McLaughlin began the Court's analysis by observing that under New York law "the statute of limitations 'begins to run once a cause of action accrues.'" 77 F.3d at 19. Reinsurance agreements are a particular kind of contract, i.e., contacts for indemnity against loss, but they are still contracts. The parties to primary insurance contracts may agree on conditions precedent to suit, such as filing a proof of loss or allowing the company time to investigate the claim.

A rule has evolved in New York that the insurer on a primary policy is not obligated to pay, and no action can be commenced against the company, until the claim becomes "due and payable." The Court in Stronghold saw "no reason not to apply the due and payable insurance rule to reinsurance policies." In the Court's view, the "timeliness of Continental's claims thus turn(ed) on a fairly simple question: when were its losses due and payable under the reinsurance policies?" 77 F.3d at 20.

Turning to the reinsurance contracts, Judge McLaughlin, formerly Dean of Fordham Law School, could not resist observing that the "representative [reinsurance] policy offered by the parties [was] hardly a paragon of clarity." The court could deduce, however, that Continental had to satisfy at least one condition before demanding payment from its reinsurers. Continental had to report any loss "as soon as possible."

The reinsurance contract in Stronghold provided that the reinsurers were liable to pay only for excess of loss over specified amounts of Continental's "ultimate net loss." The court read the contract's notice provisions to mean that Continental had to report any "actual losses" or payments on the underlying policies within a reasonable period of time under the circumstances. The court went further and concluded that Continental was entitled "indeed probably obligated — to wait a reasonable time for the reinsurers to decide whether they would pay or not and, if so, how much." 77 F.3d at 20.

> ***A rule has evolved in New York that the insurer on a primary policy is not obligated to pay, and no action can be commenced against the company, until the claim becomes "due and payable."***

The court found that the Unigard decision was consistent with this holding. In Unigard the New York Court of Appeals held that unlike policies of ordinary insurance, where a delay of a few weeks may cost a policyholder his coverage, a reinsurer had to show prejudice arising from any delay in reporting a claim. Unigard did not decide when the reinsured's "actual" losses were due and payable, but it would "distort Unigard" if the court held that the reinsurers had a duty to indemnify Continental before Continental even gave notice of payments it had made.

The reinsurers argued that this gave the cedant the power to put off indefinitely the running of the statute. The court held, however, that while Continental could not "unreasonably delay reporting these losses to its reinsurer," the reinsurers had essentially conceded that there had been no unreasonable delay when they abandoned their late notice defense.

Conclusion

The court summed up its holding:

> Consistent with longstanding New York precedent, we hold that, on these facts, Continental's losses were due and payable, and its causes of action accrued, only after it reported the losses to the reinsurers, and the reinsurers denied coverage.

77 F.3d at 22. The court also observed that Stronghold may reveal how notions of custom and practice in the reinsurance industry are changing.

The court doubted that even a decade ago a reinsurer would be pressing a statute of limitations defense in a litigated reinsurance dispute. "Custom and usage (had) established a gentility and unity of interest between the reinsured and its reinsurer." Perhaps, Judge McLaughlin concluded, times have changed. With tongue in cheek he quoted the French poet Francois Villon, who asked: "Ou sont les nieges d'antan? ('Where are the snows of yesteryear?')." 77 F.3d at 22.

Ninth Circuit Retreats from View that Follows the Settlements Doctrine is Inherent in Reinsurance Contracts

Submitted by Grais & Phillips LLP

Changing course yet again, the United States Court of Appeals for the Ninth Circuit has withdrawn its widely criticized opinion of last year that the follow the settlements doctrine is inherent in all reinsurance contracts, even those that lack any follow the settlements (or follow the fortunes) clause. The court has now remanded the case for trial, conceding that it erred previously in affirming summary judgment for the cedent. National American Insurance Co. v. Certain Underwriters at Lloyd's London, No. 94-55047 (August 15, 1996).

As discussed in detail in our 1995 in Review, this longstanding coverage dispute between National American and its reinsurers, Underwriters at Lloyd's, concerns the wisdom of National American's settlement with its insured, Hughes Aircraft, of environmental claims under two policies of liability insurance. Because the facultative certificates the Underwriters issued to National American contain no follow the settlements (or follow the fortunes) clauses, the Underwriters argued they should be free to contest whether Hughes's claims were covered under National American's policies. Applying California law, both the district court and the Ninth Circuit initially rejected this argument, granted summary judgment to National American, and held that the follow the settlements doctrine is inherent in all reinsurance contracts. The Ninth Circuit based this holding in part on National American's expert testimony, which the court stated was uncontradicted by the Underwriters, and in part on two decisions from jurisdictions other than California. The court ignored contrary decisions (including a 1920 decision of the California Supreme Court) suggesting that in the absence of an express agreement to the contrary, a reinsurer may contest coverage of a settled claim.

The court's conclusion that the follow the settlements doctrine is inherent in all reinsurance contracts provoked immediate criticism, not only by the Underwriters themselves, who moved for rehearing, but also by several commentators. In August 1995 the court amended its opinion, deleting any reference to case law in support of its controversial conclusion, and basing it instead exclusively on the highly unusual failure of the Underwriters to counter National American's expert testimony. In February 1996, in response to continued criticism, the court ordered supplemental briefing on whether the '"follow the settlements' doctrine applies as a tacit part of every reinsurance agreement. . . ." (It is the court's amended opinion of August 1995 that has now been withdrawn.)

In its latest opinion, the Ninth Circuit has belatedly recognized, and ostensibly accepted, that under California law a reinsurer is allowed to contest coverage questions settled by its cedent in the absence of an express agreement to the contrary in the reinsurance contract. The court stopped short of actually applying that rule, however, deciding instead that it did not "preclude," and might be "overcome" by, evidence of a custom in the reinsurance industry that reinsurers follow the settlements of cedents. The court has now remanded the case for a trial on this issue.

In allowing evidence of custom to be presented at the trial on remand, the court struggled to reject the well-known principle that such evidence generally cannot overcome a contrary rule of law. The court failed to recognize that the rule of law urged by the Underwriters (which dates back to the nineteenth century) is flatly inconsistent with National American's evidence of custom, and that the real issue in the case is whether the old common-law rule should stand or be changed. By obscuring this issue and elevating evidence of custom to such an extent, the court has done little to clarify the deeply-muddled state of reinsurance law. Instead, its approach encourages expert-intensive (and expensive) litigation to determine whether a particular custom, practice, or usage exists. Both cedents and reinsurers would be better served by more definite rules that enable them to know their legal situations more clearly in advance.

ARIAS•U.S. invites guest articles and encourages you to share your opinions. Fax to : (914) 699-2025

ARIAS•U.S. Certification Procedures

At its first Annual Meeting, the Membership of ARIAS•U.S. approved proposed Certification of Arbitrators procedures.

We present them in full:

ARIAS•U.S.

CERTIFICATION OF ARBITRATORS

1. **GENERAL STATEMENT**

   ARIAS•U.S. seeks to certify for its members' use knowledgeable and reputable professionals for service as panel members in industry arbitrations.

2. **CRITERIA FOR CERTIFICATION**

   As a minimum of consideration, each candidate should:

   a. **Industry experience** – have at least ten years of significant specialization in the insurance/reinsurance industry. This specialized experience can be obtained with insurance and reinsurance companies and brokers or with accounting, actuarial, consulting, law, loss adjusting firms or government service, or any combination thereof.

   b. **Arbitration experience** – have completed at least one ARIAS•U.S. seminar or workshop and two other seminars/workshops and/or insurance/reinsurance arbitrations as arbitrator or umpire for a total of at least three seminars/workshops or arbitrations within two years preceding the date the completed application is received by ARIAS•U.S. Attendance at a foreign ARIAS seminar or workshop (U.K., France, etc.) would be acceptable for these purposes.

   c. **Membership in ARIAS•U.S.** – be an individual member of ARIAS•U.S.

   d. **Sponsors** – be sponsored in writing by a person who satisfies the foregoing criteria for certification. Either the sponsor or the candidate for certification can initiate the certification process by requesting a pre-application letter from the Board of Directors. Besides issuing the sponsoring letter, the sponsor should also arrange for two seconding letters from persons who satisfy the same criteria. Upon receipt of satisfactory sponsor and seconding letter, ARIAS•U.S. will mail an application to the candidate.

   ARIAS•U.S. certification is available to all candidates regardless of geographic location.

3. **CERTIFICATION DETERMINATION**

   a. After receiving completed applications together with sponsor and seconding letter from the Administrator of ARIAS•U.S., and any other information deemed appropriate by the Board of Directors, the Board, in its sole judgment and absolute discretion, will evaluate each application and determine certification in light of the above criteria. Any dispute with respect to such determination shall be resolved by binding arbitration in accordance with the By-laws of ARIAS•U.S.

   b. Certification of a candidate requires the affirmative vote of at least two-thirds of the full membership of the Board of Directors.

   c. A copyrighted list of certified arbitrators will be maintained by ARIAS•U.S. for use by its members and shall not be published or distributed outside of the membership.

ARIAS•U.S. Objectives

The following are the objectives of ARIAS • U.S.

1. To promote the integrity of the arbitration process in insurance and reinsurance disputes.

2. To promote just awards in accordance with industry practices and procedures.

3. To certify objectively qualified and experienced individuals to serve as arbitrators.

4. To provide required training sessions for those persons certified as arbitrators.

5. To propose model rules of arbitration proceedings and model arbitration clauses.

6. To foster the development of arbitration law and practice as a means of resolving national and international insurance and reinsurance disputes in an efficient, economical and just manner.

ARIAS • U.S.

continued on page 14

Certification Programs continued from page 13

4. **APPLICATION FOR CERTIFICATION**

The application for certification must be on forms provided by ARIAS•U.S. and will contain the following information:

a. name, address, telephone and fax, home and office.

b. present and prior business affiliations.

c. number of **completed** insurance/reinsurance arbitrations as arbitrator or umpire and related information including, with respect to the three most recently completed arbitrations, the names of the other arbitrators and the date of completion.

d. number of **completed** insurance/reinsurance arbitrations as outside counsel and related information including, with respect to the three most recently completed arbitrations, the names of the arbitrators and the date of completion.

e. areas of specialty.

f. number of years of industry experience as defined in 2.a., above.

g. education – college and graduate.

h. work and military history.

i. licenses, professional associations.

j. ARIAS seminars and workshops attended.

k. criminal convictions/disciplinary rulings.

l. statement by applicant that he/she will agree to abide by the By-laws of ARIAS•U.S., including the provisions covering arbitration of disputes; that the information provided is subject to verification; and that the applicant agrees that the information is accurate to the best of his/her knowledge, information and belief.

m. other information as determined by the Board of Directors.

5. **MAINTENANCE OF CERTIFICATION**

In order to maintain certification, an individual must:

a. have attended or participated in at least one ARIAS seminar or workshop within the two years immediately preceding recertification.

b. maintain membership in ARIAS•U.S.

c. apply bi-annually for certification on forms provided by ARIAS•U.S.

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To Join ARIAS•U.S.:
Use the form provided on page 15

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Membership Application

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- Training and certifying individuals qualified to serve as arbitrators and/or umpires by virtue of their experience, good character and participation at ARIAS•U.S. sponsored training sessions;
- Empowering its members to access certified arbitrators/umpires and to provide input into developing efficient economical and just methods of arbitration; and
- Providing model arbitration clauses and rules of arbitration.

Membership is open to law firms, corporations and individuals interested in helping to achieve the goals of the Society.

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Annual Dues:	$250.00	$750.00
Total	$750.00 ☐	$2,250.00 ☐

Amount Enclosed: $__________

Return this application with check for Initial Fee and Annual Dues to:

ARIAS•U.S. Membership Committee
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