

QUARTERLY

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EDITORIAL POLICY — ARIAS-U.S. welcomes manuscripts of original articles, book reviews, comments, and case notes from our members dealing with current and emerging issues in the field of insurance and reinsurance arbitration and dispute resolution. All contributions must be double-spaced electronic files in Microsoft Word or rich text format, with all references and footnotes numbered consecutively. The text supplied must contain all editorial revisions. Please include a brief biographical statement and a portrait style photograph in electronic form. The page limit for submissions is 5 single-spaced or 10 double-spaced pages. In the case of authors wishing to submit more lengthy articles, the *Quarterly* may require either a summary or an abridged version, which will be published in our hardcopy edition, with the entire article available online. Alternatively, the *Quarterly* may elect to publish as much of the article as can be contained in 5 printed pages, in which case the entire article will also be available on line. Manuscripts should be submitted as email attachments. Material accepted for publication becomes the property of ARIAS-U.S. No compensation is paid for published articles. Opinions and views expressed by the authors are not those of ARIAS-U.S., its Board of Directors, or its Editorial Board, nor should publication be deemed an endorsement of any views or positions contained therein.

As you read this, hopefully, we are about to embark on our Fall Conference at the New York Hilton Midtown on Nov. 9-10, 2023. The conference co-chairs, Alysa Wakin, Marc Abrams, Steve Kennedy and Amy Kline, along with our members who submitted program proposals and, of course, our ARIAS meeting planner, Angela Smith-Ford, have put together a fabulous program. The festivities start on Wednesday, Nov. 8, with the Education Committee's Arbitrator and Umpire Seminar led by co-chairs, Charlie Fortune and Debra Hall. The Women's Resource Committee will also hold its event on Wednesday afternoon.

The main event starts on Thursday, Nov. 9, with our keynote speaker, the Honorable Barry R. Ostrager, Justice of the New York Supreme Court, Commercial Division. For those who don't know, Barry was a long-time ARIAS member as a partner at Simpson Thacher and later as a certified arbitrator. The next day and a half are chocked full of excellent panels and breakout sessions, including a fun networking session on Thursday afternoon.

Also on Thursday afternoon is the ARIAS annual membership meeting where we bid adieu to two long-standing members of the Board of Directors: Cindy Koehler and Steve Schwartz. We will also elect two new Board members, and we'll have our transition to new leadership, as ARIAS Chair Alysa Wakin hands over the gavel to Marc Abrams. Don't forget to attend the annual meeting to vote or submit your proxy.

This issue of the Quarterly features some interesting articles on the arbitration process. First is "How To Cheat In Ar-



bitration – Allegedly: Part I," submitted by Daniel L. FitzMaurice and Joseph K. Scully from Day Pitney LLP. This article supplements the ethics panel at the Fall Conference, "Do Cheaters Never Prosper? Suggestions for Curbing Abuses in Arbitration," and addresses issues faced in arbitration where sometimes it feels like one of the parties is trying to pull a fast one. Part II will continue the discussion from the Fall Conference and address other potential abuses of the arbitration process and how to stop them.

Next, we have an article by the prolific Robert M. Hall, of Hall Arbitrations, and a member of our Quarterly Editorial Board, covering an issue that arises during video proceedings. Titled, "Extending the Time Limit for a Motion to Vacate an Arbitration Award For Texting to a Witness During an Arbitration by Video Conference," Bob addresses how the courts have handled this issue. Keeping with the arbitration theme, Certified Arbitrator Philip M. Howe has written "A Brief Summary of Two Recent Massachusetts Arbitration Cases," which provides a summary of two recent cases decided by courts sitting in Massachusetts on arbitration issues that will be of interest to many ARIAS members.

Changing gears, Edward K. Lenci, from Hinshaw & Culbertson LLP, offers this advice: "Insurers and Reinsurers, Here and Abroad, Should Pay Attention: The

Second Circuit May Well Reconsider Reverse-Preemption of The New York Convention by the McCarran-Ferguson Act." As many of you know, there is a federal circuit split on whether the McCarran-Ferguson Act reverse-preempts the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Ed provides a scholarly analysis of this issue and what we might expect from the Second Circuit Court of Appeals in the future.

Rounding out our featured articles, Frank DeMento, from Transatlantic Reinsurance Company, provides us with an analysis of three species of damages that reinsurers face on a regular basis. Titled, "Punitive Damages, Extra-Contractual Obligations, and Losses in Excess of Policy Limits," Frank leads us through a discussion of each of these types of damages and how they are addressed.

We hope you enjoy this issue of the Quarterly. As you can see, we had tremendous support for this issue, but we need more of you to contribute to future issues. The deadlines and requirements are on the ARIAS website. The 1st Quarter 2024 deadline is January 3, 2024. We welcome committee reports, original articles and repurposed articles from ARIAS CLE programs or from company or firm publications. If you are on a panel at the Fall Conference, please turn your presentation into an article like Dan and Joe did. Leverage your thought leadership and publish an article in the Quarterly. Your thought leadership is worthy of publication.

Larry P. Schiffer
Editor



How To Cheat In Arbitration — *Allegedly*: Part I

Daniel L. FitzMaurice and Joseph K. Scully

Introduction

An omission and an addition to this article’s title warrant preliminary mention. The title refers prominently to cheating but says nothing about “getting away with it.” The techniques that might enable a cheater to avoid detection or accountability exceed the scope of this presentation (and the authors’ ken). The inclusion of “allegedly” in the title signals factual and conceptual caveats. In many of the cases discussed below, the parties disagreed over what did or did not happen and why. More-

over, even on uncontested facts, reasonable minds can sometimes differ in delineating between cheating and aggressive advocacy. Whatever the title’s nuances, the more pressing question is this: Why should anyone write about cheating in arbitration?

Cheating in arbitration constitutes a topic worthy of publication because it happens. Arbitration, like any other dispute-resolution process, relies on adherence to rules. No one should lie, conceal/alter/discard evidence, or otherwise hinder the search for the truth.

Participants also should not rig, delay, divert, or obstruct the process in order to secure an undeserved advantage. Nevertheless, cheating exists in arbitration — as it does in many human endeavors.¹ Each participant in the arbitral process — party, witness, lawyer, or arbitrator — has the capacity to cheat, and judges have found individuals acting in these various roles have done so.² If admitting to a problem is the first step toward finding a solution, then the arbitral community must recognize the existence of cheating.

A second reason to address cheating in arbitration, particularly in this publication, arises from the mission of ARIAS-U.S. Three of this Society's seven objectives refer to precepts that are antithetical to cheating: integrity, justice, and ethics.

- To promote the integrity of the private dispute resolution process, particularly in the insurance and reinsurance industry.
- To promote just awards in accordance with industry practices and procedures.
- To promote high ethical standards in the conduct of arbitration proceedings.

Find the full ARIAS-U.S. Bylaws online at: www.ariasus.org/about-arias-us/by-laws.

Lastly, cheating is interesting. When chaos arrives, restoring order is not enough: we feel compelled to examine what disturbed the cosmos. Forensic scientists study pathology and engineers reconstruct accidents to appreciate aberration and the mechanics of calamity. Readers consume mysteries to see not only who did it but why and how. Whether it evokes fear, revulsion, schadenfreude, or some other response, evil can be riveting.

“The ways to cheat in arbitration are many.”

The ways to cheat in arbitration are many. The list begins with faking an arbitration agreement and ends with destroying the panel. In between, schem-

ers can engage in a variety of tactics in hopes of gaining an unfair edge over the opponent and even securing an unwarranted outcome. Even without attempting to provide an encyclopedic list, discussing these numerous tactics requires more than one article. Accordingly, set out below is Part I of How to Cheat in Arbitration – *Allegedly*.

Tactic: Fabricate an agreement to arbitrate and then wait for the other side to default

One might assume that an arbitral agreement is a necessary predicate for cheating in arbitration. Not so. Inventing an imaginary or contrived agreement to arbitrate can be the first step toward an ill-gotten award. A fake agreement often provides a secondary benefit to the cheater: an award by default because the respondent refuses to acknowledge much less participate in the sham proceedings. This grift's most significant challenge lies in enforcing the award, because confirmation usually requires proof of an actual agreement to arbitrate.³

In *Williams v. Laimana*,⁴ the petitioner sent an email with an attachment labeled “Exhibit A” to a hotel and some

under Exhibit ‘A.’”⁵ The respondents ignored the email. In a one-sided arbitration, the petitioner obtained a default award for approximately \$1.5 million. His plan went swimmingly until he tried to confirm the award: a court found that the respondents never agreed to arbitrate and, accordingly, vacated the award for fraud.⁶ In reaching this conclusion, the court quoted from *Black's Law Dictionary* to explain that fraud is “any kind of artifice by which another is deceived,” and, thus, “all surprise, trick, cunning, dissembling, and other unfair way that is used to cheat anyone, is considered as fraud.”⁷

Others – including so-called “sovereign citizens” – have employed a similar scheme in hopes of preventing mortgage foreclosures.⁸ In *John v. Central Loan Administration & Reporting*,⁹ the plaintiffs sent three respondents several documents including a contract with an arbitration clause. The plaintiffs then declared that the respondents, by ignoring the communication, had agreed to arbitrate by “definitive non-response” and “tacit procreation.”¹⁰ The plaintiffs demanded that the respondents arbitrate before the “Universal International Arbitration Association.” The respondents brushed off the demand. The arbitrator, identified as Thomas Bradford Schaults, issued a default award granting \$1,434,000 in damages to the plaintiffs and declaring that respondents had released all of their rights and claims, including the right to enforce the mortgage note.¹¹ When the plaintiffs sued to confirm the award, the respondents failed to appear. Nevertheless, a vigilant judge refused to confirm the award because the plaintiffs' filings made “clear that the purported award is bogus because there was never an agreement to arbitrate.”¹² The court

of its employees. After accusing the respondents of wire fraud and mail tampering, the email advised that failing to reply “would constitute ‘agreement by silent consent to the arbitration clause

cited several cases decided in the past few years in which other federal courts likewise refused to enforce “sham arbitration award[s]”¹³ in similar circumstances. Others attempting to use the same gambit to avoid mortgage foreclosures have suffered the same fate.¹⁴

Although the courts in these cases rejected these scams, ignoring a bogus award may be a dangerous strategy. In *Reed v. RBMS REO Holdings*,¹⁵ another individual opposing a mortgage foreclosure relied on the respondent’s silence as purported consent to arbitrate. The respondent ignored an arbitration demand and refused to participate. The arbitrator, once again Thomas Bradford Schaults, issued a default award to Reed for \$15.2 million. Reed waited more than four months and then petitioned a federal court for confirmation. The delay was critical, because the respondent’s window to seek vacatur expired three months after delivery of the award.¹⁶ The Court dismissed Reed’s petition to confirm, but it also denied as untimely the respondent’s motion to vacate. Without confirmation, Reed could not collect the \$15.2 million. An unconfirmed award, however, might pose other problems for the respondent. For example, a court or arbitrator in another proceeding could give preclusive effect to an unconfirmed award.¹⁷ Similarly, an unconfirmed award might serve as an offset for the petitioner against affirmative claims the respondent may possess, such as damages for the mortgage deficiency.¹⁸ In some instances, unconfirmed awards can become incorporated into judgments in other proceedings.¹⁹ And an unconfirmed award might cause other havoc.²⁰ Accordingly, a victim of a contrived award would be well-advised to seek vacatur prompt-

ly to avoid possible complications.

Issues over the existence of an agreement to arbitrate can and do arise in the insurance and reinsurance context. One case involved an arbitration clause in an automobile insurance policy for uninsured motorist (“UIM”) claims. The clause provided that, if the parties mutually decided to arbitrate a particular UIM claim, the rules and procedures of the American Arbitration Association (“AAA”) would govern.²¹ After making a UIM claim, the policyholder demanded arbitration without seeking the insurer’s consent. The AAA appointed a single arbitrator, who set a hearing date. The insurer appeared at the hearing only long enough to state that (a) it never agreed to arbitrate this claim and (b) if the arbitration clause did apply to this dispute, it would require multiple arbitrators. Once the insurer left, the claimant presented her version of the facts to the arbitrator. The arbitrator rendered an award in favor of the claimant for \$450,000, the full limit of the policy. After the insurer sued, the court vacated the award, finding that the arbitrator lacked authority because both parties had not agreed to arbitrate this UIM claim.

In *Olsen v. United States*,²² policyholders sought to recover for crop losses suffered during a two-year period. Their

insurer, American Growers Insurance Company (“AGIC”), did not respond to the claim, because it had become insolvent and was in liquidation. Citing a clause in the policy, the policyholders issued an arbitration demand to AGIC’s reinsurer, the Federal Crop Insurance Corporation (“FCIC”). FCIC refused to participate beyond advising the arbitrator that he lacked jurisdiction. The arbitrator issued default awards against FCIC for over \$3 million. The parties proceeded to federal court, where the policyholders sought confirmation, and FCIC requested vacatur. FCIC won for several reasons. The court found that the reinsurer and policyholder had never entered into any agreement (i.e., “privity of contract” was absent), and the policy’s arbitration clause contemplated proceedings between only the insurer and policyholder.²³ In addition, the arbitration violated the liquidation order in AGIC’s insolvency proceedings. Accordingly, the court vacated the default awards.

In each case discussed above, a court refused to enforce an award emanating from non-existent or inapplicable agreement to arbitrate. Equally noteworthy, however, is that arbitrators in all of these cases granted relief to the petitioners despite the absence of agreements to arbitrate. Moreover, courts are fallible: one should not assume that

“...one should not assume that a court will never confirm or enforce scam or improper award.”

a court will never confirm or enforce scam or improper award. In addition, some respondents may opt to settle rather than litigate over the validity of an arbitral award. Thus, despite having never agreed to arbitrate, a respondent might pay something to resolve a fake award. And, of course, desperate parties with little to lose may try anything – even inventing an agreement to arbitrate.

Tactic: Sucker the other party into agreeing to a process that favors you

“Arbitration” is a broad term that encompasses a wide array of dispute-resolution procedures and mechanisms.²⁴ Intrinsicly, arbitration is neither fair nor unfair. Whether any particular rule or process operates equitably depends on the circumstances. A form of arbitration that functions well in resolving disputes between two sophisticated and financially able companies might severely disadvantage a consumer going up against an international conglomerate. Likewise, many workers may find it challenging to square off against their employers in an arbitration, but that concern may not apply to professional athletes, senior executives, or TV anchors.²⁵ Thus, context matters in assessing the fairness of an arbitral process. A signature way to cheat in arbitration is for one side to capitalize on the operative circumstances, by identifying arbitral features that work to that party’s favor and then euchring the other side into agreeing to arbitrate on those terms

What types of arbitral terms may advantage one party and disadvantage the other? For example, in *Rent-A-Center*,

“Arbitration” is a broad term that encompasses a wide array of dispute-resolution procedures and mechanisms.²⁴

West, Inc. v. Jackson, an employee argued that limitations on discovery and a requirement that both sides split the arbitrators’ fees were unfair to individual employees in disputes with their employers. The employee also contended that the scope of the arbitration clause was “one sided in that it required arbitration of claims an employee was likely to bring—contract, tort, discrimination, and statutory claims—but did not require arbitration of claims [the employer] was likely to bring—intellectual property, unfair competition, and trade secrets claims.”²⁶

Examples of allegedly unfair clauses in the insurance and reinsurance context include the following:

- A corporate policyholder from California challenged a forum provision requiring that the arbitration proceed in New York, and a choice-of-law provision selecting New York law to govern the policy. The policyholder also claimed that the default provision for appointing an umpire was unfair, because it gave that authority to the President of the AAA who allegedly had an institutional bias in favor of insurers. The arbitration clause also prohibited the panel from awarding punitive damages and

provided that both parties waived those damages. Other complaints included a requirement that the hearing proceed within 60 days of the umpire’s appointment and the absence of any procedural guarantees to ensure the insured was able to be adequately prepared;²⁷

- An insured/reinsured claimed that provisions in a workers’ compensation reinsurance participation agreement were illegal and unconscionable in requiring arbitration in the British Virgin Islands and delegating questions of arbitrability to the arbitrator;²⁸
- A Massachusetts-based insured challenged the fairness of a clause in a policy providing for mandatory arbitration of coverage disputes and setting the situs of the arbitration in London, the insurer’s location, while also exempting from arbitration suits for unpaid premiums;²⁹
- An individual claimed he (a) was not informed that his automobile policy had an arbitration clause, (b) did not bargain for this provision or have any meaningful choice, and (c) would be oppressed by having to travel to another city in the same state to attend an arbitration because he would need to

take time off from work without pay;³⁰

- An insurance agency claimed the arbitration clause in its agency agreement with an insurance company was one-sided and unenforceable because it allowed the insurer, at its option, to litigate claims the agent committed fraud or misconduct or had acted outside the scope of its authority.³¹

The challenges to the arbitration provisions described above all failed. Nevertheless, the losing parties were not necessarily wrong in complaining that the arbitration clauses advantaged the other side. Procedural terms can mildly favor one side, such as conferring a home-court advantage,³² or provide more significant benefits, such as banning class-wide arbitrations or the consolidation of parties with similar claims. Limitations on the types of disputes subject to arbitration or the kinds of relief available also can significantly disadvantage one party.

Whether getting the other party to accept a one-sided, arbitration clause is “cheating” may be open to debate. At least eighteen states have weighed in on this issue by enacting statutory bans on arbitration clauses in insurance policies.³³ Statutory prohibitions on arbitration clauses in insurance policies also may apply to reinsurance agreements in some states.³⁴ An advocacy group, Public Citizen, argues that policyholders have no true ability to consent to arbitration and that insurers invariably draft one-sided clauses.³⁵ Others, however, dispute the premise that all insurance policies are contracts of adhesion.³⁶ Some policyholders have substantial bargaining power and, especially with regard to certain types

of insurance, are able to negotiate and craft policy language with help from professional risk managers and brokers.³⁷ These “manuscripted” provisions may include arbitration clauses.³⁸ Policyholders may prefer to arbitrate in certain circumstances, including where they might want to maintain confidentiality over information that, if publicized, could be embarrassing or detrimental to their interests.³⁹

Cheating can include using deception to get the counterparty to agree to a one-sided procedure. The consequences of trickery depend on the technique the cheater uses. Pulling a switcheroo with the paperwork or otherwise manipulating someone into signing a contract without knowing its true contents – “fraud in factum” – will render the entire contract unenforceable, including the arbitration clause.⁴⁰ By contrast, making false promises or misrepresentations about the putative agreement – “fraudulent inducement”⁴¹ – will not invalidate the arbitration clause,⁴² unless the fraud is specific to the agreement to arbitrate.⁴³ Indeed, because most misrepresentations will not preclude arbitration, the counterparty asserting fraudulent inducement likely will need to arbitrate that defense.⁴⁴ Depending on the breadth of the arbitration pro-

vision and the power it grants to the arbitrators, a court often will resolve other contractual defenses to a claimed agreement to arbitrate,⁴⁵ including illegality⁴⁶ and unconscionability.⁴⁷

Tactic: Stack the umpire deck with ringers and unqualified candidates

Game theorists love arbitration and arbitrator-selection processes, because they are rich environments for strategic choices.⁴⁸ In the context of tripartite arbitration, the selection of the neutral may be outcome-determinative.⁴⁹ Thus, one need not be a budding Nash or Pareto to appreciate each party’s interest in selecting an umpire who appears to favor that party’s position. As such, a well-recognized way to try to rig the process is to identify and propose only candidates who are not neutral but bi-

“Umpires and neutral arbitrators are supposed to be independent and impartial.”

ased decidedly in the nominating party’s favor.

Umpires and neutral arbitrators are supposed to be independent and impartial.⁵⁰ Like Justitia, they are supposedly blind to improper influences and free from the kind of partisanship that often characterizes party-appointed arbitrators⁵¹ and which has become

a focal point for extensive and long-standing criticism of American tripartite arbitration.⁵² Impartiality, however, is not the sole objective in selecting an umpire, and other important qualifications – industry experience and substantive expertise – may interfere with unalloyed neutrality.⁵³ Moreover, a functional definition of “impartiality” may describe ranges of behaviors and views, however, rather than bright lines and identifiable patterns.⁵⁴

Naturally, each party wants an umpire whose predispositions place him or her closer to that party’s position along a continuum of impartiality.⁵⁵ Indeed, merely because an umpire candidate’s background and experience suggest he or she could be favorably disposed to one side over the other does not establish evident partiality. For example, in one insurance arbitration, a policyholder complained that the umpire, whom the insurer had nominated, was biased in favor of the insurer and that he was further compromised because, during the arbitration, the insurer unsuccessfully nominated him to serve as an umpire in a similar dispute with a different policyholder.⁵⁶ The district court refused to find evident partiality in part because the contractual criteria and selection process “permit[ed] each [party] to nominate umpire candidates ‘whose credentials suggest that they would be inclined to favor the nominating party.’”⁵⁷ In another case, the court rejected a policyholder’s claim that arbitrators certified by ARIAS-U.S. are partial to insurance companies because “the process for becoming ARIAS-certified is skewed towards those with insurance company experience.”⁵⁸ Thus, even if a candidate’s background suggests less than pure neutrality, it does

not mean the candidate cannot be impartial.

A cheater will not be satisfied with the appearance that a candidate might be favorably disposed. Cheaters want ringers. Finding a true ringer may prove challenging, however. Certain individuals might seem favorably predisposed but prove to be frustratingly impartial.⁵⁹ Indeed, even a party-appointed arbitrator, with whom the party can conduct an extensive interview before an engagement,⁶⁰ may rule in unexpected ways.⁶¹ Thus, it is far more difficult to predict the views of an umpire candidate, for whom the vetting process is usually far more limited and is not supposed to happen on an *ex parte* basis.⁶² Cheaters may choose to stretch or even ignore contractual qualifications in favor of a preferred candidate who does not meet the criteria.⁶³ Some courts have interceded to resolve logjams in the umpire-selection process arising from disputes over whether candidates meet contractual requirements.⁶⁴

In *Drobny v. American National Insurance Co.*,⁶⁵ a managing general underwriter (“NAIU”) and its former appointing company (“ANICO”) engaged in several battles over umpire selection. ANICO requested that the parties send questionnaires to the umpire candidates, but NAIU refused. Based on independent research, ANICO then claimed that one of NAIU’s three nominees did not meet the contractual requirement that all arbitrators must be “active or retired, disinterested officials of U.S. insurance or reinsurance companies.” NAIU also allegedly engaged in *ex parte* communications with its umpire candidates. Although the parties had not drawn lots to choose the umpire as prescribed in their contract,

NAIU unilaterally advised one of its candidates (not the allegedly unqualified nominee) that she had been appointed as umpire. ANICO challenged NAIU’s anointed umpire. Although she initially recused herself, she resumed the putative role after NAIU unilaterally “reinstated” her. The arbitration appeared to leap forward when NAIU’s party-arbitrator notified ANICO’s arbitrator that, in less than one month, the parties must submit all documentary evidence, with the final hearing to proceed shortly later. ANICO promptly sued, seeking among other things a temporary injunction to stop the “sham arbitration.” The trial court granted the injunction, and an appellate court later affirmed. The trial court also compelled NAIU to proceed with the selection process specified in the contract, including by naming three candidates that meet the contractual criteria. Thus, what ANICO referred to as NAIU’s attempt to “hijack the arbitration” failed.

*National Casualty Co. v. OneBeacon American Insurance Co.*⁶⁶ serves as an example of an attempt to nominate alleged ringers as umpire candidates in the context of a reinsurance dispute. From 1966 to 1986, OneBeacon ceded risk to a treaty reinsurance program; Swiss Re participated in this program in certain years as did two related reinsurers, National Casualty and Employers of Wausau. The treaties applicable to each of these reinsurers used the same definition of “occurrence.” The “occurrence” definition allowed OneBeacon to aggregate injuries to multiple persons where the injuries were “traceable to same causative agency.” These reinsurers disputed OneBeacon’s aggregation of non-products bodily injury claims from exposures to asbestos and silica.

Swiss Re arbitrated its dispute first. After winning the arbitration, Swiss Re obtained a judgment confirming the award over One Beacon's motion to vacate.⁶⁷ After losing to Swiss Re, OneBeacon demanded that National Casualty and Wausau arbitrate. The parties agreed to consolidate their disputes into one arbitration and to select an umpire by a familiar process: each side nominates three candidates, each strike two of the opponent's nominees, and then they use the Dow Jones method to identify the umpire.⁶⁸ National Casualty/Wausau first nominated two individuals who had participated in the earlier arbitration as, respectively, the umpire and Swiss Re's party-appointed arbitrator. Swiss Re's former arbitrator immediately declined this nomination, and subsequently the umpire withdrew. National Casualty/Wausau then nominated as a replacement candidate the Senior Legal Counsel at Swiss Re who had been responsible for the earlier arbitration. The selection process bogged down with disputes over the nominations, including OneBeacon's accusation that the reinsurers were "seeking to stack the arbitration panel with umpire candidates who have been involved in a prior arbitration in which OneBeacon was a party."⁶⁹ The reinsurers filed suit, seeking a judgment declaring that OneBeacon was estopped from pursuing its claims in arbitration by virtue of the confirmed award in the Swiss Re arbitration. OneBeacon moved to dismiss the complaint and requested that the court proscribe the candidacy of Swiss Re's Senior Legal Counsel. The court dismissed the reinsurer's complaint⁷⁰ but also declined to disqualify their umpire candidate.⁷¹

In *Lexington Insurance Co. & Chartis v. South Energy Homes, Inc.*, the poli-

cyholder ("SEH") accused Lexington of committing "bad faith in the umpire-selection process by nominating two individuals . . . SEH claims should be removed because they are biased." Both nominees were lawyers, one of whom SEH described as having a "resume [that] reads like a 'Who's Who Among Insurance Defense Lawyers'" and the other was a partner in a firm that had previously represented Lexington's insureds.⁷² SEH also accused both candidates of making inadequate disclosures. The Supreme Court of Alabama was unimpressed. The court held that allegations of bad faith participation in the selection process required "something more" than proof (if it existed) that the nominees were actually biased. The court identified that additional element as "proof that the nominating party, when making or pursuing the nomination, was actually aware of the underlying facts and also knew to some degree of certainty . . . that such facts were disqualifying in nature, yet proceeded to make the nomination anyway."⁷³

A later case involved an alleged ringer adverse to Lexington. In, *Wright Medical Group, Inc. v. Lexington Insurance Co.*,⁷⁴ the policyholder-petitioner accused Lexington of bad faith in declining coverage. The policyholder nominated a lawyer as the umpire, and she was selected as the umpire. After being named, the umpire disclosed that she currently represented a different policyholder in litigation seeking \$17 million from Lexington for alleged bad faith. Lexington objected to the umpire and asked the AAA, which was administering the arbitration, to disqualify her.⁷⁵ After the AAA granted Lexington's request, the policyholder sued. In a "Petition to Enforce the Arbitration Agree-

ment," the policyholder asked that the court require Lexington to arbitrate before the chosen-but-disqualified umpire. The court concluded that it lacked jurisdiction and dismissed the petition with the direction that "selection of the impartial umpire in this matter shall be resolved in arbitration pursuant to the rulings of the AAA."⁷⁶ Thus, the insurer succeeded in disqualifying an alleged ringer for bias, but only because there was an administrator with authority to resolve that dispute. Courts generally refuse requests made during the pendency of the arbitration to declare the umpire unqualified.⁷⁷ Even after awards, dissatisfied parties alleging the failure of one or more of the arbitrators to meet contractual requirements seldom succeed.⁷⁸

The importance of the umpire or neutral to any tripartite arbitration explains the temptation to find ways to rig the process to ensure the selection of a favored candidate. It should come as no surprise that some will cheat to achieve that end.

What Comes Next?

This installment does not begin to cover the many ways to cheat in arbitration. In Part II, we will discuss other tactics, including:

- Forcing the withdrawal or disqualification of opposing arbitrators and undesirable umpires;
- Replacing your arbitrator after the umpire becomes known;
- Making sure the umpire knows who is responsible for his or her nomination;
- Ex parte contacts;
- Bribery;
- Perjury;

- Obtaining access to Panel deliberations;
- Ghostwriting for your arbitrator or the Panel;
- Baiting the Panel into making mistakes or showing bias; and
- When all else fails, destroy the Panel.



Daniel "Dan" Fitz-Maurice represents clients in trials, arbitrations, and appeals of complex commercial disputes, with an

emphasis on matters involving insurance and reinsurance, corporate, banking, franchise, and financial transactions. He has tried numerous cases in state and federal courts across the United States for both domestic and foreign entities. Dan has also handled appeals before the U.S. Courts of Appeals for the Second, Third, Ninth and District of Columbia circuits, as well as the Connecticut Supreme Court. Dan has represented ceding companies and reinsurers in difficult reinsurance litigation across a wide range of legal issues.

Dan is actively engaged in AIDA Reinsurance and Insurance Arbitration Society, ARIAS-U.S., having served on the Board of Directors and as chair, and as a member and co-chair of the Arbitration Task Force. He currently serves on the Forms and Procedures Committee and Member Services Committee of ARIAS-U.S. Dan also publishes and speaks frequently on issues relating to reinsurance, financial services, and trial practice.



Joseph Scully, an experienced litigator, primarily represents insurance companies in insurance coverage

actions and reinsurance disputes. He has litigated coverage disputes in state and federal courts, including disputes arising from asbestos and other product liability claims, environmental losses, fire and other property damage, construction defects, and equipment breakdown claims. Joseph also has handled and tried disputes involving reinsurance claims before arbitration panels and in state and federal courts.

Joseph has tried complex civil disputes in courts throughout New England, as well as Delaware, Maryland, New York, Ohio and Texas. Clients seek out his experience taking matters to trial in state and federal courts and litigating numerous arbitrations through final hearings. He is also sought out for his handling of appeals before courts, including the First Circuit Court of Appeals and state appellate courts in Connecticut, Massachusetts, New York and Rhode Island.

Joseph has been published and quoted on insurance and reinsurance topics in a number of publications, including Law360 and the Connecticut Law Tribune. He is a former member of the Board of Editors of Connecticut Supreme Court History, the journal of the Connecticut Supreme Court Historical Society. He currently serves on the Board of the Greater Hartford Legal Aid Foundation.

ENDNOTES

- 1 See, e.g., Ronald E. Riggio, *Why So many of Us Lie, Cheat, and Steal*, Psychology Today (June 9, 2012), <https://www.psychologytoday.com/us/blog/cutting-edge-leadership/201206/why-so-many-us-lie-cheat-and-steal>; Dan Ariely, *The Honest Truth About Dishonesty: How We Lie to Everyone—Especially Ourselves* (2013); but see also Christian B. Miller, *An Influential Study of Dishonesty was Dishonest*, Forbes (Aug. 30, 2021), <https://www.forbes.com/sites/christianmiller/2021/08/30/an-influential-study-of-dishonesty-was-dishonest/>.
- 2 For alleged cheating by a: (a) **party**, see, e.g., *Virginia Sur. Co., Inc. v. Certain Underwriters at Lloyd's, London*, No. 1-10-1753, 2011 WL 2586357, at *5 (Ill. App. Ct. Apr. 20, 2011) (upholding vacatur of award after finding the respondent committed arbitral fraud by submitting fees and costs for two treaties despite knowing that one of the treaties required each party to bear its own fees and costs); (b) **witness**, see, e.g., *Nu-Vasive, Inc. v. Absolute Med., LLC*, 71 F.4th 861, 877 (11th Cir. 2023) (affirming vacatur for fraud, based on a finding that a witness, while testifying remotely during a hearing conducted via videoconference, conformed his testimony to texts he received from the respondent); (c) **lawyer**, see, e.g., *Insinga v. Liberty Mut. Ins. Co.*, 265 A.D.2d 411, 411-12, 696 N.Y.S.2d 506, 507 (App. Div. 1999) (upholding vacatur where petitioner's attorneys served the arbitration demand on the respondent, rather than its attorneys, and hid the demand "among voluminous other documents to prevent the respondent from contesting . . . arbitrability"); and (d) **arbitrator**, see, e.g., *Star Ins. Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 656 F. App'x 240, 242 (6th Cir. 2016) (vacating awards on a disputed factual record, where the Court concluded that party-appointed arbitrator's communications with the appointing party's counsel were impermissible under arbitral scheduling orders).
- 3 The Federal Arbitration Act, in 9 U.S.C. § 13, requires in part that "[t]he party moving for an order confirming . . . an award shall, at the time such order is filed with the clerk . . . also file the following papers with the clerk: (a) [t]he agreement." See, e.g., *Pena v. TD Auto Fin. LLC*, 860 F. App'x 220, 222 (3d Cir. 2021) (concluding that the District Court did not err in dismissing what it believed to be a sham arbitration award and noting that 9 U.S.C. §13 requires the party

- seeking confirmation to file “among other things, the agreement and the award”); *Bozek v. PNC Bank*, No. 20-3515, 2021 WL 4240359, at *2 (3d Cir. Sept. 17, 2021) (confirming dismissal of a petition to confirm where the petitioner “failed to make any colorable showing of a valid agreement to arbitrate in the first place”) (citing 9 U.S.C. § 13(a)); *Jiangsu Beier Decoration Materials Co., Ltd. v. Angle World LLC*, 52 F.4th 554, 561 (3d Cir. 2022) (stating that to enforce an international arbitration award, proof of a written agreement to arbitrate is “an essential prerequisite to the recognition and enforcement of an award under the New York Convention”); *Commodities & Mins. Enter. Ltd. v. CVG Ferrominera Orinoco, C.A.*, 49 F.4th 802, 817 (2d Cir. 2022) (discussing the choice of law governing the validity of an international arbitration agreement), *cert. denied*, 215 L. Ed. 2d 52, 143 S. Ct. 786 (2023).
- 4 *Williams v. Laimana*, No. 20-CV-01110, 2020 WL 8262400 (C.D. Cal. Dec. 22, 2020), *aff'd*, No. 21-55053, 2022 WL 563250 (9th Cir. Feb. 24, 2022).
 - 5 *Williams*, 2020 WL 8262400, at *1.
 - 6 *Williams*, 2020 WL 8262400, at *2.
 - 7 *Williams*, 2020 WL 8262400, at *2 (quoting Garner, *Black’s Law Dictionary* (11th ed. 2019)).
 - 8 On June 15, 2021, the Anti-defamation League posted an article on its website entitled “New Sovereign Citizen Bogus ‘Arbitration’ Tactics Appearing in Many States.” <https://www.adl.org/resources/blog/new-sovereign-citizen-bogus-arbitration-tactics-appearing-many-states>. The article describes a “rash of cases” dating to 2019 “in which plaintiffs go to court to ask that suspicious arbitration awards be ‘confirmed’ against the party that they claim owes the putative damages.”
 - 9 *John v. Cent. Loan Admin. & Reporting*, No. 21-CV-01411, 2021 WL 1845913 (E.D.N.Y. Apr. 13, 2021), *appeal dismissed*, No. 21-1368, slip op. (2d Cir. Nov. 16, 2021).
 - 10 *John*, 2021 WL 1845913, at *1.
 - 11 Perhaps unsurprisingly, the “lead arbitrator” who issued the default award in this matter, acting as a pro se litigant, also has cited a purported arbitral award in opposing a mortgage foreclosure. *Thomas B Schaults CQV Tr. v. LoanDepot Co. LLC*, No. 23-CV-00091, 2023 WL 1767196 (D. Ariz. Feb. 3, 2023). The arbitrator who issued the “award” in favor of Mr. Schaults, Linda L. Wall, was herself the beneficiary of an “award” for \$1,003,000 that Mr. Schaults issued in an arbitration Wall brought against the Treasurer and Tax Collector for the County of Los Angeles. *Lynda L. Wall CQV Tr. v. Knox*, No. 22-CV-08946, 2023 WL 3568062, at *1 (C.D. Cal. Jan. 20, 2023) (dismissing Ms. Wall’s suit to confirm award and enjoin a tax sale auction). Litigation that Mr. Schaults brought pro se in 2011 against an IRS agent to prevent the collection of taxes was dismissed based on Sovereign Immunity and the Anti-Injunction Act. *Schaults v. Kubik*, No. 2:11-CV-01340, 2011 WL 6020146 (W.D. Pa. Dec. 2, 2011).
 - 12 *John*, 2021 WL 1845913, at *2.
 - 13 *John*, 2021 WL 1845913, at *3.
 - 14 *Redmond v. Polunsky*, No. 4:20-CV-00204, 2023 WL 2143600, at *6 (E.D. Tex. Feb. 21, 2023) (citing eight other cases); *Redmond v. Graham*, No. 4:21-CV-00004, 2022 WL 3141866, at *7 (E.D. Tex. Aug. 5, 2022) (same result; not cited in *Redmond v. Polunsky*); *Redmond v. Wells Fargo Bank N.A.*, No. 4:21-CV-00005, 2022 WL 3142343, at *7 (E.D. Tex. Aug. 5, 2022) (same; also not cited in *Redmond v. Polunsky*); *Redmond v. PR-LAP*, No. 4:21-CV-00006, 2022 WL 3141867, at *5 (E.D. Tex. Aug. 5, 2022) (same; also not cited in *Redmond v. Polunsky*).
 - 15 *Reed v. RBMS REO Holdings, LLC*, No. 20-CV-05891, 2021 WL 4943562, at *1 (S.D.N.Y. July 12, 2021), *report and recommendation adopted sub nom.*, No. 20-CV-05891, 2021 WL 4480459 (S.D.N.Y. Sept. 30, 2021).
 - 16 9 U.S.C. § 12 (petitions to vacate arbitral awards must be served within three months of the award’s delivery).
 - 17 *See Witkowski v. Welch*, 173 F.3d 192, 199 (3d Cir. 1999) (holding that an unconfirmed arbitral award has the effect of a final judgment on the merits); *Jacobson v. Fireman’s Fund Ins. Co.*, 111 F.3d 261, 267–68 (2d Cir. 1997) (“[Under New York law,] res judicata and collateral estoppel apply to issues resolved by arbitration where there has been a final determination on the merits, notwithstanding a lack of confirmation of the award.” (quotation marks omitted)); *Wellons, Inc. v. T.E. Ibberson Co.*, 869 F.2d 1166, 1169 (8th Cir. 1989) (affirming summary judgment based on collateral estoppel effect of unconfirmed arbitration award). An unconfirmed award, however, may not receive full faith and credit under 28 U.S.C. § 1738. *Harner v. USAA Gen. Indem. Co.*, 590 F. Supp. 3d 1217, 1225 (S.D. Cal. 2022) (“Section 1738 does not require that federal courts give res judicata or collateral estoppel effect to an unconfirmed arbitration award, however, because arbitration is not a judicial proceeding.” (quotations omitted)); *cf. Patton v. Johnson*, 915 F.3d 827, 836 n.3 (1st Cir. 2019) (“An arbitration award that has been reviewed by a state court may fall within the ambit of the Full Faith and Credit Act.”).
 - 18 In *Centurion Air Cargo, Inc. v. United Parcel Service Co.*, 300 F. Supp. 2d 1281, 1286 (S.D. Fla. 2004), *aff’d*, 420 F.3d 1146 (11th Cir. 2005), UPS entered into a purchase agreement to acquire substantially all of the assets of Centurion, with certain payments to be made in installments after the sale. Subsequently, a creditor attached certain of the sold assets in Costa Rico. UPS demanded that Centurion arbitrate. The arbitrator ordered Centurion to post security in the amount needed to dissolve the creditor’s attachment. When Centurion failed to post security, UPS advised that it would use the unconfirmed award to set-off its obligation to pay an installment of the purchase price. The Court concluded that UPS was entitled to this offset, because the award though unconfirmed met the purchase agreement’s requirements of being final and binding. *Id.*
 - 19 In *Hanson v. Beach*, No. 2019AP1388, 2021 WL 822103, at *3 (Wis. Ct. App. Mar. 4, 2021), a divorcing couple arbitrated over certain financial issues. A court later incorporated the unconfirmed award into the judgment of divorce. When cited for failing to comply with a term of the award, the former husband argued that the absence of confirmation precluded a finding of contempt and corresponding sanction. The Wisconsin Court of Appeals rejected that argument, upholding the contempt and sanction because the unconfirmed award had become part of the divorce judgment.
 - 20 *See Del Monte Int’l GMBH v. Ticofrut, S.A.*, No. 16-CV-23894, 2017 WL 2901326, at *4 (S.D. Fla. Jan. 30, 2017) (discussing *Morgan Keegan & Co., Inc. v. Rotundo*, Case No. 12-21498, in which a Miami-Dade state circuit court issued a writ of garnishment allowing the enforcement of an unconfirmed award), *report and recommendation adopted*, No. 16-CV-23894, 2017 WL 2899978 (S.D. Fla. May 16, 2017).
 - 21 *Owners Ins. Co. v. Dyer*, No. 12-CV-01097, 2013 WL 12241402, at *5 (C.D. Ill. Aug. 26,

- 2013).
- 22 *Olsen v. U.S. ex rel. U.S. Dep't of Agric.*, 546 F. Supp. 2d 1122 (E.D. Wash. 2008), *aff'd sub nom., Olsen v. U.S. ex rel. Fed. Crop Ins. Corp.*, 334 F. App'x 834 (9th Cir. 2009).
- 23 It is possible for a contract that has no arbitration clause to incorporate by reference an agreement to arbitrate from another contract. For example, in *Century Indem. Co. v. Certain Underwriters at Lloyd's*, 584 F.3d 513, 555 (3d Cir. 2009), the Court held that a retrocessional reinsurance agreement between INA and Underwriters incorporated an arbitration clause from the underlying reinsurance agreement, even though the clause referred specifically to the parties to the underlying reinsurance agreement, INA and Argonaut.
- 24 See, e.g., Thomas J. Stipanowich, *Living the Dream of ADR: Reflections on Four Decades of the Quiet Revolution in Dispute Resolution*, 18 Cardozo J. Conflict Resol. 513, 533 (2017) (referring to arbitration as “one of the primary conceptual frameworks for third-party intervention in the resolution of disputes” and noting that “[w]ithin that framework is a broad spectrum of procedural choice that has given rise to a wide variety of arbitration formats, many of which result in a legally binding award, or decision”). In an early taxonomy of commercial arbitration, a professor at the University of Chicago – later dubbed a “mother of ADR” – identified three main categories: “individuated” arbitration in which two parties contract to settle disputes before named arbitrators or persons to be named later; trade association or exchange arbitration in which a group establishes its own mechanism (e.g., FINRA for the securities industry); and administrative arbitration in which an organization hosts the process and sets the rules (e.g., the International Chamber of Commerce or the American Arbitration Association). Soia Mentschikoff, *Commercial Arbitration*, 61 Colum. L. Rev. 846, 849 (1961); see Carrie-Menkell-Meadow, *Mothers and Fathers of Invention: The Intellectual Founders of ADR*, 16 Ohio St. J. on Disp. Resol. 1, 22 (2000) (describing Mentschikoff as a “‘mother’ of ADR” and “one of the first women to leave a deep imprint on legal institutions”).
- 25 See Theodore J. St. Antoine, *Labor and Employment Arbitration Today: Mid-Life Crisis or New Golden Age?*, 32 Ohio St. J. Disp. Resol. 1, 12-14 (2017) (noting that “there are enormous differences between one nonunion employment arbitration and another,” including whether the agreements were negotiated or employer imposed, the category of employee, the amount at stake, how the arbitrator is selected and case administered, etc.).
- 26 *Rent-A-Ctr., W., Inc. v. Jackson*, 561 U.S. 63, 73, 130 S. Ct. 2772, 2780, 177 L. Ed. 2d 403 (2010). In a five-to-four decision, the Supreme Court held that the arbitration clause required the employee to arbitrate the defense that the contract should not be enforced, because it was unconscionable.
- 27 See, e.g., *Tutor-Saliba Corp. v. Starr Excess Liab. Ins. Co., Ltd.*, No. 15-CV-01253, 2015 WL 13285089, at *4 (C.D. Cal. Apr. 23, 2015) (rejecting challenges); see also *CIC Buyer LLC v. Pac. Ins. Co. Ltd.*, No. 21-CV-01164, 2021 WL 5986918, at *3 (C.D. Cal. Sept. 15, 2021) (same).
- 28 *Minnieland Priv. Day Sch., Inc. v. Applied Underwriters Captive Risk Assurance Co., Inc.*, 867 F.3d 449, 454 (4th Cir. 2017).
- 29 *DiMercurio v. Sphere Drake Ins., PLC*, 202 F.3d 71, 73 (1st Cir. 2000).
- 30 *S. United Fire Ins. Co. v. Howard*, 775 So. 2d 156, 163 (Ala. 2000).
- 31 *Molton, Allen & Williams, LLC v. Cont'l Cas. Ins. Co.*, No. 09-CV-06924, 2010 WL 780353, at *4 (N.D. Ill. Mar. 3, 2010).
- 32 For example, reinsurance agreements often provide for the arbitration to take place at the site of the cedent's home office, unless the parties agree otherwise. See, e.g., *Yosemite Ins. Co. v. Nationwide Mut. Ins. Co.*, No. 16-CV-05290, 2016 WL 6684246, at *2 (S.D.N.Y. Nov. 10, 2016) (finding that arbitration clause in contract involving a cedent based in California provided that “[t]he arbitration must take place in San Francisco, unless the parties agree on another location, and a decision made by a panel majority is binding”); *Hamilton Life Ins. Co. of N.Y. v. Republic Nat'l Life Ins. Co.*, 408 F.2d 606, 613 (2d Cir. 1969) (“The arbitration clause states that arbitration is to be ‘held in the city where the home office of CED-ING COMPANY (Hamilton) is domiciled,’ which was and is New York City.”) Similarly, insurance agency and underwriting agreements frequently provide for arbitration in the appointing company's location. See, e.g., *Windward Agency, Inc. v. Cologne Life Reinsurance Co.*, No. 95-CV-07830, 1997 WL 164269, at *1 n.2 (E.D. Pa. Apr. 1, 1997) (“The General Agents Agreement provides, ‘It is agreed that the State of New York will govern the construction of this Agreement and that all disputes with regard to this Agreement, or any part thereof, unless we can settle such disputes amicably, must be submitted to arbitration at the domicile of the company.’” (emphasis omitted)).
- 33 The following states regulate or ban arbitration clauses in insurance policies, in whole or in part: Ariz. Rev. Stat. Ann. § 12-3003(B)(2); Ark. Code Ann. § 16-108-233(b)(3); Ga. Code Ann. § 9-9-2(c)(3); Haw. Rev. Stat. § 431:10-221(a)(2); Ky. Rev. Stat. Ann. § 417.050; La. Stat. Ann. § 22:868(A)(2); Me. Rev. Stat. tit. 24-A, § 2433; Md. Code Ann., Cts. & Jud. Proc. § 3-206.1(b)(1); Mass. Gen. Laws Ann. ch. 175, § 22; Mont. Code Ann. § 27-5-114(2)(c); Mo. Ann. Stat. § 435.350; Neb. Rev. Stat. Ann. § 25-2602.01(f)(4); Okla. Stat. Ann. tit. 12, § 1855(D); 10 R.I. Gen. Laws Ann. § 10-3-2; S.C. Code Ann. § 15-48-10(b)(4); S.D. Codified Laws § 21-25A-3; Vt. Stat. Ann. tit. 12, § 5653(a); Va. Code Ann. § 38.2-312(2); and Wash. Rev. Code Ann. § 48.18.200. State prohibitions on arbitration clauses in insurance policies do not always survive preemption by either the Federal Arbitration Act or, more so, the United Nations Convention. See, e.g., *Next Level Hosp. LLC v. Indep. Specialty Ins. Co.*, No. 2:21-CV-04240, 2023 WL 2771583, at *2 (W.D. La. Mar. 31, 2023) (“McCaran-Ferguson allows state laws like Louisiana Revised Statute section 22:868(A)(2) to ‘reverse-preempt’ the Federal Arbitration Act's provisions on the enforceability of insurance agreements. However, this ‘reverse preemption’ applies only to ‘Acts of Congress’ and not to treaties [like the U.N. Convention].” (citation omitted)); *Antoine's Rest, LLC v. Certain Underwriters at Lloyd's, London*, No. 23-CV-00229, 2023 WL 3751509, at *3 (E.D. La. June 1, 2023) (refusing to reconsider order compelling arbitration involving foreign insurers and, thus, implicating the U.N. Convention).
- 34 *Minnieland Priv. Day Sch., Inc. v. Applied Underwriters Captive Risk Assurance Co., Inc.*, 913 F.3d 409, 416 (4th Cir. 2019) (affirming district court's conclusion that a reinsurance participation agreement with respect to workers' compensation losses “is an insurance contract for purposes of Virginia Code § 38.2-312”); *Onken's Am. Recyclers, Inc. v. Cal. Ins. Co.*, 2018 IL App (4th) 180240-U, ¶ 41 (concluding that arbitration clause in reinsurance participation agreement that delegated authority to the arbitrator to determine enforceability violated Neb. Rev. Stat. § 25-2602.01(f)(4)).

- 35 *Arbitration Clauses in Insurance Contracts: The Urgent Need for Reform*, Public Citizen (n.d.), <https://www.citizen.org/article/arbitration-clauses-in-insurance-contracts-the-urgent-need-for-reform/>.
- 36 See Susan Randall, *Freedom of Contract in Insurance*, 14 Conn. Ins. L. J. 107, 124 (2007-2008) (“From the consumer’s perspective, standardization means that the insurance industry controls the content of the policy and that there is no negotiation over terms. Insurance policies are thus adhesion contracts, standard forms drafted by the insurer, offered on a take-it-or-leave-it basis, with the prospective policyholder at a complete disadvantage in terms of bargaining power.” (footnote omitted)); see *id.* at 123 (acknowledging a “possible exception” to the absence of bargaining power for “some large commercial policyholders”).
- 37 See, e.g., Stephen D. Allred, *Key Issues in Evaluating and Negotiating D&O Insurance Coverage*, Notes Bearing Interest, N.C. Bar Association, 18 (June 2014), <https://www.mcguirewoods.com/news-resources/publications/Key-Issues-D-O-Insurance-Coverage.pdf> (noting that directors’ and officers’ insurance policies are “not issued on standard forms” and that “there is a range of difference in the willingness of insurers to negotiate policy terms.”).
- 38 See, e.g., Peter A. Halprin & Daniel Garrie, *Arbitrating Cyber Coverage Disputes*, ABA (March 13, 2019), <https://www.americanbar.org/groups/litigation/committees/insurance-coverage/articles/2019/arbitrating-cyber-coverage-disputes/> (“Policyholders and brokers, however, should bear in mind that arbitration clauses can and should be the subject of negotiation. . . . As reshaped by negotiation . . . arbitration can be beneficial to policyholders as well as to insurance companies.”).
- 39 See, e.g., Andrew Nadolna, Adrienne Publicover, & Daniel B. Garrie, *Why Arbitration Clauses May Make Sense in Cyber Insurance Policies*, JAMS ADR Insights, 5 (Nov. 1, 2017), <https://www.jamsadr.com/publications/2017/why-arbitration-clauses-may-make-sense-in-cyber-insurance-policies> (describing the cyber market for insurers as highly competitive and noting that “[p]olicyholders can and are negotiating policy language” and that arbitration, especially for its confidentiality, may benefit policyholders).
- 40 See, e.g., *Geico Marine Ins. Co. v. Treasure Coast Mar., Inc.*, No. 2:18-CV-14419, 2019 WL 467854, at *3 (S.D. Fla. Feb. 6, 2019); *Royal Ins. Co. of Am. v. BHRS, LLC*, 333 F. Supp. 2d 1293, 1297 (S.D. Fla. 2004); *Revak v. SEC Realty Corp.*, 18 F.3d 81, 91 (2d Cir. 1994) (“Fraud in the factum occurs in those ‘rare cases’ where ‘the misrepresentation is regarded as going to the very character of the proposed contract itself, as when one party induces the other to sign a document by falsely stating that it has no legal effect.’” (quoting E.A. Farnsworth, *Contracts* § 4.10 (1990))).
- 41 See, e.g., *Solyamar Invs., Ltd. v. Banco Santander S.A.*, 672 F.3d 981, 994 (11th Cir. 2012) (distinguishing fraudulent inducement from fraud in the factum).
- 42 See, e.g., *Rock Hemp Corp. v. Dunn*, 51 F.4th 693, 703-04 (7th Cir. 2022) (discussing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404, 87 S.Ct. 1801, 18 L. Ed. 2d 1270 (1967)).
- 43 See, e.g., *In re StockX Customer Data Sec. Breach Litig.*, 19 F.4th 873, 882-83 (6th Cir. 2021) (“[I]f the claim is fraud in the inducement of the arbitration clause itself—an issue which goes to the ‘making’ of the agreement to arbitrate—the federal court may proceed to adjudicate it.” (quotation marks omitted) (quoting *Prima Paint*, 388 U.S. at 403-04)).
- 44 *ACE Cap. Re Overseas Ltd. v. Cent. United Life Ins. Co.*, 307 F.3d 24, 29 (2d Cir. 2002) (“It is well settled that a claim or defense of fraudulent inducement, when it challenges generally the enforceability of a contract containing an arbitration clause rather than specifically the arbitration clause itself, may be subject to arbitration.”) (quoting *Prima Paint*, 388 U.S. at 403-04).
- 45 See, e.g., *Manios Props., LLC v. Riverport Ins. Co. of Cal.*, No. 17-CV-01700, 2017 WL 3493125, at *3 (D. Ariz. Aug. 15, 2017) (refusing to compel arbitration, because the parties’ factual dispute over date of loss did not fall within the agreement to arbitrate over the meaning of a policy provision).
- 46 See, e.g., *Bufkin Enters. LLC v. Indian Harbor Ins. Co.*, No. 2:21-CV-04017, 2023 WL 2393700, at *8 (W.D. La. Mar. 7, 2023) (under Louisiana law, arbitration clause in insurance policy was unenforceable), *appeal filed*, No. 23-30171 (5th Cir. Mar. 27, 2023); *Galilea, LLC v. AGCS Marine Ins. Co.*, 879 F.3d 1052, 1057 (9th Cir. 2018) (under New York law, arbitration clause in an application for insurance was not an enforceable contract because the application was not attached to the policy); *All. Grp., Inc. v. Zurich Am. Ins. Co.*, No. 8:21-CV-00188, 2021 WL 5325883, at *3 (D. Neb. Nov. 16, 2021) (concluding that Nebraska prohibition on arbitration clauses in insurance policies did not apply, because the Court found enforceable the policy’s choice of New York law), *reconsideration denied*, No. 8:21-CV-00188, 2022 WL 1406670 (D. Neb. Jan. 7, 2022); *Nielsen Contracting, Inc. v. Applied Underwriters, Inc.*, 22 Cal. App. 5th 1096, 1115, 232 Cal. Rptr. 3d 282, 295 (2018) (concluding that arbitration clause in reinsurance participation agreement was unenforceable, because it was an unendorsed side agreement, prohibited by California insurance regulations); *Lexington Ins. Co. v. Exxon Mobil Corp.*, No. 9:16-CV-00357, 2017 WL 1532271, at *4 (Tex. Ct. App. Apr. 27, 2017) (reversing trial court’s conclusion that arbitration clause in insurance contract was unconscionable when applied to an additional insured).
- 47 See, e.g., *Minnieland Priv. Day Sch., Inc. v. Applied Underwriters Captive Risk Assurance Co., Inc.*, 867 F.3d at 454 (stating that the court must resolve in the first instance whether arbitration provision was unconscionable in delegating authority to arbitrator to resolve issues of arbitrability).
- 48 See, e.g., Xington He & Hinyan Jiang, *Research on the Selection of Arbitrators Based on Game Theory*, *Advances in Social Sciences, Education and Humanities Research*, vol. 415 (2020), <https://www.atlantispress.com/article/125936756.pdf>; Geoffroy de Clippel, Kfir Eliaz, & Brian Knight, *On the Selection of Arbitrators*, *The American Economic Review*, vol. 104, no. 11 (Nov. 2014), https://www.brown.edu/Departments/Economics/Faculty/Geoffroy_deClippel/selection.pdf.
- 49 Three well-known reinsurance arbitrators noted in 2010: “There are some who believe that the outcome of the dispute is determined once the umpire is selected.” Caleb Fowler, Robert M. Hall, & Lawrence O. Monin, *All-Neutral Arbitration Panels* (May 9, 2010), <https://debrahalljd.files.wordpress.com/2018/02/all-neutralpanelart.pdf>.
- 50 See *UBS Fin. Servs., Inc. v. Asociacion De Empleados Del Estado Libre Asociado De Puerto Rico*, 997 F.3d 15, 19 (1st Cir. 2021) (discussing the meaning of “evident partiality” for neutrals and noting that U.S.

Courts of Appeals have split on whether “a reasonable appearance of bias is sufficient to demonstrate evident partiality”).

- 51 In a well-known reinsurance case, the United States Court of Appeals for the Seventh Circuit flatly rejected a plea to vacate an award based on accusations of bias levied against the winning side’s party-appointed arbitrator. Writing for the Court, Judge Easterbrook noted that the absence of any precedent for this type of attack was “unsurprising, because in the main party-appointed arbitrators are supposed to be advocates.” *Sphere Drake Ins. Ltd. v. All Am. Life Ins. Co.*, 307 F.3d 617, 620 (7th Cir. 2002); see also *Nationwide Mut. Ins. Co. v. Home Ins. Co.*, 429 F.3d 640, 647 (6th Cir. 2005) (noting, with approval, that “[t]he rationale of *Sphere Drake* . . . places an onerous burden of proof on the party alleging evident partiality of a party-appointed arbitrator”); *Certain Underwriting Members of Lloyds of London v. Fla., Dep’t of Fin. Servs.*, 892 F.3d 501, 503-04 (2d Cir. 2018) (referring to the “higher burden to prove evident partiality on the part of an arbitrator who is appointed by a party and who is expected to espouse the view or perspective of the appointing party”); *Lozano v. Md. Cas. Co.*, 850 F.2d 1470, 1472 (11th Cir. 1988) (“[A]rbitrator appointed by a party is a partisan only one step removed from the controversy and need not be impartial.”).
- 52 For a detailed discussion of the history of American arbitration and the challenges of the tripartite process, see David Branson, *American Party-Appointed Arbitrators – Not the Three Monkeys*, 30 Univ. of Dayton L. R. No. 1 (2004), <https://ecommons.udayton.edu/udlr/vol30/iss1/1/>. See also Seth Lieberman, *Something’s Rotten in the State of Party-Appointed Arbitration: Healing ADR’s Black Eye that Is “Nonneutral Neutrals,”* 5 Cardozo J. Conflict Resol. 215 (2004); but see Olga Byrne, *A New Code of Ethics for Commercial Arbitrators: The Neutrality of Party-Appointed Arbitrators on a Tripartite Panel*, 30 Fordham Urb. L. J. 1815, 1840 (2003) (reporting from interviews with lawyers that the existence of party-appointed arbitrators in the reinsurance industry make awards more acceptable to the parties), <https://ir.lawnet.fordham.edu/ulj/vol30/iss6/1>.
- 53 In a case arising from a reinsurance arbitration, Judge Richard Posner observed:
- There is a tradeoff between impartiality and expertise. The expert adjudicator

is more likely than a judge or juror not only to be precommitted to a particular substantive position but to know or have heard of the parties (or if the parties are organizations, their key people). Expertise in an industry is accompanied by exposure, in ways large and small, to those engaged in it. . . . No one would dream of having a judicial panel composed of one part-time judge and two representatives of the parties, but that is the standard arbitration panel, the panel Leatherby chose—presumably because it preferred a more expert to a more impartial tribunal—when it wrote an arbitration clause into its reinsurance contract with Merit.

Merit Ins. Co. v. Leatherby Ins. Co., 714 F.2d 673, 679 (7th Cir. 1983) (quotation marks, ellipses, and citations omitted), *amending mandate*, 728 F.2d 943 (7th Cir. 1984).

- 54 For a discussion of how impartiality hinges on the various roles that a decision-maker plays, see Catherine Rogers, *Regulating International Arbitrators: A Functional Approach to Developing Standards of Conduct*, 41 Stan. J. Int’l L. 53, 120 (2005), https://elibrary.law.psu.edu/cgi/viewcontent.cgi?article=1235&context=fac_works (arguing that “‘impartiality’ as applied to arbitrators is distinct from its definition in the judicial context” and suggesting the possibility of licensing as a means to regulate arbitrator conduct).
- 55 To be sure, it is not “cheating” for parties to act in their own self-interest in selecting nominees that they perceive will be at least fair. See, e.g., William W. Park, *Arbitrator Bias*, Boston University School of Law, Public Law Research Paper, No. 15-39, 19 (2015) (“Even if a litigant knows that an arbitrator cannot be in its pocket, the litigant may, understandably, still hope to appoint someone who falls into its corner doctrinally.”).
- 56 *Dow Corning Corp. v. Safety Nat’l Cas. Corp.*, 335 F.3d 742 (8th Cir. 2003).
- 57 *Id.* at 750.
- 58 *Nat’l Union Fire Ins. Co. of Pittsburgh, PA v. Beelman Truck Co.*, No. 17-CV-02946, 2017 WL 3049550, at *2 (S.D.N.Y. July 17, 2017).
- 59 In the authors’ opinion, the vast majority of arbitrators possess a high degree of integrity and have earned good reputations that they would not surrender.
- 60 Under the ARIAS-U.S. Code of Conduct,

“[p]arty-appointed arbitrators may communicate with the party who is considering appointing them about their fees and, excepting those who by contract are required to be ‘neutral’ or the equivalent, may also communicate about the merits of the case prior to acceptance of the appointment until the date determined for the cessation of ex parte communications.” ARIAS-U.S., Code of Conduct, Canon V, cmt. 2, <https://www.arias-us.org/arias-us-dispute-resolution-process/code-of-conduct/code-of-conduct-canon-v/>.

- 61 For example, *Nationwide Mutual Insurance Co. v. Home Insurance Co.*, 429 F.3d at 642-43 concerned a multi-phase arbitration process preside over by three arbitration panels. Despite its familiarity with the dispute by the time it chose an arbitrator for the final phase, Nationwide’s appointed arbitrator in phase three joined with the other two arbitrators to issue a unanimous decision that, while somewhat mixed, largely favored the reinsurer, Home. Nationwide unsuccessfully attempted to have the award vacated based on the alleged bias and non-disclosures of Home’s party-appointed arbitrator.
- 62 Some arbitral systems allow for interviews of umpire candidates at least to some degree. See William W. Park, *Arbitrator Bias*, Boston University School of Law, Public Law Research, Paper No. 15-39, 17 (2015), https://scholarship.law.bu.edu/faculty_scholarship/15/ (noting that in international arbitrations “limited interview of candidates by counsel has been allowed, at least with safeguards to avoid discussion of the merits of the case.”). Aside from allowing the parties jointly to pose limited inquiries in the umpire questionnaire regarding the subject matter of the arbitration, the ARIAS-U.S. Code of ethics proscribe ex parte communications with umpire candidates by a party, its counsel, or party-appointed arbitrator. Compare ARIAS-U.S. Umpire Questionnaire, at 4, <https://www.arias-us.org/wp-content/uploads/2017/04/ARIAS-U.S.-Questionnaire-Umpire-Selection-1-2-17-Fillable.pdf> with ARIAS-U.S. Code of Ethics, Canon I, cmt.3, <https://www.arias-us.org/wp-content/uploads/2019/07/ARIAS-Code-of-Conduct-Canon-I-2019-Update.pdf> (identifying as a circumstance in which a neutral must decline an appointment: “where the candidate is nominated for the role of umpire and the candidate was contacted prior to nomination by a party, its counsel or the

- party's appointed arbitrator with respect to the matter for which the candidate is nominated as umpire").
- 63 An arbitration clause in one contract may specify qualifications for the arbitrators that differ from the qualifications that appear in another contract. This inconsistency may present an issue in a consolidated arbitration covering disputes under multiple contracts. A court may need to resolve an impasse in the selection process based on differences in the applicable criteria. See, e.g., *Safety Nat'l Cas. Corp. v. Certain Underwriters at Lloyd's London*, No. 2-CV-01146, 2011 WL 3610411, at *1-2 (M.D. La. Aug. 16, 2011) (stating that where some but not all of the 22 contracts at issue called for an "umpire who is an expert in the field of workers compensation reinsurance," the Court decided to compel the parties to nominate candidates who met the "most restrictive and narrow provisions of the contracts at issue").
- 64 See *Odyssey Reinsurance Co. v. Certain Underwriters at Lloyd's London Syndicate* 53, 615 F. App'x 22, 23 n.2 (2d Cir. 2015) (holding that a district court may examine a candidate's "qualifications to serve" as umpire incidental to its authority to appoint an umpire pursuant to FAA § 5, 9 U.S.C. § 5). Other decisions, however, hold that courts cannot intercede during the pendency of an arbitration to address claims either of arbitrator bias or of any failure to meet the contractual requirements. See, e.g., *Savers Prop. & Cas. Ins. Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 748 F.3d 708, 720 (6th Cir. 2014); *Gulf Guar. Life Ins. Co. v. Conn. Gen. Life Ins. Co.*, 304 F.3d 476, 491 (5th Cir. 2002) ("[A] court may not entertain disputes over the qualifications of an arbitrator to serve merely because a party claims that enforcement of the contract by its terms is at issue, unless such claim raises concerns rising to the level that the very validity of the agreement be at issue."); *John Hancock Life Ins. Co. (U.S.A.) v. Employers Reassurance Corp.*, No. 15-CV-13626, 2016 WL 3460316, at *4 (D. Mass. June 21, 2016); see also *Aviall, Inc. v. Ryder Sys., Inc.*, 110 F.3d 892, 895-96 (2d Cir. 1997) (refusing to consider whether arbitrator met the criteria of being an "independent" auditor because of its relationship to one of the parties.).
- 65 *Drobny v. Am. Nat'l Ins. Co.*, No. 1:12-CV-01034, 2013 WL 4680411 (Tex. App. Aug. 29, 2013).
- 66 *Nat'l Cas. Co. v. OneBeacon Am. Ins. Co.*, No. 12-CV-11874, 2013 WL 3335022 (D. Mass. July 1, 2013), *aff'd sub nom., Emps Ins. Co. of Wausau v. OneBeacon Am. Ins. Co.*, 744 F.3d 25 (1st Cir. 2014).
- 67 *OneBeacon Am. Ins. Co. v. Swiss Reinsurance Am. Corp.*, No. 9-CV-11495, 2010 WL 5395069 (D. Mass. Dec. 23, 2010).
- 68 *Nat'l Cas. Co.*, 2013 WL 3335022, at *2.
- 69 *Nat'l Cas. Co.*, 2013 WL 3335022, at *4 (quoting from email sent by OneBeacon's counsel).
- 70 *Nat'l Cas. Co.*, 2013 WL 3335022, at *8 (concluding that the preclusive effect of the earlier award was a matter for the arbitrators in the later arbitration to decide).
- 71 *Nat'l Cas. Co.*, 2013 WL 3335022, at *11-12 (reasoning that the FAA does not authorize courts to intercede in pending arbitrations to remove arbitrators for alleged bias, much to eliminate the candidacy of someone who might or might not become an arbitrator.).
- 72 *Lexington Ins. Co. & Chartis, Inc. v. S. Energy Homes*, 101 So. 3d 1190, 1202-03 (Ala. 2012).
- 73 *Id.* at 1207.
- 74 *Wright Med. Grp., Inc. v. Lexington Ins. Co.*, No. 18-CV-02571, 2018 WL 7437049, at *2 (Mass. Super. Ct. Dec. 20, 2018), *judgment entered*, 2018 WL 8996184 (Mass. Super. Ct. Dec. 19, 2018).
- 75 Lexington relied on AAA Commercial Rule 18(a), which provides:
- R-18. Disqualification of Arbitrator
- (a) Any arbitrator shall be impartial and independent and shall perform his or her duties with diligence and in good faith, and shall be subject to disqualification for:
- i. partiality or lack of independence,
- ii. inability or refusal to perform his or her duties with diligence and in good faith, and
- iii. any grounds for disqualification provided by applicable law.
- Am. Arbitration Ass'n Commercial Arbitration Rules and Mediation Procedures, R-18, <https://adr.org/sites/default/files/Commercial%20Rules.pdf>.
- 76 *Wright Med. Grp.*, 2018 WL 8996184, at *1.
- 77 See, e.g., *Gulf Guar. Life Ins. Co.*, 304 F.3d at 490 ("[E]ven where arbitrator bias is at issue, the FAA does not provide for removal of an arbitrator from service prior to an award, but only for potential vacatur of any award. . . . [T]he FAA appears not to endorse court power to remove an arbitrator for any reason prior to issuance of an arbitral award."); *Smith v. Am. Arb. Ass'n, Inc.*, 233 F.3d 502, 506 (7th Cir. 2000) ("The time to challenge an arbitration, on whatever grounds, including bias, is when the arbitration is completed and an award rendered."); *Aviall, Inc.*, 110 F.3d at 895 ("Although the FAA provides that a court can vacate an award where there was evident partiality or corruption in the arbitrators, it does not provide for pre-award removal of an arbitrator." (quotation marks, alteration marks, and citation omitted)).
- 78 For example, *MSE Distributing, Inc. v. Southwest. Reinsure, Inc.*, No. 10-CV-00880, 2011 WL 13216989 (D.N.M. Mar. 9, 2011) involved in dispute over whether the respondent owed commissions to agents after terminating them. The agent-petitioners appointed all three arbitrators after the respondent failed to participate in the selection process. After the arbitrators issued an award granting petitioners over \$4 million, the respondent moved to vacate arguing, among other things, that the arbitrators were not "executive officers or retired officers of insurance companies," as the contracts required. The Court found that the respondent failed to object to the arbitrators' qualifications at the time of the hearing, as required, and that the arbitrators met the contractual requirements. *Id.* at *11-12.



Extending the Time Limit for a Motion to Vacate an Arbitration Award For Texting to a Witness During an Arbitration by Video Conference

By Robert M. Hall

I. Introduction

The parties to an arbitration may seek to vacate an arbitration award “procured by corruption, fraud or undue

means” under Section 10 of the Federal Arbitration Act (“FAA”). However, the motion must be served on the adverse party within three months after the award is made pursuant to Section 12

of the FAA. There are no exceptions to this time limit in the statute but there are some exigent circumstances (indeed a shocking one examined immediately below) that have caused some courts to

devise an exception to the three-month time limit.

II. Exception to the Three-Month Ruling for Motions to Vacate an Arbitration Award

NuVasive, Inc. v. Absolute Medial, LLC, No. 22-10214 (11th Cir. Jun. 21, 2023), involved a breach of contract and other claims related to the sale of medical products. The breach of contract claim was subject to arbitration. During litigation of the remaining issues, the defendant delayed producing documents even after the court issued an order to compel. Eventually, the defendants produced documents, and, on November 15, 2021, plaintiffs filed a motion to vacate the March 4, 2021, final arbitration award based on the document production revealing that during the arbitration proceeding, one of the defendants prompted the testimony of a witness by text message.

The defendant in *NuVasive* argued that the plaintiff had missed the June 4, 2021 deadline to serve the motion to vacate. The district court granted “equitable tolling” on the three-month limit for a motion to vacate based on a three-part test: (1) fraud must be established by the movant by clear and convincing evidence; (2) fraud must not have been discoverable with due diligence before or during the arbitration; and (3) a demonstration that the fraud materially related to an issue in the arbitration.¹ The district court went on to vacate the arbitration award.

The 11th Circuit Court of Appeals in *NuVasive* affirmed the district court and followed the Ninth Circuit in *Move, Inc. v. Citigroup Global Markets,*

Inc., 840 F.3d 1152 (9th Cir. 2016), examined below. The *NuVasive* court characterized the actions of the defendant and the witness as “shocking” in that: (1) the witness took an oath that nobody else was in the room with him or communicating with him; (2) there was clear evidence that the defendant prompted the witness’ testimony; (3) after the conduct was discovered, the witness submitted a declaration that this was not the case; (4) the defendants clearly tried to run out the clock on the motion to vacate; and (5) plaintiff acted promptly after defendant’s actions were discovered. The court ruled: “NuVasive satisfied both prongs of the equitable tolling analysis. The defendants’ conduct presented extraordinary circumstances, and NuVasive was diligent once it learned that there was reason to pursue vacatur.”²

The *NuVasive* court followed the earlier decision of *Move, Inc. v. Citigroup Global Market, Inc.*, 840 F. 3d 1152 (9th Cir. 2016). This case involved an arbitration related to a dispute over a transaction governed by the Financial Industry Regulatory Authority (“FINRA”). FINRA provided a list of approved arbitrators and the plaintiff selected as umpire an individual with a certain desired background. The arbitration panel found for the defendant and the plaintiff learned four years later that the umpire was an impostor without the desired background. Two and one-half months later, the plaintiff filed a motion to vacate.

Initially, the *Move* court noted that caselaw on equitable tolling under the FAA was conflicted³ but found a rebuttable presumption that the three-month limit on motions to vacate was subject to equitable tolling.⁴ The court

next addressed the compatibility of equitable tolling with the structure of the FAA:

[A] moving party would still need to meet the heavy burden of establishing its entitlement to equitable tolling for a court to vacate an award, and it would only be the rare case in which the three-month deadline for a motion to vacate would not apply. We therefore find that the structure of the FAA is compatible with equitable tolling.⁵

The court then found that the FAA was subject to equitable tolling:

Balancing the needs for both finality and due process, the arbitral process will not be disrupted if parties are permitted to satisfy the high bar of equitable tolling in limited circumstances. More importantly, permitting equitable tolling will enhance both the accuracy and fairness of arbitral outcomes.⁶

The *Move* court went on to vacate the arbitration award. *See also, Jesus v. United Health Group*, No. CV-22-00532-PHX-DJH (D. Ariz. Jan. 23, 2023).

III. Caselaw Rejecting Equitable Tolling for Motions to Vacate Arbitration Orders

Florasynth, Inc. v. Pickholz, 750 F. 2d 171 (2nd Cir. 1984), involved an employment-related dispute subject to arbitration. The arbitration panel issued an order in favor of the employer. When the employer moved to confirm the award four months later, the employee moved to vacate the arbitration award. The court found that there was nothing in the FAA or common law that would support an exception to the

three-month time limit. As to the policy behind the limit, the court commented:

[P]arties choose to arbitrate because they want quick and final resolution of their disputes. The role of arbitration as a mechanism for speedy dispute resolution disfavors delayed challenges to the validity of an award. Thus, when a party to an arbitration believes that he has been prejudiced in the proceedings by behavior that the [FAA] condemns he [sic] bring a motion to vacate within the allotted time. When the three-month limitations period has run without vacation of the arbitration award, the successful party has a right to assume the award is valid and untainted and to obtain its confirmation in a summary proceeding.⁷

See also *M.J. Woods, Inc. v. Conopco, Inc.*, No. 01 Civ. 3135 (S.D. N.Y. 2003).

IV. Caselaw Finding a Lack of a Factual Basis for Equitable Tolling

The losing party in an arbitration claimed an arbitrator's lack of disclosure demonstrated evident partiality in *A. Miner Contracting, Inc. v. Dana Kepner Co.*, No. 16-15209 (9th Cir. Aug. 27, 2017). The motion to vacate was served on the adverse party more than three years after the panel award. The court acknowledged the exception enunciated in *Move*, but found that the party had not acted with due diligence:

Tolling is not warranted in this case because Miner did not act with due diligence – in particular, it has not alleged circumstances beyond its control that prevented it from discovering the evidence on which it

“[P]arties choose to arbitrate because they want quick and final resolution of their disputes.”

now relies. Indeed, Miner admits that it uncovered the information that it contends shows bias on the part of the arbitrator by searching the internet. Because the information on which Miner relies was readily available to it during the limitations period, tolling of the limitations period is not justified.⁸

Taylor v. Nelson, 788 F.2d 220 (4th Cir. 1986) involved the failure of Willie Nelson to perform at a concert. On September 11, 1984, the arbitration panel issued an award in favor of Nelson and his attorneys filed a motion in New York to confirm on September 21. The opposing party challenged the jurisdiction of the New York court to confirm and that court, on February 1, 1985, ruled that a Virginia federal court was the proper court for the confirmation motion. On February 12, 1985, the opposing party filed a motion to vacate. The court questioned whether equitable estoppel was a proper exception to the three-month rule for motions to vacate but ruled, in any case, that the seven-month period between the arbitration ruling and the motion to vacate required a ruling for Nelson:

We do not consider, however, whether due diligence or tolling rules are proper exceptions to the

limitations period prescribed by the Federal Arbitration Act, for we conclude that Tayler did not, in any event, act with due diligence, and was not prevented by the pendency of the New York proceeding from making a timely motion to vacate in the district court.⁹

For a District Court's reading of *Taylor v. Nelson*, see *Lawson-Jackson v. Rosenhaus*, Civil Action No. TDC-16-4049 (D. Md. Sep. 12, 2017).

Ballantine v. Dominican Republic, No. 20-7086 (D.C. Cir. Oct. 22, 2021), emphasized that section 12 of the FAA requires that the motion to vacate must be *served* on the adverse party within three months, not just *filed*. In this case, the appellants filed the motion on the last day of the three-month period but did not affect a proper service until 1.5 months later. The court ruled that “served” means what it says. The court stated that “even if equitable tolling were [sic] available, Appellants would not so qualify”¹⁰ due to lack of diligence in effecting service or any other extraordinary circumstances beyond their control.

V. Commentary

It appears from the above caselaw that the application of equitable estoppel related to a motion to vacate is fact-specific. Lack of due diligence or even ordinary problems in formulating and affecting service is not an excuse for failing to meet the three-month deadline since the court favors finality to arbitration proceedings. But truly extraordinary and unforeseeable barriers to understanding and acting on a basis for a motion to vacate are likely to receive a more favorable reception in most courts.



Robert Hall spent 20 years as in-house counsel for various insurers and reinsurers, most recently as senior vice president, general counsel and director of a major reinsurer. He is a former partner of a leading law firm and currently is an ARIAS-certified arbitrator and umpire, an expert witness and a frequent author whose articles can be found on his website: robertmhalladr.com. Hall is on the Editorial Board of the ARIAS Quarterly.

Endnotes

- 1 *Slip op.* at 15.
- 2 *Slip op.* at 28.
- 3 840 F.3d 1152 at 1156.
- 4 *Id.* at 1156-7.
- 5 *Id.* at 1157.
- 6 *Id.*
- 7 750 F.2d 171 at 177.
- 8 *Slip op.* at 3.
- 9 788 F.2d 220 at 225.
- 10 *Slip op.* at 3.

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A Brief Summary of Two Recent Massachusetts Arbitration Cases

By Philip M. Howe, Esq., *ARIAS Certified Arbitrator, Boston, MA.*

A federal court in Boston ruled that parties must arbitrate the issue of arbitrability even though the agreement required only that any disagreement between the parties must be arbitrated in accordance with the AAA Rules and did not specify that the arbitrator would decide the issue of arbitrability.

The plaintiff, American Graphics Institute (“AGI”) provided professional development and technical training to companies on graphics, design, and marketing. The defendant, Noble Desktop (“Noble”) operated a business similar to AGI. Noble entered into an agreement with AGI to perform services for AGI. A related agreement provided that disputes, that could not be mediated, “..will then be resolved solely and exclusively by binding arbitration conducted in accordance with the then effective Commercial Arbitration Rules of the American Arbitration Association...”

AGI alleged that Noble improperly used AGI’s “trademarks, copyrighted works, and goodwill to attract customers to its competing business.” AGI filed an action alleging copyright and trademark infringement. Noble moved to dismiss and compel arbitration.

The Court relied on *Air-Con, Inc. v. Dalkin Applied*, 21 F. 4th 168, 174 (1st Circuit 2021). which in turn had relied on the U.S. Supreme Court’s decision in *Henry Schein v. Archer & White Sales*,

139 S. Ct. 524, 529 (2019) and cited the Federal Arbitration Act, 9 USC Sections 1 – 16, particularly Section 4.

The issue in this case was whether the matter should be arbitrated at all; i.e., the issue of arbitrability. The arbitration provision in the agreement provided that the matter will be resolved in accordance with the rules of the A.A.A. Rule 7(a) of the A.A.A. states that the “arbitrator shall have the power to rule on his or her own jurisdiction.” The court noted that the Supreme Court had not yet taken a position on whether incorporating the A.A.A. Rules is clear evidence of the intent of the parties to delegate arbitrability. But, many federal courts of appeal have done so, including the First Circuit. *Awuah v. Coverall N.M. Inc.*, 554 F. 3d 7, 11 (1st Circuit 2009).

Consequently, the court ruled that the authority to determine arbitrability has been delegated to the arbitrator. Because the court found only that the threshold issue of arbitrability was arbitrable, the court did not grant the motion to dismiss. Instead, it stayed the action pending a decision by the arbitrator on the arbitrability of AGI’s claims

Case: *American Graphics Institute v. Noble Desktop NYC*, No.22-cv-11404-ADB (D. Mass. Jul. 27, 2023)

Issues Discussed: Who determines arbitrability of the dispute where arbitrability was not specifically provided for in the arbitration agreement.

Issue Decided: Where the arbitration agreement provided that disputes were to be resolved in accordance with the rules of the American Arbitration Association (“AAA”), and those rules provide that the arbitrator has the power to rule on his or her own jurisdiction, the arbitrator will decide the issue of arbitrability.

Submitted by: Philip M. Howe, Esq., ARIAS Certified Arbitrator, Boston, MA.

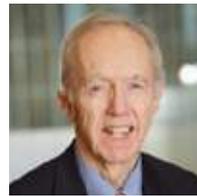
The Massachusetts Appeals Court has enforced an arbitration provision in an agreement a patient had signed with his eye surgeon even though the Spanish-speaking patient had very little understanding of English.

Prior to eye surgery, a patient signed a form agreement with a provision that any disputes regarding the surgery would be submitted to arbitration. Following the surgery, the patient filed an action for medical malpractice against the surgeon. The surgeon moved to dismiss the action and to compel arbitration.

The court ruled that arbitration agreements regarding interstate commerce are governed by federal and state law. *Miller v. Cotter*, 448 Mass. 671, 678 (2007), holds that health care is interstate commerce. The U.S. Supreme Court ruled that states may not decide that a contract is fair enough to enforce

all its basic terms, but not its arbitration clause. *Allied-Bruce Terminix v. Dobson*, 513 U.S. 265, 281 (1995).

The court ruled that there had been reasonable notice of the terms of the agreement with the surgeon and the plaintiff had manifested his assent. The agreement included a provision that the plaintiff “has read, understands, and had an opportunity to refuse to execute this arbitration agreement and agreed to be legally bound by its terms.” A Spanish-speaking staff member in the surgeon’s office was available to the plaintiff to discuss any of the documents if necessary.



Philip M. Howe is a civil litigator with lengthy experience in defending complex medical and financial issues.

Case: *Rivera v. Stetson*, No. 22-P-904 (Mass. App. Aug. 31, 2023)

Issues Discussed: Whether the arbitration provision was enforceable where the patient spoke Spanish and had very limited English in an agreement between a patient and an eye surgeon.

Issue Decided: The arbitration provision was enforceable as the patient had access to an interpreter and had the option not to sign the agreement.

Submitted by: Philip M. Howe, Esq., ARIAS Certified Arbitrator, Boston, MA.

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Insurers and Reinsurers, Here and Abroad, Should Pay Attention

The Second Circuit May Well Reconsider Reverse-Preemption of The New York Convention by the McCarran-Ferguson Act

By Edward K. Lenci

A significant number of states prohibit or restrict the arbitration of disputes between an insurer and its policyholder and/or preclude the inclusion of arbitral provisions in insurance policies.¹ The McCarran-Ferguson Act ("MFA")² is a federal statute that generally precludes an "Act of Congress" from preempting state statutes involving the business of insurance.³ The Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958, com-

monly known as the New York Convention (the "Convention"), is a treaty of the United States and the foundation of the international system of arbitration. Its enabling legislation is Chapter 2 of the Federal Arbitration Act ("FAA Chapter 2").⁴ However, the federal Circuit Courts of Appeals are split about whether MFA reverse-preempts the Convention.⁵ The First, Fourth, Fifth, and Ninth Circuits have held that the Convention preempts MFA while the

Second and Eighth Circuits have held that the MFA reverse-preempts the Convention.⁶ The Supreme Court may decide to resolve this split of authority in the future, but that is a discussion for another day.

Today's discussion arises from the decision of the U.S. District Court for the Southern District of New York, on August 15, 2023, in *Certain Underwriters at Lloyds v. 3131 Veterans Blvd LLC*.⁷

There, the court followed, as it must, the Second Circuit's holding in *Stephens v. American International Insurance Co.*⁸ that the MFA reverse-preempts the Convention. If the insurers appeal, it will be interesting to see whether the Second Circuit changes its mind on reverse preemption.

By way of background, MFA exempts insurance from most federal regulations. Congress enacted the MFA in 1945 after the U.S. Supreme Court overruled a long-standing precedent in *U.S. v. South-Eastern Underwriters Association*,⁹ holding that the Commerce Clause of the U.S. Constitution¹⁰ allowed Congress to regulate the business of insurance. The MFA provides in pertinent part as follows:

5 U.S.C. § 1012. Regulation by State law; Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948.

- a) State regulation. The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
- b) Federal regulation. No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance[.]

According to the National Association of Insurance Commissioners ("NAIC"), "[t]he fundamental reason for govern-

ment regulation of insurance is to protect American consumers," and state regulation of insurance is preferable because "[s]tate insurance regulatory systems are accessible and accountable to the public and sensitive to local social and economic conditions[,] [and] [s]tate regulation has proven that it effectively protects consumers and ensures that promises made by insurers are kept."¹¹ It should be well noted, though, that in response to the financial crisis of 2007-08, Congress broadly expanded the federal government's involvement in the regulation of the business of insurance with the enactment of Title V of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-

Frank"), including the establishment of a Federal Insurance Office, as part of the Treasury Department, with authority over most areas of insurance, the major exceptions being health, long-term care, and crop insurance.¹² As an "Act specifically relate[d] to the business of insurance," Title V of Dodd-Frank is not subject to the MFA.

Turning back to *Stephens*, the Second Circuit held that the MFA preempts the Convention despite the Supremacy Clause of the U.S. Constitution,¹³ thus permitting reverse-preemption of the Convention by Kentucky's Liquidation Act in that case. The Second Circuit reasoned that "the Convention is not

“Our constitution declares a treaty to be the law of the land. It is, consequently, to be regarded in courts of justice as equivalent to an act of the legislature, whenever it operates of itself, without the aid of any legislative provision.”

self-executing, and therefore, relies upon an Act of Congress for its implementation[.]" *viz.*, FAA Chapter 2. In support of this holding, the Second Circuit quoted an 1829 decision of the U.S. Supreme Court penned by Chief Justice John Marshall:

A treaty is, in its nature, a contract between two nations, not a legislative act. It does not generally effect, of itself, the object to be accomplished; especially, so far as its operation is infra-territorial; but is carried into execution by the sovereign power of the respective parties to the instrument. In the United States, a different principle is established. Our constitution declares a treaty to be the law of the land. It is, consequently, to be regarded in courts of justice as equivalent to an act of the legislature, whenever it operates of itself, without the aid of any legislative provision. But when the terms of the stipulation import a contract -- when either of the parties engages to perform a particular act, the treaty addresses itself to the political, not the judicial department; and the legislature must execute the contract, before it can become a rule for the court.¹⁴

Congress shall be construed to ... supersede any law ... regulating the business of insurance.' 15 U.S.C. § 1012(b) (1994). Accordingly, the implementing legislation does not preempt the Kentucky Liquidation Act[.] ...The Convention itself is simply inapplicable in this instance."¹⁵

In May, the First Circuit, in *Green Enters., LLC v. Hiscox Syndicates Ltd.*, became the latest Circuit Court to disagree with *Stephens*. Based on the Supreme Court's 2008 decision in *Medellín v. Texas*,¹⁶ the First Circuit held that "the text of the Convention makes plain that Article II(3) provides a clear 'directive to domestic courts.' *Medellín*, 552 U.S. at 508. Article II(3), by its express terms, directly commands courts to channel arbitrable disputes to arbitration: "The court ... shall ... refer the parties to arbitration...."¹⁷ In other words, the Convention is a self-executing treaty. In so deciding, the First Circuit followed the Ninth Circuit's 2021 holding in *CLMS Management Services LP v. Amwins Brokerage of Ga., LLC*,¹⁸ which in turn relied on a concurrence in the Fifth Circuit's 2009 *en banc* decision in *Safety National Casualty Corp. v. Certain Underwriters*.¹⁹ Additionally, the *en banc* Fifth Circuit, over the

an "Act of Congress" and not "a treaty implemented by an Act of Congress,"²⁰ and the Fourth Circuit agreed in 2012, in *ESAB Group, Inc. v. Zurich Insurance PLC*.²¹

Furthermore, the First, Fifth, Fourth, and Ninth Circuits all called into question the Second Circuit's reasoning. The First Circuit observed as follows: "... *Stephens* predated *Medellín*, offered no analysis of the text of Article II(3), and contained little explanation for why it concluded that the Convention was in relevant part non-self-executing."²² The Ninth Circuit made the same point in 2021.²³

The *en banc* Fifth Circuit, in *Safety National*, offered an additional criticism of *Stephens* based on a footnote in a subsequent decision of the Second Circuit:

We also note that the reasoning of the Second Circuit in *Stephens v. American International Insurance Co.* is at least in tension with that of its subsequent decision in *Stephens v. National Distillers & Chemical Corp.* [69 F.3d 1226 (2d Cir. 1995)], in which the Second Circuit held that the McCarran-Ferguson Act did not cause a state law requiring out-of-state insurers to post security before participating in court proceedings to preempt the Foreign Sovereign Immunities Act. In support of its first alternative ground for that holding, the Second Circuit reasoned that it must "apply federal law to the insurance industry, in spite of the McCarran-Ferguson Act, whenever federal law clearly intends to displace all state laws to the contrary." The McCarran-Ferguson Act does not "force a federal law that clearly intends to preempt all other state laws to give way sim-

“A treaty is, in its nature, a contract between two nations, not a legislative act.”

The Second Circuit then added that "McCarran-Ferguson states' no Act of

dissent of three judges, held in *Safety Nat'l* that the text of the MFA applies to

ply because the insurance industry is involved." In a footnote appended to this statement, the court concluded that because an additional, alternate ground (that international law preempted the state insurance law before the passage of both the McCarran-Ferguson Act and the Federal Sovereign Immunities Act) supported its holding, it "need not consider whether [its decision to apply federal law when it was clearly intended to displace all state law] is in conflict with the holding in *[Stephens v. American [International Insurance Co.]*."²⁴

The Fourth Circuit agreed with the Fifth Circuit on this point in *ESAB Group*.²⁵

All of the foregoing points, and assuredly more from the detailed discussions in the decisions of the First, Fourth, Fifth, and Ninth Circuits, will undoubtedly be made in the event of an appeal from *3131 Veterans Blvd LLC*. If there is an appeal, the states that prohibit or restrict the arbitration of insurance disputes will be watching closely and, so too, insurers and reinsurers in the United States and the world over should be watching closely.



Edward K. Lenci is a partner in the New York City office and Chair of the Reinsurance Section of the global Insurance Services Practice Group of Hinshaw & Culbertson LLP. Lenci is now in his fourth decade of practice with a track record of achieving successful outcomes for his clients in U.S.-based and international arbitrations, commercial disputes, rein-

sureance disputes, appeals, or when they find themselves the target of consumer class action lawsuits. He is the long-time chair of the Reinsurance Section of Hinshaw's global Insurance Services Practice Group. His full profile can be found at <https://www.hinshawlaw.com/professionals-edward-lenci.html>

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- 3 15 U.S.C. § 1012(b), titled "Federal regulation," states that, "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance...."
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- 9 *U.S. v. South-Eastern Underwriters Assoc.*, 322 U.S. 533 (1944).
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- 17 *Green Enters.*, 68 F.4th at 667-68.
- 18 *CLMS Mgmt. Servs. LP v. Amwins Brokerage of Ga., LLC*, 8 F.4th 1007, 1015-16 (9th Cir. 2021), cert. denied, 142 S. Ct. 862, 211 L. Ed. 2d 569, 2022 U.S. LEXIS 545 (2022)
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Punitive Damages, Extra-Contractual Obligations, and Losses in Excess of Policy Limits

By Frank DeMento

Introduction

Punitive damage awards often make headlines in civil liability litigation. Similarly, Extra Contractual Obligations (ECOs) and Excess of Policy Limits (XPLs) are inextricably linked and equally important because they also impact insurer behavior, claim negotiations, and final settlements. I offer an analysis of all three.

Punitive Damages

In civil litigation, compensatory damages seek to restore the plaintiff to pre-injury conditions. Punitive damages may also be awarded, but always in addition to compensatory awards, never alone. Punitive damages are designed to punish the defendant, send a message to society at large and act as a deterrent to others who may consider similar courses of action. Punitive dam-

ages are an exception to a key principle of the civil tort system, that tort damages are intended to restore the victim back to pre-injury conditions. Punitive damage awards allow the victim to be compensated beyond their pre-injury condition, which is why some jurisdictions take issue with the concept.

Within the U.S., different rules apply in each state – some do not recognize punitive damages at all, while others pro-

hibit their insurability, to reinforce the punishment aspect and to deter repeat behavior. As a brief comparison:

Most Favorable Jurisdiction

Intended to circumvent state prohibitions, this clause allows insured and

State	Allowable?	Insurable?	Beneficiary
Alabama	Yes	Yes	Claimant – no portion payable to State
Arizona	Yes	Yes	Claimant (other than Environment Impairment liability which is paid to the State)
California	Yes	No	State – not recoverable by the Claimant
Colorado	Yes	No	Claimant
Nebraska	No	N/A	N/A
Utah	Yes	No	50% of any award in excess of \$20,000 is paid to the State

Even when punitive damages are allowed, many states apply limitations as to how much can be awarded. The monetary amount of these “caps” varies by state. The most common caps are a fixed dollar amount or a multiple of the total compensatory damages award. Damage caps are an attempt by state legislatures to manage the high costs of doing business within a particular state and to prevent a drag on the overall economy.¹ Capping punitive damages prevents the increased costs of doing business from being ultimately passed on to the consumer. Additionally, they are meant to discourage plaintiffs from filing frivolous lawsuits with the hopes of a financial windfall.

Insuring Punitive Damages

Affirmative Cover

Explicit wording avoids any ambiguity, but affirmative wording cannot override state law – if punitive damages are not insurable in the state, then the policy will not respond.

insurer to choose a favorable jurisdiction to govern the policy, but only if the parties have some connection to the selected jurisdiction. The jurisdiction must be one of the following:

- where the wrongdoing occurred
- the location where the insured is incorporated
- where the original policy was issued

Punitive Wrap

Puni-wrap policies are separate, stand-alone indemnity covers providing difference in conditions coverage for punitive damages in states where punitive damages are not insurable. These policies are issued outside the U.S. (often Bermuda) to avoid coverage gaps in states that prohibit punitive damage coverage. The controlling policy covers compensatory damages while the puni-wrap policy covers any punitive damages. Puni-wrap policies come with some standard conditions:

- compensatory damages must be awarded
- the limit is shared between the companion policy and the puni-wrap policy. The amount of coverage available for punitive damages

under the puni-wrap policy is reduced by the amount of the compensatory damages award covered by the companion policy.

- both damages must be from the same incident
- the insured must have paid the punitive damages
- punitive damages would have been covered under the companion policy, but for state law.
- if the standard policy doesn't cover a claim, the puni-wrap won't provide coverage

In addition, puni-wraps are only triggered by “final judgments,” not for out of court settlements. Because final judgment means the exhaustion of any possible appeal (up to the highest state or federal court), in practice puni-wrap policies are almost never triggered.

Defending Punitive Damages

The plaintiffs' bar is adept in advocating for punitive damages. The most popular tactic is utilizing the Reptile Theory: by tapping into the ‘reptilian’ part of jurors' brains, the part that is biologically sensitive to danger, lawyers can elicit a reaction that a societal wrong must be corrected regardless of whether the plaintiff was injured. This approach encourages jurors to award damages to punish current defendants and deter other presumed “bad actors” who are not defendants in the case at issue. Plaintiff attorneys often suggest that without a proper verdict featuring an “appropriate” deterrent, an already existing danger may become worse.²

A recent Gallup poll found that Americans' faith in their institutions (including big business, large technology com-

panies, and banks) has fallen to new lows since the survey began in 1979.³ This distrust of corporations has made its way into the jury box and the courtroom. Research conducted by Magna Legal Services found that 76% of jurors believe that corporate executives lie and cover up.⁴

Covid lockdowns affected jurors in many states. Dealing with personal tragedy and financial challenges, many jurors have seen local businesses struggle but large corporations report record profits. Many jurors are more vulnerable (health and/or wealth wise) than they were pre-pandemic. All of this makes jurors more plaintiff friendly. The recent Magna polling indicated 71% of potential jurors surveyed do not

believe there should be a cap on jury awards, while 30% believe that it takes “billions” to send a message to corporations.

A recent study from Marathon Strategies highlights similar insights. The median ‘nuclear’ (over \$10 million) verdict against corporate defendants increased 55% in the decade from 2009-19. Pandemic shutdowns in 2020 paused the nuclear verdict trend, but the study concluded that once courts began to return to normal levels of activity, so too did the trend. In fact, the total cost of corporate nuclear verdicts almost quadrupled (from \$4.9 billion in 2020 to \$18.3 billion in 2022), the number of verdicts doubled, and the country’s median nuclear verdict against corporate

defendants increased from \$21.5 million in 2020 to \$41.1 million in 2022.⁵

Punitive damages are awarded after verdict while most (95%) of claims settle pre-verdict.⁶ Defendants are reluctant to litigate their wrong-doing and are mindful of the potential for a nuclear verdict. Plaintiffs are also incentivized to settle because, unlike compensatory damages, punitive damage awards are taxable. When claims that include punitive damages or bad faith (ECO) allegations settle, there is no allocation and one (tax free) compensatory amount is paid. These allegations are putting pressure on insurance companies to settle and to settle for larger amounts that may give rise to payments in excess of policy limits (XPL).

Punitive Damages – A Case Study⁷

Insured: Brinton Tower Realty

The insured, Brinton Tower Realty, owned an apartment complex that offered affordable housing to low income residents. Charles Hart, had been a resident of the complex since 2012 and lived alone. On July 6th 2017, Mr. Hart was discovered deceased in his unit. It was alleged that the air conditioning in his apartment was not functioning and contributed to his death. Mr. Hart’s family filed a wrongful death lawsuit against the insured.

The insured had problems with its air conditioning system and in May 2017 engaged a contractor to perform repairs on the overall systems. Some tenants had complained about their apartments being too warm, but the insured had no record of the deceased ever complaining. The insured had retained appellate

counsel prior to the start of the trial and they were confident the plaintiff’s counsel did not meet the requisite burden of proof under Georgia law. Since there were no witnesses and no autopsy, there was no evidence to support a conscious pain and suffering award. Without conscious pain and suffering, there can be no punitive damages award.

In the state of Georgia, there is a cap of \$250K on punitive damages unless there is evidence of willful intent to cause the harm. There was no evidence presented of a willful intent, yet the jury found willful intent which allowed them to negate the cap. Claimant’s counsel successfully focused the case on the maintenance of the building, rather than whether the insured caused the death of the claimant. \$50M in punitive damages was awarded by the jury.



Location: Georgia

Punitive Damages Allowed?: Yes

Punitive Damages Cap?: \$250,000
(uncapped if willful intent to cause the harm is proven)

Beneficiaries: 25% to injured party, 75% to the state

Award

\$35 million Wrongful Death
\$15 million Pain & Suffering
\$50 million Punitive Damages
\$25 million Attorney’s Fees
Total: \$125 million

Lesson

While Georgia caps punitive damages at \$250,000, a notable exception allows the recovery of additional punitive damages if there is evidence a defendant willfully intended to cause harm. Never underestimate the animosity of jurors towards a particular insured (the landlords) nor the impact of skilled advocacy to craft the damages discussion toward willful conduct to overcome punitive damages caps.

It's not all bad news!

Nuclear verdicts such as Brinton Tower Realty should concern every re/insurer, but the headlines focus on "breaking news" of an initial award, not on post-verdict mediations, post-verdict settlements and the appeal process; all of which can dramatically lower such awards. After the jurors leave the courtroom, the judicial process continues.

For example:

A \$5 billion punitive damages award in Texas could be capped at \$200,000 or 2x the economic damages awarded (plus non-economic damages up to \$750,000) on the basis that the Texas Penal Code has not been violated.⁸

Extra Contractual Obligations and Losses in Excess of Policy Limits

Extra Contractual Obligations (ECO) claims lie outside the coverage of the underlying insurance policy, while Excess of Policy Limits (XPL) would have been covered by the terms of the policy but exceed the limits.⁹ It is common practice for reinsurers to cover ECO and XPL claims, but not typically for 100% – some risk sharing is normally required of the cedent.

ECO losses are caused by insurer actions that adversely impact the insured while punitive damages are awarded due to egregious behavior by the insured. ECO awards are not related to the underlying claim but are a result of the bad faith handling of that claim by the insurer/cedent.¹⁰ Bad faith is the failure of an insurance carrier to fulfill the obligations of the insurance con-

tract to its policyholder in a fair and prudent way.

Examples of bad faith include:¹¹

- failure to properly defend the underlying action
- failure to properly investigate the underlying claim
- failure to affirm or deny coverage in a reasonable timeframe after completing an investigation
- failure to settle a claim promptly, fairly, and equitably once liability has become reasonably clear

ECO claims are rising due to the coordinated efforts by the plaintiffs' bar to "set up" the insurer with conditional time element policy limit demand letters.

XPL damages can arise for a variety of reasons. The most common cause is an insurer's failure to settle the underlying claim within the policy limits. XPL clauses provide reinsurance coverage for losses brought against the insured by a third party for acts that would be covered by the underlying policy but for the limits of the original policy.

Historically, the main cause of an XPL claim was an adverse verdict in excess of the available policy limits. In an adverse verdict situation, the XPL exposure is usually known and quantifiable (verdict – limits = XPL exposure). There are instances where unquantifiable damages are alleged in conjunction with the XPL exposure and, depending on the individual state, recoverable damages could include punitive damages, statutory damages, treble damages, and/or business harm to reputation. More recently, we are seeing an increase in compromise settlements beyond the original policy limit due to allegations

of bad faith or punitive damages without a verdict. These compromise settlements are paid as compensatory damages.

Market Impact of ECO/XPL

The plaintiff bar is using bad faith to put insurers in an untenable position.¹² The threat of bad faith litigation is real, as is the rise of nuclear verdicts, which cause insurers to worry about their public reputation/brand. Similar to punitive damages, plaintiff attorneys attempt to "set up" insurers to force them to choose between paying a larger amount to settle the underlying claim or rolling the dice on a bad faith trial. As a result, many insurers choose to settle, but the settlements are being done against the threat of bad faith litigation rather than the insurer's evaluation of the underlying case.¹³ This behavior may allow fraud to seep into the equation – by encouraging inflated claims with the hope of getting either a nuisance value settlement or other recoveries from bad faith¹⁴.

Bad faith allegations also may lead to:

- premature settlements (which should have been litigated) resulting in excessive claim payments;¹⁵
- increased loss adjustment expenses to defend the bad faith action and the underlying claim;¹⁶
- increased premiums (passed on to consumers) due to the increased payments noted above which results in some consumers choosing to forego purchasing insurance;¹⁷
- difficulty in charging an appropriate premium due to the inability to price the subjective potential liability resulting from ECO/XPL damages;¹⁸ and

- insurers choosing not to underwrite or insure policies in certain states due to the judicial climate.¹⁹

Having recognized this problem, Florida recently passed a property insurance reform bill making it harder for policyholders to pursue bad faith claims

under insurance policies.²⁰ Florida also passed a tort reform bill that modifies third-party bad faith law to the benefit of insurers: mere negligence is not sufficient to prove bad faith. The claimant, insured and any representatives have their own duty to act in good faith with regard to providing information about

the claim, demanding settlement, setting deadlines, and attempting to settle the claim.²¹ Other states continue to enact legislation and issue judicial opinions that expand insurers' potential exposure to bad faith claims.

Bad Faith – A Case Study²²

Bonnie Winslett struck a cyclist while driving the insured's car (with permission). The SUV owner's auto policy limit was \$30,000. The insurer was notified, accepted the driver was responsible and notified the driver they would handle the injury directly with the cyclist's attorney.

The claimant's attorney sent a letter to the insurer, demanding the insurer tender the \$30,000 policy limit, noting the claimant's medical expenses already exceeded \$10,000, and that additional treatment would be necessary. The insurer rejected the demand and counteroffered \$12,000. Despite several attempts by the insurer's claim professional to reach them, the claimant's attorney did not respond to the counteroffer. There is no indication that the driver was contacted by the claim professional.

The claimant filed suit directly against the driver in Georgia state court but did not inform the insurer. The driver also failed to inform the insurer and discarded the papers. The driver did not answer the complaint or appear in court.

Following a hearing, a default judgment was entered against the driver in the

amount of \$2.9 million. One week later, the claimant's counsel informed the insurer of the judgment. The insurer retained counsel on the driver's behalf. A motion to set aside the judgment was denied. The claimant pursued the judgment, the driver was forced to declare bankruptcy and a court-appointed bankruptcy trustee filed suit against the insurer in federal court in Georgia. The allegation was the insurer failed to settle the claim in bad faith, resulting in a judgment in excess of policy limits. The insurer argued the driver's failure to provide notice of the suit relieved it of any liability to pay the judgment. The insurer further argued that the default judgment was not the correct measure of damages because they did not have an opportunity to contest the damages in the underlying case.

Georgia's Supreme Court found the driver was not the named insured, did not have a copy of the policy, was unstable (no driver's license, apartment had no electricity or furniture) and was not told by the insurer to forward any lawsuits, contrary to the insurer's claim manual.

The court further found that the driver's failure to give the required notice of the suit did not prevent the driver from recovering against the insurer for failure to settle a covered claim.



Insured: Karen Griffis (car owner), Bonnie Winslett (car driver)

Claimant: Terry Guthrie (cyclist)

Insurer: GEICO

Location: Georgia

Award

The final judgment against GEICO, including interest, exceeded \$2.7M

Lesson

This decision is part of a trend that expands insurers' potential exposure to bad faith claims. The decision places a burden on insurers to evaluate their insureds to predict if they may breach the notice provisions of the insurance policy. The court believes an insurer should be able to foresee a potential breach and then monitor dockets to see if lawsuits are eventually filed. In this case the court was clearly sympathetic to the individual insured.

The court further used the default judgment as the appropriate measure of damages.

The jury found that the insurer was 70% liable for the default judgment and the driver was 30% liable.

Conclusion

Both the frequency and severity of punitive damage, ECO, and XPL awards have risen in recent years and all three are now routinely sought in civil litigations.²³ As a result, the sum of all nuclear verdicts (above \$10 million) has almost quadrupled between 2020 and 2022.

Of most concern is the unpredictability this brings for insurers and reinsurers. Regardless of whether a plaintiff ultimately prevails, the allegations are a challenge for insurers, and can ultimately drive up settlement values for case where such damages are sought. As stated by the American Tort Reform Association, “The difficulty of predicting whether punitive damages will be awarded by a jury in any particular case, and the marked trend toward astronomically large amounts when they are awarded, have seriously distorted settlement and litigation processes and have led to wildly inconsistent outcomes in similar cases.”²⁴ Many consider the Securitas “Champlain Towers” settlement in Florida to be one such settlement.

The main concern is not an upsurge in payments via a specific punitive wrap policy. Rather, it is the gradual costs creep from the increased threat of punitive damages, excess of policy limits and bad faith awards. This cost escalation is not as easy to identify as a specific punitive wrap payment and can be masked within standard inflationary increases.



Frank J. DeMento is an experienced insurance and reinsurance lawyer and prior insurance company executive. Currently, he is counsel in the Insurance Reinsurance Group in Crowell & Moring's New York office. DeMento's practice specializes in managing complex insurance and reinsurance disputes, arbitrations, litigations, and mediations involving a broad spectrum of issues. Prior to joining Crowell & Moring, DeMento was a Vice President and the head of run-off claims, the head of retroceded claims, and claims counsel for XL Reinsurance America, Inc. He also was a partner in the Insurance and Reinsurance Litigation Group at Mendes & Mount, LLP.

DeMento has been a member of ARIAS since 2003. He was also a member of the board of directors of ROM Reinsurance Management Co., Inc. for six years and served as its chairman. DeMento also served as a member of the board of directors of the Association of Insurance and Reinsurance Run-off Companies (AIRROC) for three years and served as co-chairman on its education committee. Additionally, DeMento holds the following industry designations: Associate in Reinsurance; Chartered Property Casualty Underwriter; and Certified Legacy Insurance Professional.

DeMento received his undergraduate degree from Washington and Lee University and his Juris Doctor degree from St. John's University School of Law.

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Obituary



ARIAS Certified Arbitrator Steve Gilford passes away

ARIAS Certified Arbitrator Steve Gilford passed away on Aug. 14, 2023. He was 70 years old.

Steve was a trial and appellate litigation attorney at Isham Lincoln & Beale, Mayer Brown and Proskauer. Steve then "retired" from private practice to continue domestic and international arbitration mediation and other forms of alternative dispute resolution. He was a JAMS neutral as well as an ARIAS member.

Steve was good-humored, charismatic, and passionate about learning. His sharp wit brought joy to those he met. Steve dedicated his life to improving the lives of many through his professional and volunteer efforts.

Our condolences to his wife, Anne, and his family.

Newly Certified Arbitrators



Timothy E. Curley

Timothy E. Curley is the senior reinsurance counsel at Allianz Reinsurance America, where he provides legal advice on a variety of ceded and assumed reinsurance issues, including arbitrated and litigated disputes, and commutations. Prior to joining Allianz in 2017, Curley represented cedents and reinsurers as a counsel in the Insurance/Reinsurance Group at Crowell & Moring, and as an associate at Chadbourne & Parke. Curley's legal career outside of reinsurance has included periods of government service at the Commercial Litigation Branch of the U.S. Department of Justice and the U.S. Navy Judge Advocate General's Corps.



Frank D. Papalia

Frank D. Papalia is the founder of FDP Advisory, LLC, where he provides arbitration, mediation and advisory services to the insurance and reinsurance industry utilizing decades of experience as a legal, claims, and general management executive in international insurance and reinsurance groups. Prior to founding FDP Advisory in 2022, Papalia was chief legal officer and head of claims at ProSight Global, Inc. He also previously served as executive vice president, general counsel and general secretary, and member of the management board for Pairs Re (formerly AXA RE); and as vice president and counsel for Equitable (then AXA Financial, Inc.). He received his JD from Fordham University School of Law and a BS in accounting from Manhattan College.



Ryan Russell

Ryan Russell is an assistant general counsel and a corporate officer of Allianz Reinsurance America, Inc. As Head of Reinsurance and Claims Litigation, Russell oversees a staff of lawyers handling reinsurance and claims disputes involving Fireman's Fund Insurance Company and other Allianz affiliates in the United States.

After graduating from the University of Michigan and the University of California College of the Law San Francisco, Russell practiced law at insurance defense firms in San Francisco before moving in-house. At Allianz, Russell has been working in the reinsurance field for over 15 years, handling both ceded and assumed reinsurance legal matters. He has served as either corporate representative or counsel in dozens of matters that went to trial or arbitration.

When not working, Russell enjoys spending time with his family, traveling, tennis, golf, and carving carousel figures.



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300 First Stamford Place, 7th Floor
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203-977-6074
awakin@odysseyre.com

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pagentile@optonline.net

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646-877-1063

Stacey Schwartz

Swiss Re
175 King Street
Armonk, NY 10504
914-828-8193
stacey_schwartz@swissre.com

Steve Schwartz

Chaffetz Lindsey LLP
1700 Broadway, 33rd Floor
New York, NY 10019
212-257-6940
s.schwartz@chaffetzlindsey.com

Seema Misra

Arch Insurance Group, Inc.
Harborside 3
210 Hudson Street, Suite 300
Jersey City, NJ 07311
212-458-6350
smisra@archinsurance.com

Jonathan Rosen

*Arbitration, Mediation and Expert
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646-330-5128
jonrosen55@aol.com

Joy Langford

Partner Reinsurance Company of the U.S.
200 First Stamford Place
Ste 400
Stamford, CT 06902
202-701-9519
joy.langford@partnerre.com

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(516) 650-1827
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ARIAS-U.S.

222 S. Riverside Plaza, Suite 1870
Chicago, IL 60606
info@arias-us.org
www.arias-us.org

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AIDA Reinsurance & Insurance Arbitration Society

222 S. Riverside Plaza, Suite 1870
Chicago, IL 60606
Email: info@arias-us.org