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London and Bermuda Insurance Arbitrations: A **Roadmap** for Policyholders

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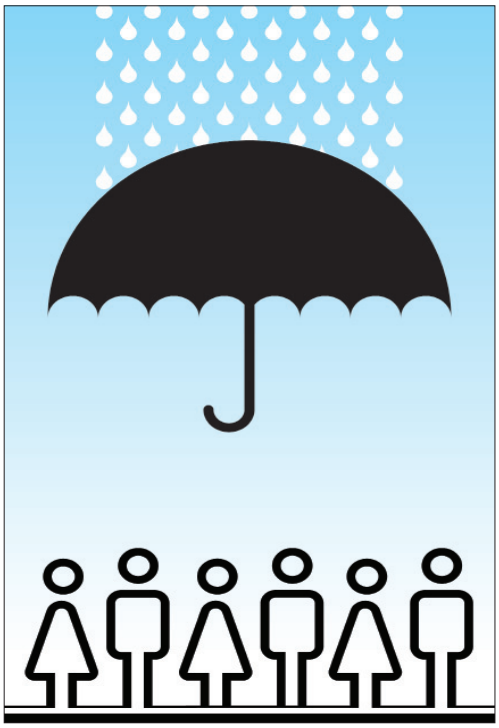
If your company requires large limits of property and liability insurance, it will probably have to shop in the London or Bermuda markets. More often than not, policies purchased in those markets contain clauses mandating that all disputes be resolved under arbitration rules and acts of their own jurisdictions—along with substantive choice-of-law and policy interpretation provisions that are unfavorable to policyholders.

Arbitration clauses in insurance policies issued by domestic insurance companies can be successfully challenged in some cases. Though the Federal Arbitration Act of 1925 (9 U.S.C. §1) creates a presumption in favor of enforcing arbitration agreements in other contexts, the McCarran-Ferguson Act vests the states with the power to regulate the business of insurance. Currently, approximately 26 states have laws that expressly limit or wholly restrict submitting claims arising out of insurance disputes to binding arbitration. Many courts have found that a state's insurance code can invalidate a policy's arbitration clause where to impose arbitration would directly or indirectly impair a state law regulating insurance.[1]

London Arbitration Clauses Are Generally Enforceable. The picture is quite different with respect to insurance policies sold by insurance companies from the overseas market. In recent years, a line of cases has developed in English jurisprudence that would suggest that policyholders facing arbitration clauses providing for London arbitration could be exposed to litigation in the United Kingdom to enjoin coverage litigation in a policyholder's home country or the country where the risk is located. In addition, where an arbitration clause in a policy provides for arbitration in London, questions as to the validity of an arbitration clause, or the enforceability of an award, will likely be decided under English law.

In *XL Insurance v. Owens Corning*,[2] the insurance policy at issue, as is common in many London-arbitration clauses,[3] identified New York state law as the law governing the substantive contract and incorporated the Federal Arbitration Act by reference, but provided for London arbitration under the provisions of the (English) Arbitration Act.



The policyholder sought a declaratory judgment in Delaware that, under the insurance it purchased, the policyholder was entitled to indemnification for certain Y2K costs. The insurance company sought an anti-suit injunction in London to enjoin the policyholder from pursuing the Delaware action. The policyholder, in turn, opposed the injunction on the grounds that the arbitration agreement was invalid under New York law. The Queen's Bench granted the injunction

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and held that by selecting London as the seat of arbitration, and in referencing the Arbitration Act, the parties had chosen English law to govern matters failing within the scope of the Act, including the validity of the arbitration agreement.

Notably, the *Owens Corning* court rejected the policyholder's argument that a Delaware court would be forced under the Federal Arbitration Act to apply New York law and thus subject XL to jurisdiction. The court opined:

> The grant of an anti-suit injunction involves by definition a degree of interference with foreign court procedures, because that is its object. But if the English court is satisfied that litigation in another country would be a breach of contract to arbitrate the dispute in London, the grant of an injunction involves no disrespect or unfriendliness towards the foreign court, but merely an insistence on parties respecting their own contractual obligations.

In *C v. D*,[4] the policy's arbitration clause proved itself a double-edged sword. The policy was governed by New York law but contained an arbitration provision that provided for London arbitration "under the provisions of the Arbitration Act of 1950 as amended." The policyholder initiated arbitration in London and prevailed in arbitration. The insurance company then asked the tribunal to re-consider the award on the grounds that the rationale supporting the award constituted a manifest disregard of New York law. The insurance company also indicated that it would seek to vacate the award on the grounds of manifest disregard of the law in the United States. The policyholder then sought relief in the English courts by way of an injunction that would enjoin the insurance company from initiating a challenge to the award in New York or otherwise relying on New York law to oppose enforcement of the award. The English court granted the injunction and held that the choice of London as the seat of arbitration "necessarily imports that…challenges to any award are governed by the relevant sections of the [Arbitration Act]" and thus the only permissible challenges are those provided for by the Arbitration Act.[5] On appeal, the Court of Appeal affirmed the decision of the trial court and held that "the choice of the seat of arbitration was also a choice of forum for remedies to challenge any award."[6]

Many courts have found that a state's insurance code can **invalidate a policy's arbitration clause** where to impose arbitration would directly or indirectly impair a state law regulating insurance.

Ironically, *C v. D* highlights the fact that while the field is tilted toward insurance companies in overseas arbitration, policyholders who are properly prepared can get a fair hearing. Policyholders should not capitulate to unreasonable settlement demands simply because they fear that they will be at a disadvantage in a foreign arbitration. They do, however, need a good roadmap to navigate their way through the various minefields presented by such arbitrations, which can differ dramatically from arbitrations in the United States.

Arbitration and Choice-of-Laws Clauses: Dealer's Rules. Many excess liability insurance policies seek to give insurance companies an advantage in the resolution of any dispute by including provisions requiring the arbitration of disputes in London and the application of New York law. The choice of venue allows London-based underwriters to arbitrate on their home turf and provides a forum in which certain Bermuda-based insurance companies can insulate themselves from the jurisdiction of the U.S. Courts. However, applying U.K. law to coverage for risks located in the United States might not survive challenge in the courts of either country, so the law of an American jurisdiction was needed. New York law is favorable to insurance companies in some respects when compared to that of most other states. Indeed, New York law can be quite draconian towards policyholders—and insurance companies strengthen their hands even further by inserting language into the choice of law provision that removes any conceivable legal presumption in favor of coverage. Moreover, this provision prohibits the introduction of parole or other extrinsic evidence to aid in the interpretation of the policy.

Clearly, the combination of a U.K. forum, New York law and an extra provision that changes New York law is intended to give the insurance company a significant advantage when a dispute arises. That advantage need not be determinative of the outcome, but it certainly could be detrimental if the policyholder is not prepared for the rarified world of the London arbitration.

Two Peoples Separated by a Common Language. The most common, and potentially disastrous, mistake made by American policyholders is assuming that they know how to proceed because they have been in arbitrations at home. Do not go into a London arbitration thinking it will be just like arbitrating in the United States. From the selection of arbitrators to the drafting of briefs and the presentation at the hearing, London arbitrations are conducted in their own unique way under the English Arbitration Act.

The arbitration panels, which usually consist of three members, will likely include at least two Queen's Counsel (QC), the highest level of barrister, i.e., litigator. As a result, the arbitration will probably follow a standard protocol that incorporates a particular set of English practices, rather than the more com-

mon approach followed in arbitrations elsewhere of structuring the proceeding at the initial stage with the participation of the parties. All three arbitrators must serve as neutrals. Each party appoints one member of the panel, and those appointees select the chairperson. The insurance company will probably select a Q.C. as its party-appointed arbitrator. The policyholder need not select a Q.C., and should in fact base the decision whether to choose a Q.C., an ordinary barrister or an arbitrator with different qualifications, upon the circumstances of the particular case. Indeed, the policyholder may be well served by selecting an arbitrator from the United States if the law of New York or another U.S. jurisdiction is to be applied. If a U.S. arbitrator has considerable stature, such as that of a retired appellate court judge from a well-regarded court, he or she ought to be viewed as an expert on U.S. law, and should therefore be able to speak with authority on legal issues during the hearing and in panel deliberations. The selection of the panel may be the most important part of the arbitration, and it should be done with the assistance of experienced U.S. and U.K. counsel.

Typically, there is little or no discovery or live testimony in a London arbitration. Written submissions are thus the principal means of presenting evidence to the panel. The briefs are not drastically different from those presented in U.S. arbitrations, but a higher level of civility is expected, and care must be taken not to invade the province of the panel by arguing too directly for the ultimate conclusions a party wants adopted. For many U.S. disputants, this is an alien concept that requires some adjustment.

With a few idiosyncrasies, hearings are conducted much like those in U.S. arbitrations. Perhaps most unusual from a U.S. perspective is the practice of counsel and panel members having the entire evidentiary record and all legal authorities in front of them in binders (called bundles), and extensively reading aloud from cases, as well as insurance policies and other evidence. Counsel should be prepared to give a very thorough discussion of the cases, and to read into the record every passage from a decision that is relied upon.

British or American Counsel? Or Both? There is a difference of opinion among policyholder counsel on the issue of whether the client should be represented at the hearing by U.S. or U.K. counsel. Certainly both have a role to play in the preparation of the case. If U.S. law is to be applied, a strong argument can be made for having a U.S. policyholder-appointed arbitrator, and if so, having U.S. counsel present the party's case at the hearing. On the other hand, if the panel consists of three individuals with backgrounds in British law, the policyholder usually should be represented at the hearing by English counsel.

Regardless of who makes the oral argument before the tribunal, the policyholder will likely want U.S. counsel to do as much of the preparation work as possible, both because U.S. law will be applied and because, believe it or not, a New York lawyer charges hundreds of dollars per hour less than his or her English counterpart!

English Rule for Payment of Attorneys Fees. Although a panel sitting for a London Arbitration may apply New York law, it will also follow the English procedure of requiring the losing side to pay the opponent's attorney fees and costs, and all of the arbitrators' fees and costs. This can create a powerful incentive for both sides to settle, provided the claims are not enormous. Often, though, the claims are so large that the prospect of paying another million dollars or so in costs is not significant. Policyholders must be careful not to assert makeweight claims or counterclaims, because even if they prevail on the key claims, if they lose on others, they might be required to pay some of the insurance company's attorney fees and costs.

To London, To London. Companies frequently include arbitration provisions in their commercial contracts, but often have a strong negative reaction when a coverage dispute arises and they are required to arbitrate. This is due in large part to the fact that the arbitration clauses in insurance policies typically contain unfavorable choice-of-laws provisions. It is certainly worth the effort to try to remove such provisions from policies, but since market for excess liability insurance has surprisingly few participants that may prove impossible except in the softest of insurance markets. However, being required to arbitrate a coverage dispute in London, even with a pro-insurance company choice-of-law provision, is no reason to settle cheaply based upon the assumption that the policyholder will not be treated fairly. The caliber of arbitrator found on the panels is typically quite high and their decisions are generally well-reasoned. While the results of the arbitrations are confidential, the policyholder bar does not perceive a trend favoring insurance companies. Moreover, it should not be assumed that a London arbitration panel will at best "split the baby." Often, London arbitrations turn primarily upon issues of contract interpretation and result in awards that are entirely in favor of one side or the other. Therefore, policyholders should evaluate each claim on its merits and pursue a recovery without feeling that it is at a disadvantage. Bottoms up!

1. Robert Horkovich and Alexander Hardiman, "Challenging Unfavorable Arbitration Clauses," Risk Management Online, Feb. 5, 2013, at http://www.rmmagazine.com/2013/02/05/challenging-arbitration-clauses/.

2. *XL Ins. v. Owens Corning (XL)*, [2000] 2 Lloyd's Rep. 500 (QBD (Comm.)).

3. See Richard Jacobs et al., Liability Insurance in International Arbitration: The Bermuda Form, 1.25-1.26 (Hart Publishing 2004).

4. *C v. D*, [2007] 2 Lloyd's Rep. 367 (QBD (Comm.)).

5. Id. at para. 27.

6. *C v. D*, [2008] 1 Lloyd's Rep. 239 (Ct. App. Civil Div.).