Marine Insurance – Watch Out for Hidden London Arbitration Provisions

R. Mark Keenan is a senior shareholder in the New York office of Anderson, Kill & Olick, P.C. and heads Anderson Kill's Marine Insurance Group. Greg Hansen is an associate in the Marine Insurance Group in Anderson Kill's New York office. If you have any questions, please contact Mr. Keenan at (212) 278-1888 or mkeenan@andersonkill.com or Mr. Hansen at (212) 278-1173 or ghansen@andersonkill.com

If you are buying a marine insurance policy, be warned – you may find yourself bound to London arbitration. London arbitration provisions are very common in the marine industry. See e.g. In re Standard Tallow Corp. v. Kil-Management A/S, 901 F. Supp. 147 (S.D.N.Y. 1995).

Arbitration is based upon the concept of fairness. Fundamentally, there must be an agreement to arbitrate between the parties – a meeting of the minds on the issue of arbitration. But, this does not always occur.

Oftentimes, insurance companies attempt to foist an arbitration agreement upon their policyholders, which requires the policyholder to forfeit their right to trial (and the concomitant benefits thereof) and arbitrate their claims (often in a jurisdiction in which the policyholder does not want to be). This is particularly true with marine insurance policies – which often contain arbitration provisions requiring policyholders to submit to arbitration in London, England – a notoriously pro-insurance company jurisdiction.

Policyholders are left in the dark about the arbitration provisions through a number of methods by the insurance company. For example, instead of providing the full insurance policy, marine insurance companies may send certificates of insurance or certificates of entry, purportedly providing "evidence" of insurance coverage, which incorporate arbitration provisions, but don't actually refer to the arbitration provision. It would be exceedingly easy for the insurance company to state "this insurance is subject to arbitration in London, England," but, in our experience, insurance companies to not do so. Why? Because they know that many policyholders would never agree to such a provision. So, based upon the documents provided to policyholders, the policyholder would have no way of knowing that they are submitting to London arbitration.

This certainly goes against the basis of arbitration – which contemplates and requires an agreement to arbitrate between the parties. See Sen Mar Inc. v. Tiger Petroleum Corp., 774 F. Supp. 879 (S.D.N.Y. 1991). But, Courts have crowded dockets and will take almost any opportunity to ease their caseloads. Thus, when a court sees the word "arbitration" it often jumps at the chance to have someone else decide the dispute. So, A policyholder may quickly find himself involved in arbitration, completely against their will and desire, and, with marine insurance policies, that arbitration may take place in a far away location – London.

Besides the inconvenience of being required to take part in London arbitration, and the increased cost of hiring English counsel, being forced into arbitration can have serious adverse effects on policyholders. In order to emphasize the importance of ensuring that a policyholder does not inadvertently enter into an arbitration "agreement," below are some examples of the factors in English arbitration which may impact policyholders:

First, English arbitration has very limited discovery. Indeed, while in the United States, pre-trial depositions are considered the most common and effective device to obtain and flesh out relevant evidence. Under U.K. law, however, depositions are rarely granted. Moreover, in English arbitration there are no mechanisms to obtain discovery from a third-party who is not a U.K. citizen, Commerce Ins. Co. v. Lloyd's Underwriters, 1 W.L.R. 1323 (2002), or to obtain deposition discovery of material witnesses prior to an arbitration hearing. South Carolina Co. v. Assurante N.V., 1 A.C. at 35 (H.L.(Eng.) 1987).

This is particularly problematic for United States policyholders. Usually, a United States policyholder will have entered into his policy through a broker in the United States, but that broker will be beyond the evidentiary reach of the arbitration panel. Thus, unless the broker is cooperating with the policyholder (which experience tells us is rare, since when there is a dispute concerning insurance the broker is usually at least partially responsible for the dispute), the policyholder will be arbitrating without substantial evidence.

Second, English arbitration rules typically provide that the losing party must pay all the successful party's fees and expenses – including legal fees. See e.g. Azov v. Baltic Shipping Co. [1999] 2 Lloyd's Law Reports 39. The responsibility of payment of the opponents fees can attach at each stage of the arbitration. Thus, an unsuccessful policyholder may be required to make payments on a rolling basis. This has the direct effect of preventing policyholders, who usually have less financial resources than insurance companies, from pursuing extended or otherwise complex arbitrations.

Further, insurance companies can use this rule to coerce policyholders into simply dropping their claims, by threatening to extend the arbitration. In this connection, the insurance company may intentionally (and artificially) lengthen the proceedings, knowing that their attorneys and the arbitration panel are paid on an hourly basis. Thus, a policyholder can find himself not only losing his dispute (and therefore his insurance coverage), but also responsible to pay the insurance company for the pleasure of taking part in an arbitration that the policyholder never wanted to be in in the first place – which can cost the policyholder an arm and a leg. And, If the policyholder opts not to take part in the arbitration, the insurance company may simply proceed in the policyholder's absence and require the policyholder (who, in their absence, is almost certainly going to lose since they aren't there) to pay their expenses.

Third, England is a notoriously pro-insurance company jurisdiction. Thus, English law can work against policyholders – especially as compared to United States law. For example, England maintains the idea of caveat emptor, or buyer beware, even with insurance policies. In this regard, English laws often view insurance companies and policyholders on equal footing, (see Banque Keyser Ullmann S.A. v. Skandia Ins. Co. Ltd. [1987] 1 Lloyd's Reports 69 (recognizing that the requirement of utmost good faith by both the insurance company and the policyholder does not retract from the principle of caveat emptor)) whereas American law recognizes that policyholders have very little power in the relationship. See Eagle Star Ins. Co., Ltd. v. International Proteins Corp., 45 A.D.2d 637, 639, 360 N.Y.S.2d 645, 650 (1st Dep't 1974). Therefore, American law utilizes the doctrine of contra proferentem, resulting in insurance policies, in the event of ambiguities, being read in favor of the policyholder and against the insurance company. See, e.g., Katz v. Am. Mayflower Life Ins. Co. of N.Y. 14 A.D.3d 195, 205, 788 N.Y.S.2d 15, 22 (1st Dep't 2004).

Another distinction is that under English law, all insurance provisions can be incorporated by (a vague) reference to voluminous a document appearing in a simple a one page document, such as a cover note, whereas in the United States insurance companies must provide the full policy. See Jet Setting Serv. Corp. v. Toomey, 91 A.D.2d 431, 459 N.Y.S.2d 751 (1st Dep't 1983). That is the basis for American courts recognizing that insurance contracts are generally contracts of adhesion. England does not share that view.

Moreover, arbitrators who hear these types of disputes are chosen by the parties and hear these disputes continuously (for example, the insurance company will choose one arbitrator, the policyholder will choose one and then the arbitrators will select a third), and insurance companies actively limit the individuals that can serve as arbitrators. Obviously, arbitrators are paid for their services and have a direct interest in being selected often. Since, insurance companies have far more arbitrations, arbitrators are chosen more often if they are pro-insurance company. (which, as discussed above, they tend to be anyway). Further, although the policyholder is able to select a member of the panel, the insurance companies tend to chose more influential members – who often "take over" the proceedings. So, in a recent arbitration handled by this firm, the "lead" arbitrator was appointed by the insurance company and the other members of the panel simply deferred to his decisions on every major point.

Fourth, arbitrators are not bound by the same strict rules of evidence, precedent and procedure as courts. While this may be designed to allow for more informal dispute resolution, it can often be injurious to the less powerful party to the arbitration – i.e. the policyholder.

Of course, arbitration is not completely without benefit. For example, arbitration will almost certainly lead to a much quicker result. This added speed in reaching a resolution, and the other benefits of arbitration (e.g. its more informal, there tends to be more negotiation, there are less "all or nothing" results) may cause a policyholder to desire arbitration. But, A policyholder must weigh these benefits against the drawbacks discussed above.

We are not suggesting that a policyholder would never want to enter into arbitration, even London arbitration, but policyholders should make that decision consciously, not have that decision it made for them. Thus, policyholders must be extremely careful and diligent in entering into insurance agreements.

Finally, policyholders must make sure that they have every relevant policy document before entering into the insurance agreement – because failure to know about an arbitration provision, even when it has been fraudulently withheld, may not be a defense against arbitration. ■