■ INSURANCE

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Arbitration Deadlines Have Teeth

by Brett H. Ludwig

Insurers often think of arbitration proceedings as less formal than courtroom litigation. In its recent decision in *Certain Underwriters at Lloyd's v. Argonaut Ins. Co.,*[1] the 7th U.S. Circuit Court of Appeals has made clear that, at least with respect to contractual arbitrator appointment deadlines, a party who presumes that arbitration proceedings will allow it freedom from strict enforcement of contractual terms may be in for a rude awakening.

The *Argonaut* case involved a reinsurance dispute over an asbestos claim. Argonaut had settled with one of its insureds and sought reimbursement from a Lloyd's syndicate under several reinsurance treaties. When the syndicate asked for more information rather than offering payment, Argonaut responded with an arbitration demand.

The timing of the arbitration demand and subsequent correspondence became critical. The treaties required the parties to name arbitrators within 30 days of being demanded to do so. Argonaut's August 4, 2004 arbitration demand asked the Lloyd's syndicate to name an arbitrator within 30 days. Perhaps seeking the tactical advantage of not having to name its arbitrator first, Argonaut's demand was silent as to its own arbitrator. Consequently, two days after getting Argonaut's demand, the syndicate sent notice asking Argonaut to name its arbitrator within 30 days of that letter.

On Friday, September 3, 2004, exactly 30 days after Argonaut sent its initial demand, the Lloyd's syndicate named its arbitrator. Argonaut's 30-day period for naming its arbitrator was to expire two days later on September 5, 2004, which turned out to be a Sunday. When that day passed without any arbitrator appointment from Argonaut, the syndicate responded on the following Monday (the Labor Day holiday in the United States, but not in the United Kingdom) by informing Argonaut that it was in default. Consistent with treaty terms, the syndicate then purported to name Argonaut's party-arbitrator for it.

When Argonaut finally got back into the office after the long weekend, it first responded (incorrectly) that it had appointed someone the prior week. After realizing this was not true, Argonaut instead argued that because the 30-day deadline had expired on a non-business day, it was entitled to have until the next business day, Tuesday, September 7, 2004, to name an arbitrator.

The syndicate took Argonaut to federal court to enforce its right to appoint Argonaut's arbitrator. The district court agreed. On appeal, the Seventh Circuit affirmed. Concluding that federal common law governed the issue, the Court of Appeals ruled that the 30-day deadline should be strictly enforced with "no exceptions." The appellate court reasoned that Argonaut was simply bound "to comply with the deadline for which [it] bargained."

On one level, the *Argonaut* case is just another lesson on the importance of adherence to deadlines.

No lawyer or client ever wants to be on the side of arguing that he or she should be excused from failing to meet a deadline. Where there is a debate on when a deadline expires, it almost never makes sense to take a chance on blowing the time limit. But another important, and perhaps less obvious, lesson is that the mere existence of an arbitration clause should not cause an insurer to assume that a lack of formality will accompany resolution of your dispute. Argonaut appears to have learned that second lesson the hard way.

[1] No. 06-3395, 2007 WL 2433139 (7th Cir. Aug. 29, 2007).

For a Surprised Reinsurer, That First Step Can Be a Big One

by James D. Ossyra

When a reinsurer discovers facts contrary to those it contemplated when making its reinsurance contract, the first step it makes to address the problem can be critical.

Suppose a ceding insurer has specifically represented that the policyholder would comply with recommendations made in an engineering survey. Also suppose the reinsurer later discovers that the policyholder had rejected most of these recommendations when the insurer made this representation and that the insurer knew it. This could be a good case for rescission of the reinsurance contract.[1] But suppose the reinsurer then cancels the contract. This action could kill any chance for rescission.[2]

How does a surprised reinsurer avoid a misstep that forfeits a chance to rescind an reinsurance contract?

Do the New Facts Justify Rescission?

To avoid a misstep, a reinsurer must be aware that the circumstances may justify rescission. The law governing rescission of a reinsurance contract is not simple (for example, the doctrine of *uberrimae fidei* imposes an obligation of utmost good faith that is specific to reinsurance), and the outcome of disputes over rescission are heavily fact dependent. Nevertheless, a short checklist of questions may be useful to identify situations where rescission may be appropriate. First, are the newly discovered facts contrary to an explicit understanding with the ceding insurer?[3] Second, even if they are not contrary to an explicit understanding, are the newly discovered facts contrary to an implicit understanding, *i.e.*, would a prudent underwriter have considered them important to the risk and relied upon them in accepting or pricing the business?[4] And third, do the newly discovered facts substantially change the risks assumed by the reinsurer?[5]

If answers to these questions are positive, a reinsurer would be well advised to proceed cautiously. Seemingly appropriate actions may diminish the reinsurer's rights irretrievably.

Losing the Right to Rescind

Rights to rescind have been lost, for example, where the reinsurer, shortly after learning of the facts, cancelled or terminated the contract rather than declaring the contract rescinded.

In *Wise, Ltd. v. Grupo National Provincial SA,*[6] the court rejected a reinsurer's claim of rescission because the reinsurer had issued a notice of cancellation after a large loss. The reinsurer accepted coverage for a shipment of cargo that was described, because of a mistranslation, as "clocks," when the cargo in fact was Rolex watches. Because the reinsurer issued a notice of cancellation after learning of the loss, the court held that the reinsurer affirmed the contract, instead of rescinding it, and accordingly denied the reinsurer's rescission claim.

Similarly, in *Iron Trades Mutual Insurance Co. Ltd. v. Companhia De Seguro Imperio,*[7] a retrocessionaire (Imperio) terminated its contract with a reinsurer (Iron Trades) after discovering that some of the business retroceded had originated with reinsurers other than Iron Trades and that changes in the business and parties involved had occurred over several renewal periods without any notice to Imperio. Because Imperio, after its investigation, terminated its contract with Iron Trades, the court concluded that Imperio had affirmed the contract and therefore denied Imperio's rescission claim.

Needless to say, issuing a certificate that confirms an earlier agreement to provide reinsurance may be an impediment to a subsequent rescission claim. In *Sumitomo Marine & Fire Ins. Co. v. Cologne Reinsurance Co. of America,*[8] defendant reinsurers sought to void their reinsurance on the ground that they had not been informed of an unusual risk that the ceding insurer had agreed to cover, a business interruption loss caused by incidental radioactive contamination of metal at a steel mill. After agreeing to provide reinsurance, the reinsurers learned of the full extent of the underlying coverage and of the loss itself. Nevertheless, they issued a formal reinsurance certificate without asserting any right to rescind. Because the reinsurers had not immediately asserted their rights, the court held that they had waived any rescission claim.

Conclusion

These fact patterns highlight the importance for a reinsurer to consult with experienced counsel promptly after discovering facts on which a rescission claim may be based, to ensure that the reinsurer's conduct thereafter is consistent with any right of rescission that it may have. When a potentially material misrepresentation or omission is discovered, careful attention must be paid as to the appropriate reaction and communication with the reinsured. The value of a reinsurer's possible right to rescind may be substantially reduced if the reinsurer's actions after discovery are inconsistent with that claimed right.

[1] *See Allendale Mut. Ins. Co. v. Excess Ins. Co.,* 992 F. Supp. 278, 282-85 (S.D.N.Y. 1998).
[2] *Wise Ltd. v. Grupo Nacional Provincial SA,* [2004] EWCA (Civ) 962 [1]-[45] (Eng.).
[3] *See, e.g., Allendale Mut. Ins., supra; Compagnie de Reassurance D'Ile de Fr. V. New England Reinsurance Corp.,* 57 F.3d 56 (1st Cir. 1995); Calvert Fire Ins. Co. v. Unigard Mutual Ins. Co., 526 F. Supp. 623 (D. Neb. 1980).

[4] *See, e.g., ERC Frankona Reinsurance v. Am. Nat'l Ins. Co.,* [2005] EWHC (Comm) 1381 [1]-[204], 2005 All E.R. 500 (reinsured's key officers were convicted of securities fraud); *Brotherton v. Aseguradora Colseguros SA,* [2003] EWCA (Civ) 905 [1]-[50], [2003] 2 All E.R. (Comm.) 298 (policy-holder's officers were the subject of media reports of corruption and embezzlement).

[5] *See, e.g., Christiana Gen. Ins. Co. v. Great Am. Ins. Co.,* 979 F.2d 268 (2d Cir. 1992) (reinsurer could not rescind where unexpected coverage did not change the reinsurer's assumed risks).

[6] *Wise Ltd. v. Grupo Nacional Provincial SA,* [2004] EWCA (Civ) 962 [1]-[45] (Eng.).

[7] *Iron Trades Mut. Ins. Co., Ltd. v. Companhia De Seguros Imperio,* [1990] Q.B. (Commercial Court).

[8] 75 N.Y. 2d 295, 552 N.E.2d 139 (1990).

Florida to Develop Rule Requiring Extensive Disclosure to Viators in Viatical Settlement Transactions

By Wes Strickland

On August 24, 2007, the Florida Office of Insurance Regulation (OIR) published a notice that it intends to develop a new rule that would require viatical settlement providers and brokers to make detailed and comprehensive disclosures to viators regarding the terms of the offer and the compensation to be paid to brokers in viatical and life settlement transactions. A viator is an owner of a life insurance policy who sells the policy to an investment company, known as a viatical or life settlement provider, for a purchase price that is greater than the cash surrender value of the policy. A broker acts as the agent of a viator in a viatical or life settlement transaction. Viatical and life settlements are regulated by OIR pursuant to Florida Statutes Part X, Chapter 626.

Under the preliminary text of the proposed rule, to be numbered 69O-204.101, Florida Administrative Code, a viatical settlement provider would be required to give a disclosure statement to a viator and obtain the viator's signature on the statement prior to the viator's execution of a viatical settlement contract. The disclosure statement would be required to include the following:

- The name of each viatical settlement broker who receives compensation and the amount of compensation received by that broker. As used in this rule, the term "compensation" would include anything of value paid or given to the viatical settlement broker in connection with the viatical settlement contract.
- A complete reconciliation of the gross offer or bid by the viatical settlement provider to the net amount of proceeds or value to be received by the viator. As used in this rule, the term "gross offer or bid" would mean the total amount or value offered by the viatical settlement provider for the purchase of one or more life insurance policies, inclusive of commissions, fees, or other expenditures related to the viatical settlement transaction.

A viatical settlement provider would have to give the viator an amended disclosure statement if anything changed regarding the broker compensation or gross offer or bid. The amended disclosure statement would have to identify clearly any information that changed from the preceding disclosure statement. The viator's signature also would be required for the amended disclosure statement.

In addition to requiring the viator's signature on the disclosure statement, the preliminary text of the proposed rule indicates that the viatical settlement provider also may be required to obtain the signature of any brokers who receive compensation in connection with the viatical settlement transaction.

Although viatical settlement brokers have been required since 1999 to disclose their compensation to viators pursuant to Florida Statutes Section 626.99181 OIR has not required a particular form to be provided for that disclosure, and the obligation is not placed directly on the viatical settlement provider to ensure that the disclosure has been made by the broker. The disclosure requirements of the proposed rule appear to be aimed at preventing certain practices that OIR has characterized as "fraudulent or dishonest." The preliminary text of the proposed rule contains requirements that are similar to the new disclosure requirements of the amendments to the Viatical Settlements Model Act adopted by the National Association of Insurance Commissioners in June 2007.

OIR scheduled a workshop on September 11, 2007 in Tallahassee, Florida to receive public comment regarding the development of proposed rule 69O-204.101. If you have any questions regarding this proposed rule development, please contact Wes Strickland at 850.513.3369 or nstrickland@foley.com.

Legal News Alert: Developing Case Law at the Intersection of Insurance Receivership Law and Bankruptcy Law

When disputes arise between an insolvent insurance company that has been placed under the supervision of a state receivership court and a company with debts that has sought protection under the supervision of a federal bankruptcy court, which court will decide disputes between the insurer and the debtor? When an insolvent insurer in a state receivership and its holding company in bankruptcy both have claims to the same property, again, which court will decide who owns the property?

Answers have begun to emerge from recent cases, and it has become clear that in-depth understanding and experience both in federal bankruptcy law and state insurance insolvency law is necessary to derive the answers. Where a debtor in bankruptcy has a claim against an insolvent insurer in receivership, for example, it may be necessary to invoke both the abstention provisions of federal bankruptcy law and state case law concerning the Uniform Insurers Liquidation Act to determine whether a bankruptcy court is required to defer, or may be persuaded to defer, to a state insurance receivership court for resolution of the issues.

While the courts have begun to address these issues, the case law is far from settled. To provide a thorough understanding of the case law as it has evolved to this point, Foley Partner Wm. Carlisle Herbert, a member of the firm's dedicated Insurance Industry Team, has authored, "When Jurisdictions Collide: Determining Judicial Roles When Bankruptcy Court and Insurance Receivership Court Responsibilities Overlap." The article is slated for publication in the Fall 2007 issue of the American Bar Association's *Tort Trial & Insurance Practice Law Journal* (Vol. 43, No. 1).

It is apparent from the current cases that courts are not being fully advised of all the potentially applicable authorities on this subject, possibly because lawyers with state insurance insolvency expertise and bankruptcy expertise have not worked in tandem when these issues have been presented. Foley has decades of experience both in state insurance receivership law and federal bankruptcy law, and the firm regularly establishes cross-disciplinary teams necessary to address issues that bridge differing fields of law.

ANNOUNCEMENTS

Successes

The article, "HIPPA Affects Transfer of Health Insurance and Managed Care Contracts," authored by Foley Partner **John N. Gavin** appeared in BNA's Health Law Reporter (Vol. 16, No. 23) and also in BNA's Health Plan & Provider Report (Vol. 13, No., 23).

Upcoming Events

Foley's Reinsurance Practice attorneys will host clients, colleagues and friends in New York on October 31, 2007 at "Foley's ARIAS Conference Kick-off Dinner."

Partner **Richard Bromley** will chair a panel on "State Tax Issues for Insurers," at the 32nd Annual Insurance Tax Conference in Chicago on November 1-2, 2007. Partner **Brian S. Kass** will speak on recent legislative developments impacting the reinsurance industry.

On November 14, 2007, Foley Partner **Richard Bromley** will be speaking and chairing a panel on the "Federal Perspective on Insurance Regulation." Of Counsel, **Philip G. Kiko** will also present on the panel.

On December 5-7, 2007, the 2007 Blue Cross Blue Shield National Tax Conference will be held on at the Westin La Cantera Resort in San Antonio, Texas. Foley attorneys are participating in the following panels: Partner **Richard Bromley** will discuss insurance tax reserves and Partner **Kevin G. Fitzgerald** will discuss state and local tax and a Blue Card Update.

Sunday evening, December 2, 2007 Foley's Insurance Industry Team will host friends and colleagues from the National Association of Insurance Commissioners' Winter Meeting in Houston, Texas at a networking cocktail reception. More details to follow in the coming months. Please save the date.

Recent Events

On September 17-18, 2007, Foley sponsored The Life Settlements Conference at in Orlando, Florida. Foley Senior Counsel from the Tallahassee office, **Wes Strickland,** also presented on a panel titled, "Fee Disclosure: Should there be Transparency on Compensation?"

Foley Partner **Richard Bromley** chaired a panel on "Federal Income Tax Issues," at the Casualty Actuarial Society Loss Reserving Seminar in San Diego, California on September 10, 2007.

Foley Partner **Thomas J. Maida** and Public Affairs Director **Leonard E. Schulte** presented on the topic of the politics of property insurance in Florida at Florida's Private Sector Summit held August 22-23, 2007, in Orlando, Florida.

On July 31, 2007, Foley Partner **Ethan D. Lenz** presented the Web conference, "What Every Lawyer (and Other Executives) Should Know About Directors and Officers Liability."

Are there particular reinsurance issues of concern to you? Foley & Lardner LLP is pleased to offer you a complimentary seminar on a reinsurance-related legal topic of interest to your organization. Foley has broad experience in reinsurance law and dispute resolution. Let us help you better understand the important issues you face. To schedule a seminar, please contact Foley Partner **James D. Ossyra** at 312-832-4565 or jossyra@foley.com. For more information about our reinsurance practice, visit Foley.com/reinsurance.

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