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A Recap: MReBA's First Annual Symposium



I am certain that those of you who, like me, "joined the revolution" and attended the October 1, 2009 Symposium - "A Fresh Perspective on Reinsurance Disputes and Arbitrations" - agree that MReBA's first annual symposium was an overwhelming success by any metric. While the concept of MReBA's hosting a day-long symposium in its inaugural year sounded ambitious, to say the least, the Symposium Committee and its Chair, [Jerry McElroy](#), should be commended for delivering an informative program filled with insights about emerging trends and developments in reinsurance disputes and for providing a forum in which panels of industry experts could exchange ideas and discuss issues facing both reinsurers and cedents alike.

The Symposium garnered nearly 100 attendees, with over half of those attending coming directly from the ranks of the insurance and reinsurance industry. There were also 19 panelists and the balance of the roster of attendees consisted of MReBA members and their guests. Many of those attending hailed from New England, but other participants traveled from places such as New Jersey, Virginia, Maryland, Georgia and Wisconsin. The Harvard Club provided an excellent setting both for the lively discourse that occurred during the Symposium and for the cocktails that followed and served as a festive finale to the day's events.



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MReBA Calendar

MReBA Meetings

November

Wednesday, November 18
12:30 pm

Focus: Discussion of *ReliaStar Life Insurance Company of New York v. EMC National Life Company*, 564 F.3d 81 (2d Cir. 2009)

Location: [Mintz Levin](#)

December

Wednesday, December 9
12:30 pm

Focus: TBD

Location: [Prince Lobel](#)

General Interest

[National Conference of Insurance Legislators Annual Conference](#)

November 18-22
New Orleans

[Insurance Coverage and Practice Seminar](#)

December 4-5
New York City

[NAIC Winter Meetings](#)

December 5-8
San Francisco

[Cat Modeling Conference 2010: Probabilities and Possibilities](#)

This edition of *MReBA Cover Notes*, the quarterly publication of the Massachusetts Reinsurance Bar Association, summarizes the presentations from the Symposium. For those of you who attended, this issue will help memorialize the event and supplement the excellent materials you received at the Symposium (which are now also available at www.mreba.org). For those of you who did not attend, this will provide you a thumbnail sketch of what you missed: we look forward to having you join the conversation next year.

Steven J. Torres

Mintz Levin
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Industry Spotlight: Nonnie S. Burnes

Massachusetts' Former Commissioner of Insurance Nonnie S. Burnes - On The Reinsurance Regulatory Modernization Act of 2009, Managed Competition, And The Power Of The Regulatory Process

By **Susan A. Hartnett**, Sugarman, Rogers, Barshak & Cohen, P.C.



MReBA was delighted to present Nonnie Burnes, until very recently Massachusetts' Commissioner of Insurance, as the Keynote Speaker for MReBA's First Annual Reinsurance Symposium. Appointed as Massachusetts' Commissioner of Insurance in 2007, Commissioner Burnes can lay claim to a number of notable achievements, not the least of which is her leadership role in the National Association of Insurance Commissioners (NAIC) as chair of its [Reinsurance \(E\) Task Force](#). That Task Force is responsible for the Reinsurance Regulatory Modernization Act of 2009 - proposed federal legislation that seeks to modernize reinsurance regulation by the states. Given the significance of these very new

legislative developments to the reinsurance industry and reinsurance bar, Commissioner's Burnes' Keynote discussion of NAIC's proposed legislation was both informative and timely.

This proposed legislation is based on a Framework adopted by the NAIC in December of 2008. As explained by Commissioner Burnes and previously reported in MReBA's [Summer 2009 issue](#), the proposed federal legislation seeks to revamp reinsurance regulation through a system that, among other things, creates a national plan and uniform standards for supervisors and reinsurers, permits single state regulation and supervision of domestic and foreign reinsurers, liberalizes collateral requirements for reinsurers with strong financial ratings and other indicia of financial strength, and simplifies the methods of dealing with foreign reinsurers and foreign jurisdictions. The NAIC's Reinsurance (E) Task Force adopted the proposed legislation on September 15, 2009 after considering various constitutional aspects raised during the drafting and comment process, including questions concerning the relationship between the proposed Reinsurance Supervision Review Board and the federal government, and whether it is appropriate for individual states to enter into information-sharing agreements with foreign jurisdictions. On September 24, 2009, the NAIC's Government Relations Leadership Council voted to submit the proposed bill to Congress. A strong champion for the proposed new regulatory regime, Commissioner Burnes is optimistic that the proposed bill will pass through Congress and believes that the proposed regulatory system will improve the ability of states to regulate reinsurers, and will provide participating states with economic benefits in the form of increased reinsurance capacity and, therefore, a stronger insurance industry.

The Reinsurance Regulatory Modernization Act of 2009 is not the only major regulatory challenge that Commissioner Burnes has tackled in the past few years. Her tenure as Massachusetts' Commissioner of Insurance was also notable for her introduction of managed competition to the auto insurance industry in Massachusetts, a departure from the prior state-set rating system, and something that many thought could not be done given the Commonwealth's long history of rate setting. Indeed, Massachusetts was the last state in the country to move to a competitive rating system for auto insurance. As a result of the changes in the auto insurance system, in the first year of managed competition nine new insurers entered the Massachusetts auto market, agents reported increasing the number of represented insurers, and consumers' average auto premiums dropped approximately 8%, saving collectively \$273 million. For the Division of Insurance Executive Summary [click here](#).

February 9-11
Orlando

[RIMS Annual Conference](#)

April 25-29
Boston

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These accomplishments in a relatively short period of time are all the more remarkable given that Commissioner Burnes' prior professional experience as a trial judge in the Massachusetts Superior Court and as a litigator in private practice at the Boston firm of Hill & Barlow did not focus on insurance specifically, or regulatory or administrative law more generally. Her effectiveness as Commissioner was aided by an ability to look at the big picture with a fresh perspective and by her belief that one must "think systemically" and look at all of the moving parts that make up an issue in order to identify and solve problems. This perspective is, perhaps, what most distinguishes her work as Commissioner from the case-by-case approach to problem-solving that characterizes the work of most litigators and judges.

Commissioner Burnes' appreciation for the regulatory process has led her to her next career - that of a scholar and educator. As of October 1, 2009, Former Commissioner Burnes is a Senior University Fellow at Northeastern University in Boston, where she is developing (and this Spring will be teaching) a graduate level course on regulatory process and reform. Her two-and-a-half years as Commissioner have clearly provided her with practical first-hand knowledge of the power and mechanics of regulation, and the growing need for those engaged in regulated industries and professions - that is to say, just about everyone - to better understand what regulation is and how it is a powerful and insufficiently understood tool for improving life in modern society.

As the former Commissioner notes, the job of Commissioner of Insurance is to ensure a healthy and robust market for insurers while, at the same time, to ensure that consumers of insurance products are being provided with appropriate services and products. While these are sometimes seen as competing concerns, and the debate over issues can be contentious at times, there has been praise from the industry and consumers alike for Nonnie Burnes's success during her tenure as Massachusetts' Commissioner of Insurance in striking a fair and effective balance between the industry's and consumers' needs and interests. Northeastern University is fortunate to have her join its ranks.

Susan A. Hartnett can be reached at hartnett@srbc.com.

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Recent Decision by Britain's House of Lords Fundamentally Changes the Interpretation and Application of Follow the Fortunes Clauses under U.K. Law

By [Rachel M. Davison](#), Morrison Mahoney LLP

At the First Annual Symposium of the Massachusetts Reinsurance Bar Association, John T. Harding, partner at Morrison Mahoney LLP, provided an analysis of [Lexington Insurance Company v. AGF Insurance Limited and Wasa International Insurance Company Limited](#), [2009] UKHL 40, which marks a dramatic shift in the interpretation and application of "follow the fortunes" and "follow the settlements" clauses in commercial reinsurance contracts placed in the London Market. Despite a final determination of liability by the Washington Supreme Court and a businesslike settlement made in good faith by Lexington, the House of Lords refused to bind the reinsurers to follow the settlement and pay their share of the reinsurance that they had agreed to assume.

Harding presented an overview of the historical treatment of "follow the fortunes" and "follow the settlements" clauses by various U.K. courts to provide the context for the surprising holding of *Lexington*. He laid out nearly a quarter century of significant precedent establishing a reinsurer's obligation to indemnify a ceding company for its good faith, business-like settlements if the settled claims fell within the risks insured by the policy and the reinsurance contract. Despite this long line of precedent, the House of Lords chose to treat the *Lexington* case as a decision about "conflicts of law" and, to the surprise of many, ruled that the reinsurer was not obligated to follow the honest and good faith settlement of a claim where liability had been adjudicated before the Washington Supreme Court.

The claimed loss arose from the alleged environmental contamination at 35 sites in the United States by Alcoa and its subsidiary. The Washington Supreme Court made an "all sums" allocation of the damages, essentially imposing joint and several liability on the insurers who issued applicable policies of insurance to Alcoa during the period of continuous contamination. Lexington was one of those insurers and had issued a policy, governed by Pennsylvania law, for a three-year period in the late 1970s.

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Panelists Examine Recent U.S. Case Law Defining The Boundaries of The Follow the Fortunes Doctrine

By [Christine T. Phan](#), Zelle Hofmann Voelbel & Mason LLP

Panelists:

[Jerry McElroy](#), Zelle Hofmann Voelbel & Mason LLP
Cynthia Koehler, Liberty Mutual

Because of its importance to cedents and reinsurers alike, no reinsurance symposium would be complete without an examination of the latest developments on the scope of the follow-the-fortunes doctrine under U.S. law. How the doctrine is being applied by our courts to post-settlement allocations was addressed by the morning's first Panelists, Jerry McElroy, a partner at Zelle Hofmann Voelbel & Mason LLP, and Cynthia Koehler, Vice President and Assistant General Counsel at Liberty Mutual, who added a practical perspective to McElroy's remarks based on her experience in representing Liberty Mutual in its ceded claims.

McElroy first provided a brief introduction to the follow the fortunes doctrine, a fundamental reinsurance doctrine that is frequently invoked by cedents in support of their post- settlement allocation of payments where disputes later arise with their reinsurers concerning the reinsurer's obligation to indemnify the cedent. That doctrine obligates a reinsurer to indemnify its reinsured for any reasonable payments the reinsured made to its insured in good faith within the underlying policy coverage. McElroy observed that while the doctrine's operation is defeated by proof that the reinsured's settlement payment was made in bad faith, was a product of fraud or collusion, or was beyond the bounds of the insured's underlying policy, the follow the fortunes doctrine, when applied, is favorable to the reinsured. Cynthia Koehler concurred with this characterization of the follow the fortunes doctrine, noting that even if not explicitly asserted in a reinsurance contract, panels often presume that the follow the fortunes doctrine applies and the reinsurer bears the burden of proving that it does not. She added that because of the cedent's and the reinsurer's mutual interests in settling a claim fairly and quickly, the operation of the follow the fortunes doctrine is, in her experience, rarely challenged on charges of bad faith, fraud, or collusion. Instead, when the application of follow the fortunes is challenged, it is typically the reasonableness of the cedent's investigation that is questioned. Koehler emphasized, however, that what constitutes a "reasonable" investigation, such as seeking the advice of outside counsel or hiring experts, depends on the particular facts of the loss.

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Mock Arbitration Panel & Decision

By [Alexander G. Henlin](#), Robins, Kaplan, Miller & Ciresi L.L.P.

Panelists:

[Natasha C. Lisman](#), Sugarman, Rogers, Barshak & Cohen, P.C.

[John N. Love](#), Robins, Kaplan, Miller & Ciresi L.L.P.

Andrew Maneval, Chesham Consulting LLC

"You're manipulating the settlement to maximize your reinsurance coverage."

"You're breaching your duty to follow the settlements."

And so it begins. Another reinsurance arbitration gets underway. Cedents and their reinsurers may hope that they never have to invoke their contracts' dispute-resolution clauses; but, when they must, the dynamics of the process are not all that different from a typical coverage dispute. John Love, Natasha Lisman, and Andrew Maneval demonstrated that fact at the MReBA symposium in a lively and well-executed presentation that simulated an American arbitration panel's deliberations.

The panel assumed familiarity with a commonplace set of facts. A ceding carrier with a 1960's-era primary liability policy was presented with a claim for environmental contamination at 22 of its insured's production facilities. Facing significant exposure, the carrier settled the claims against its insured for \$2.2 million. Its in-house attorney negotiated the settlement to cover 7 of the sites, with the remaining 15 thrown in as a gesture of goodwill by the underlying plaintiff's attorney. The most polluted site, accounting for over \$800,000 of the settlement, was covered by two policies issued by the cedent. The cedent allocated that entire amount to the first policy, which covered no other site.

The cedent had reinsured its primary policies on a facultative certificate, with the reinsurer bearing 50% of up to \$400,000 in excess of the first \$100,000 of loss. The certificate contained follow-the-settlements and honorable engagement clauses. The cedent made a demand for \$200,000 upon its reinsurer for the first policy, based on the \$800,000 allocation. The reinsurer denied the claim, arguing that the \$2.2 million should be evenly spread among all 22 sites, with the result that no site would exceed the \$100,000 reinsurance threshold.

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Panel Debates Problems with Reinsurance Arbitrations

By [Seth V. Jackson](#), Zelle Hofmann Voelbel & Mason LLP

Panelists:

[Andrew Ian Douglass](#), Morrison Mahoney LLP

[Thomas M. Elcock](#), Prince Lobel Glovsky & Tye LLP

Eric Herstine, Lexington Ins. Co. - Boston

Richard G. Waterman, Northwest Reinsurance, Inc.

During this lively panel, Andrew Douglass, Tom Elcock, Eric Herstine and Richard Waterman discussed and debated the problems that cedents and reinsurers face in reinsurance arbitrations as well as possible solutions. Ultimately, the panel seemed to agree that "if it ain't broke, don't fix it." Or as panel member, Richard Waterman stated: although the reinsurance arbitration process has numerous problems, the process is a good one that, at most, needs a few improvements.

Some panelists had greater concern than others over the effectiveness of arbitration. For example, it was noted that that some people consider the arbitration process to be broken because it is not being administered the way that it was initially intended - as a quick, simple, private and cost effective tool. Those holding this view feel that some participants drag out arbitrations to extend the time before it is necessary to make payments. One panelist countered that arbitration panels have a duty to manage arbitrations and narrow the scope of the issues to be arbitrated to ensure

that arbitration fulfills its goals. However, another panelist responded that many arbitrators do not agree that it is their duty to limit the arbitration, but instead prefer to allow the parties wide latitude to pursue the discovery and issues that they believe are important.

The panelists also emphasized the positive aspects of arbitration. For example, while conceding that there is a certain level of dissatisfaction with the current arbitration process, Waterman argued that overall, arbitration is a sensible and effective way to resolve reinsurance disputes. Rather than throwing the system out altogether, the industry should look for ways to improve it. Waterman noted, for example, that arbitration panels are preferable to courts because companies can control the composition of the panels-ensuring knowledgeable decisionmakers-and freeing them from the random selection of judges and juries in the court system. In a similar context, other panelists noted the value of confidentiality. For example, Douglass explained that while lawyers may want to win in the court of law, on the executive floor, it is also important that the company win in the court of public opinion. In this context, confidentiality provides an additional benefit of arbitration.

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Proposals To Increase Efficiency of the Reinsurance Dispute Resolution Process

By [Adam R. Doherty](#), Prince Lobel

Panelists:

Susan E. Grondine, Cavell USA

[Joseph S. Sano](#), Prince Lobel

[Paul White](#), Sugarman, Rogers, Barshak & Cohen, P.C.

[Robert A. Whitney](#), White & Williams

Panelists Susan E. Grondine (Cavell USA), Joseph S. Sano (Prince Lobel), Paul White (Sugarman, Rogers), and Robert A. Whitney (White & Williams) discussed different approaches cedents and reinsurers can take to reduce the cost and increase the efficiency of the reinsurance dispute resolution process. Joe Sano introduced the panel's presentation by outlining some of the obstacles to the efficient resolution of reinsurance disputes and some of the approaches that the panel would present for streamlining the dispute process. The panel participants then presented three vignettes based on a fact pattern involving a dispute (with a relatively modest amount at stake) that demanded careful attention to cost control by the parties.

The vignettes showcased three significant cost control points in the arbitration/litigation process-an initial call between client and counsel; a follow up call at which key strategy decisions are made; and a call between opposing counsel during which cost control and scheduling proposals are exchanged in advance of the organizational meeting or scheduling conference.

Introducing the first vignette-the initial telephone conference between a party to a reinsurance dispute and its outside counsel-Sano explained the importance of giving outside counsel the tools needed to plan and formulate a strategy for handling the reinsurance dispute, including communicating client guidelines regarding cost control. Sano's presentation included a review of topics that should be discussed during such a phone conference. Sue Grondine (as cedent's in-house counsel) and Rob Whitney (as outside counsel) then demonstrated these points during a simulated telephone conference. As part of their discussions, Grondine suggested the possibility of a "fixed fee" legal expense arrangement for the arbitration, while Whitney proposed the possible use of the ARIAS-US "single arbitrator program," a stream-lined process involving a single arbitrator designed for arbitrations with smaller contested values. As an additional cost-savings measure, Whitney and Grondine also discussed when consideration should be given to "phasing" the resolution of certain key issues, for example by using either a summary adjudication or a "mini-hearing" procedure, where a quick determination of a certain issue is likely to facilitate the resolution of the remaining issues between the parties.

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Emerging Insurance Risks And Arbitration Reinsurance Disputes Under Massachusetts Law

Peering Into the Crystal Ball

By [Alexander G. Henlin](#), Robins, Kaplan, Miller & Ciresi L.L.P.

Panelists:

[William N. Erickson](#), Robins, Kaplan, Miller & Ciresi L.L.P.

[Ana M. Francisco](#), Ropes & Gray

[Benjamin L. Hincks](#), Mintz Levin Cohn Ferris Glovsky & Popeo P.C.

Jonathan I. Mishara, FM Global

"Asking an insurance professional to identify future claim trends is a lot like asking a doctor if he has treated any interesting diseases recently," began FM Global's Vice President and Assistant General Counsel, Jon Mishara. "Both have great anecdotes, but not so many facts." For an industry that strives to evaluate and quantify risk, however, a little educated guessing at the end of the day about what the future might hold seems worthwhile, and so, the MReBA Symposium wrapped up with a panel that looked to the future. Mishara kicked off the discussion by talking about property insurance claims. He noted that the property industry is undergoing a sea change because of the environmental risks of climate change and the economic risks of globalization. Mishara led by explaining how Hurricane Katrina had increased awareness of climate change risks. Using the example of constructing his own company's new global headquarters to LEED standards-which are being mandated in some jurisdictions and adopted by many more insureds-Mishara demonstrated that climate change affects all industries. Property policies are now often being amended to include some coverage for rebuilding to LEED standards, but also creating new considerations in loss adjustment and ensuring that climate change will continue to impact the industry both as a risk and as a reason for increased construction costs.

Globalization also presents unique challenges. Consider, Mishara said, the example of an automobile manufacturer whose supply chain is suddenly disrupted by a fire at the sole supplier of its brake valves. Suddenly, all production stops because a single part is not available, and contingent business interruption claims result. Ceding carriers write contingent and dependent time element coverages for their policyholders, but substantial questions remain about how those losses can be investigated and adjusted in a global economy.

Mishara suggested that reinsurance questions may also arise as a result of globalization. What if the civil authority in another nation refuses to allow insurance adjusters to investigate a major loss at the site of a third-party supplier? If the ceding carrier cannot determine the cause of the loss at the third party supplier's site, what are its options? How will reinsurers respond? The only certainty is that reinsurers and ceding companies will need to work cooperatively in light of the realities of the new economy.

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