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"Arbitration and ADR in the Insurance Sector"

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**Arbitration in the insurance sector - a practitioner's perspective**.

I have been asked to give a view of the use of arbitrations in insurance cases from ground level, the practitioner's perspective. In doing so, I intend to deal with two points

- The prevalence of arbitration clauses in insurance and reinsurance contracts.
- The factors which commonly influence the choice between arbitration and court, particularly the commercial court, in individual cases.

A common conception of the role of arbitration in insurance has been elegantly articulated by Richard E. Stewart in an article charting the relationship of insurance and arbitration:

> *". . . the feeling of many today [is] that **insurance arbitrations** work best when the dispute is between two members of the same insurance-merchant class (that is, reinsurance arbitrations) rather than between parties of different classes (that is, primary disputes between insurers and lay people)."*[2]

**The contract stage**

The first question for today is – Does the market share the view the binary view that arbitration is good in reinsurance but not in direct insurance? Well, judging by the pattern of usage of arbitration clauses in policies of insurance and reinsurance, the answer is yes and no.

Reinsurance.

The reinsurance market certainly favours arbitration for both treaty and facultative placement disputes. This is epitomised by the widely used London Joint Excess Loss Committee wording EXEL 1.1.90. Clause 15 of which requires disputes to be placed, in the absence of agreement to the contrary, before a tribunal of three arbitrators all of whom are to have at least 10 years experience of insurance or reinsurance. That choice is supported by the Commercial Court to the extent that if there is any doubt as to the venue chosen by the parties, it will tend to come down in favour of arbitration. So in *Axa Re v Ace Global Markets Limited [2006] EWHC 216 (Comm)*, Mrs Justice

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[2] *"Arbitration and Insurance Without the Common Law"* by Richard E. Stewart, ARIAS-US Quarterly, Third Quarter 2004, Volume 11 Number 3

Gloster was faced with a reinsurance slip which incorporated EXEL 1.1.90 by reference and included an express choice of law and jurisdiction of apparently unlimited scope in favour of the English courts - "*This Contract shall be subject to English Law and Jurisdiction."* The apparent conflict was resolved by construing the slip as requiring all substantive disputes to be referred to arbitration and limiting the court's role to a supervisory one. It is worth noting that the jurisdiction clause was included in the main part of the slip and therefore in front of the parties at the time of placement of the cover. The EXEL wording was not. The standard arbitration clause nevertheless trumped the non-standard jurisdiction clause in the slip.

So, at least at the contracting stage, the reinsurance industry tends to follow Richard Stewart's view. That said, in my experience, reinsurance counterparties are often more open to changing the venue after a dispute has arisen, for reasons I will mention in moment.

Direct insurance.

In the direct market it is not so easy to generalise.

Yes, in marine insurance, in the open market hull underwriters prefer to have their disputes dealt with in court. The Institute Hull clauses contain no arbitration clause and the MAR form selects English law and jurisdiction. This may in part because the underwriters want to deploy the full majesty of the court system when dealing with insured owners whom they suspect of scuttling. Personally, I cannot remember having pursued any hull claim in arbitration rather than in court.

P & I Clubs have a slightly different approach and are an interesting case – a number of them have rules which allow the managers the option to have hull and liability claims resolved in court or arbitration as they see fit.

Property insurance too, fire claims and the like, are usually handled by the Courts.

There are pockets of the direct market where arbitration has been fully embraced, sometimes for very striking commercial reasons:

In the aviation insurance market the dominant form is AVN1C, which provides both hull and liability cover to aircraft operators. For many years, that has contained a clause requiring any dispute between the insured and insurers to be submitted to arbitration in London (Clause C5). That clause has operated very successfully for underwriters for a very simple reason. One of the special characteristics of the AVN policy is that is an express condition precedent to any liability on the part of the insurer that the insured shall have complied with "*all navigation and airworthiness orders issued by any competent authority affecting the safe operation of the aircraft*" (Clause B2). This is usually taken to compliance with the Air Navigation Order which in its current form (2009) which contains 270 separate articles. In particular, articles 137 and 138 prohibit any negligent conduct which may endanger any aircraft, any person in the aircraft or on the ground. However, negligence by an aircraft operator is one of the principle circumstances which is likely to give rise to the liability which the insurance is otherwise intended to cover. On its face, therefore AVN1C appears to grant underwriters an extremely wide defence to claims for indemnity against insured's liabilities to passengers and third parties. When, in the 1970s, similar provisions came before the courts in other jurisdictions the courts have tended to react by construing them very restrictively against the

insurer.[3] Because of the arbitration clause, the point has always been taken by insurers behind closed doors so no such body of precedent has built up here. Of course, in the modern day the highly reputable insurers with whom I deal are very reluctant to take the breach of condition precedent point except in flagrant cases but, even so, it is often influences settlement negotiations.

This is one example of where arbitration is chosen in insurance policies at the direct level of the tangible commercial impact of that choice.

Another is the Bermuda form, introduced in the mid -1980s by Ace and XL after the collapse of the excess casualty market in the US, from which large US corporations had previously purchased their catastrophe level liability insurance. One of the most striking features of the Bermuda form is that is applies New York law as the substantive law of the insurance but provides for arbitration in London (or sometimes Bermuda). And the arbitrators are typically English lawyers. The right of appeal, including on points of NY law is expressly excluded. Why this clashing combination? The reasons are intensely practical. The insurers were reeling from the decisions of US courts in policy interpretations in asbestosis cases which they thought were over-favourable to insureds, and above all were unpredictable/difficult to reserve for. It was thought that London arbitrators might take a more neutral and predictable approach. On the other hand, they recognised that it was likely to be unacceptable to their clients, in corporate America, to be required to submit to English law. Hence the compromise. The Court of Appeal in *C v D [2007] EWCA Civ 1282* recognised the balance between the two jurisdictions and upheld an anti-suit injunction preventing a challenge in the US courts to the manner in which the London arbitration had applied New York law.

That is at least a partial survey of the use of arbitration clauses by the insurance market at the contracting stage.

**Post-Dispute**

The second topic I wanted to touch on is the choice that is sometimes made after the dispute has arisen to change the form of dispute resolution and, in particular, the considerations inform that decision. In my experience, in the reinsurance market and among its lawyers, there is less of a prevailing preference for court or arbitration than in other areas say, charterparties or construction.

Each case is taken on its merits

1. No consolidation/confidentiality in arbitration. Sometimes the structure of a dispute is unsuitable for arbitration. For example,

    a. Alternative claims. Where a London reinsurer denies liability on the grounds of a non-disclosure in the course of the placement of the cover, the reinsured may well have alternative claims against the reinsurer and the broker (typically a London placing broker). The reinsured will normally want to pursue both claims in a single case and the reinsurer can sometimes be persuaded to join in those court

[3] See *Maclean v Maclean (1977) 15 SASR 306* in Australia and *Aviation Insurance Co of Africa v Burton Construction (Pty) 1976 (4) SA 769* in South Africa.

proceedings involving the broker. This avoids the ungainly pursuit of two sets of proceedings involving similar issues and the same evidence.

b. Need for precedent. Historically, there has a high degree of interrelationship between market participants, particularly through reinsurance and pooling. Sometimes there is a need for a public and binding decision on issues of common interest. A recent example is the *Equitas v R & Q [2010] 1 LR IR 600*. The London XL market was in effective "lockdown". 20 year old losses (including the capture of BA and KAC aircraft in the Gulf War and Exxon Valdiz) had been aggregated for the purpose of each participant in the reinsurance chain and the claims had circulated on that basis in 2003 and 2005 the Court of Appeal held that they had been aggregated wrongly over many years. By then it was impossible to unwind the claims on a contract by contract basis and a market-wide solution was needed. All the reinsurances were on the EXEL 1.1.90 and provided for arbitration, but self-evidently was not going to provide the answer. It ended up in the commercial court which provided what it is hoped was a practical answer, allowing the differential effect of the new approach to aggregation to be estimated in actuarial evidence.

c. Multiple claims of a similar nature. Reinsurance programmes are now complex. An insurance company may have scores of reinsurance contracts with the participants in its programmes. Where a large claim comes in, the reinsured faces the prospect of having to make multiple claims in separate arbitration references. That is potentially inconvenient from a reinsured's perspective, but it bothers them less than one might expect. As far as I can divine, this is more than compensated for by the benefits of confidentiality. If one of the reinsurers takes, for example, a non-disclosure point, it is thought to be easier to quarantine the problem. The protection of confidentiality makes it less likely that other reinsurers will jump on the bandwagon.

2. Cost and delay. Reinsurance Practice and the Law (para 43.16) paints a rather negative picture of reinsurance arbitrations:

> "As the conduct of reinsurance arbitrations has developed, there often is little difference in practice between the procedures adopted in arbitration and litigation proceedings. Consequently, arbitrations commonly take just as long as court actions. In many cases, however, arbitrations can take longer because strict timetables backed by sanctions are not set by the arbitrators."

I believe that this paints rather too negative a picture of arbitration. It may be a personal experience, but I find arbitrators reasonably demanding when it comes to setting timetables, although not quite able to meet the standards of the early arbitrators at medieval Fairs who reckoned to resolve disputes within "two tides", ie 24 hours.

There are some frustrations with the busy diaries of the main arbitrators when it comes to setting a date for the final hearing and, of course, the Comm Court is offering fairly short lead times. As of this morning you could get a 1 week trial in April and a 2 week trial in

October next year. But, I know my solicitors have found arbitrators very flexible, especially when it comes to interlocutory hearings – not unusual to get a call at midday with an invitation to join in a telephone conference at 5.30 or 9am next morning.

3. Expertise. Clients do value the expertise of arbitrators, especially the commercial perspective which they bring to the resolution of disputes. Some commentators suggest that the expertise of "market" arbitrators can obviate the need to call experts on issues such as materiality. This sounds correct in theory, but I have never seen it done. The reinsurance market is has spawned a large number of sub-specialisations and is using increasingly sophisticated underwriting methods, such as modelling and actuarial assistance. In my experience, it is difficult to match the precise nature of the dispute to the experience of the arbitrators, and arbitrators welcome accurately-targeted expert underwriting and actuarial evidence.

   I have not yet seen arbitrators following the suggestion of Jackson LJ of having the experts give evidence at the same time – "hot –tubbing". But someone must take the plunge soon!!!

4. Enforcement. Enforcement is, in many cases, very high up the list of factors when advising insurance clients on the differential advantages of arbitration over litigation. If you are reinsured by a company in say Dubai or even Afghanistan, for example, the New York Convention will provide a means of enforcement if you can arbitrate. In such a case, a English court judgment may be of little practical use. The reach of the Convention is a major factor in the continued use of arbitration in reinsurance.

There are of course other factors which bear on the choice between arbitration and court in insurance disputes but those are some of the main ones.

## Conclusion

Arbitration and litigation each have their particular advantages and disadvantages, in insurance and reinsurance. Particular sections of the market have their preferences, sometimes for special commercial reasons. It is fair to say that the differential has narrowed, particularly when it comes to comparing cost and speed.

As in other fields of commercial endeavour, it does pay to consider the relative merits at the stage of making the contract, if not before, rather than automatically incorporating an arbitration or a jurisdiction clause through force of habit.

EXEL 1.1.90 Arbitration Clause

“15 Arbitration15.1 The parties agree that prior recourse to courts of law any dispute between them concerning the provisions of this contract shall first be the subject of arbitration.

15.2 The following arbitration procedure shall be used in any dispute concerning this contract, and shall exist as a separate contract if there is a dispute over the validity or formulation of the contract.

15.3 Unless the parties agree upon a single arbitrator within thirty days of one receiving a written request from the other for arbitration, the claimant (the party requesting the arbitration) shall appoint his arbitrator and give written notice thereof to the respondent. Within thirty days of receiving such notice the respondent shall appoint his arbitrator and give written notice thereof to the claimant, failing which the claimant may apply to the appointor hereinafter named to nominate an arbitrator on behalf of the respondent.

15.4 Before the commencement of arbitration proceedings the two arbitrators shall appoint a third arbitrator who shall act as chairman of the tribunal. Should they fail to appoint such a third arbitrator within thirty days of the appointment of the respondent's arbitrator then either of them or either of the parties may apply to the appointor for the appointment of the third arbitrator. The arbitrators appointed by the parties in dispute shall decide the verdict: if they cannot agree, they shall seek the verdict of the chairman of the tribunal, which shall prevail.

15.5 Unless the parties otherwise agree the arbitration tribunal shall consist of persons with not less than ten years' experience of insurance or reinsurance.

15.6 The arbitration tribunal shall have power to fix all procedural rules for the holding of the arbitration including discretionary power to make orders as to any matters which it may consider proper in the circumstances of the case with regard to pleadings, discovery, inspection of the documents, examination of witnesses and any other matter whatsoever relating to the conduct of

the arbitration and may receive and act upon such evidence whether oral or written strictly admissible or not as it shall in its discretion think fit.