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EXPERT ANALYSIS

Bellefonte: The Tide Continues to Turn

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Insurance disputes often involve the issue of whether a particular claim is covered under a policy. These disputes sometimes deal with how much coverage is available. For example, there may be a disagreement as to whether the insurer is required to pay attorney fees in addition to the policy limits or within the policy limits.

There is a similar and often-litigated issue in reinsurance law. Specifically, reinsurance agreements contain "limits," typically referred to as "reinsurance accepted" amounts. Historically, insurance companies and their reinsurers generally understood that the reinsurance accepted amounts in their agreements applied to settlements of underlying claims and other "loss" payments and that reinsurers would reimburse attorney fees *in addition to* the reinsurance accepted amounts.

In other words, where insurance companies pay attorney fees in addition to limits, reinsurers are required to do so as well. This was the well-accepted industry custom and practice.

Then came a 1990 2nd U.S. Circuit Court of Appeals decision, referred to as *Bellefonte*. Under *Bellefonte* and cases ostensibly applying it, reinsurers started to argue that the reinsurance accepted amounts capped their total liability for settlements *and* attorney fees. Because reinsurance disputes involve significant attorney fees, court decisions approving that approach created serious gaps in available reinsurance.

However, the tide is turning. A series of recent rulings have properly focused on the specific terms of the reinsurance agreement and have found that reinsurance accepted amounts do not necessarily cap reinsurers' liability. As explained below, a recent Pennsylvania court decision after a bench trial — a first of its kind — further demonstrates the eroding legal support for the arguments the reinsurers have been relying on for more than two decades.

THE *BELLEFONTE* DECISION

The genesis of the reinsurance limits dispute is the *Bellefonte* ruling.[1]

In that case, the insurer requested that its reinsurers reimburse defense costs in addition to the reinsurance accepted amounts in the reinsurance agreements. Some of the reinsurers argued that the reinsurance accepted amounts capped their liability and that they were not required to pay attorney fees in addition to those amounts.

The 2nd Circuit ruled in the reinsurers' favor. The appeals court relied heavily on a provision in the reinsurance policies that made all of the reinsurance "subject to the ... amount of liability" set forth as the reinsurance accepted amounts in the agreements.

THE FALLOUT FROM *BELLEFONTE*

Bellefonte was not well-received in the industry. Commentators found the *Bellefonte* decision inconsistent with the custom and practice.[2] They "roundly criticized" the decision.[3]

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But the near-universal disapproval was of no moment for some reinsurers. Many began to rely on *Bellefonte* to attempt to cap their liability for settlements and defenses costs[4] — even if their contract language was materially different from the language at issue in *Bellefonte*.

Some courts agreed with those reinsurers, even going so far as to refer to a presumption that reinsurance accepted amounts limited liability for settlements and defense costs.[5]

The tension between the developing case law and the industry custom and practice is perhaps best illustrated by a dispute between Pacific Employers Insurance Co. and Global Reinsurance Corp. of America. In that case, PEIC was the insurance company and Global Re was the reinsurance company.

PEIC had issued an umbrella policy to Buffalo Forge. Global Re was responsible for three different reinsurance agreements covering that umbrella policy: two issued by Gerling Global Reinsurance Corp., U.S. Branch and one issued by Constitution Reinsurance Corp. The two Gerling Global reinsurance agreements were subject to arbitration, while the Constitution Re reinsurance agreement was not.

In the arbitration, which focused more on industry custom and practice than litigation, the panel found that Global Re was responsible for defense costs in addition to limits under the two Gerling Global agreements.[6] In the litigation, the court "agree[d] with and follow[ed] *Bellefonte*" and related cases and found that Global was not responsible for defense costs in addition to limits under the Constitution Re agreement.[7]

Despite this example of the different conclusions reached by arbitration panels and courts, the gap between how panels and courts view this issue is narrowing.

A RETURN TO FUNDAMENTALS

Recently, courts have begun to rebuff reinsurers' reliance on *Bellefonte* and similar decisions. These courts have returned to fundamental contract interpretation principles. They have refused to apply the presumption that reinsurers advocate for and have instead properly evaluated each contract based on its terms.

This trend began with the 2nd Circuit's most recent decision addressing this issue in a dispute between Utica Mutual Insurance Co. (the insurer) and Munich Reinsurance America (the reinsurer).[8]

The U.S. District Court for the Northern District of New York relied on *Bellefonte* and summarily disposed of the case. It did so without the benefit of a full record regarding the intent of the parties and evidence related to how Munich Re had handled similar prior claims. The trial court also applied a presumption that the reinsurance accepted amounts served as a total cap.

The 2nd Circuit reversed, making it clear that was the wrong approach. The court emphasized that *Bellefonte* turned on a specific provision making the reinsurance subject to the amount of liability set forth in the reinsurance accepted amount. Critically, the Munich Re certificate did not contain any such provision.

The appeals court also rejected the idea, advanced by reinsurers, that there was a presumption mandating a preordained result for all reinsurance agreements. Rather, the court evaluated the particular terms of the reinsurance agreement at issue, found the terms ambiguous, and returned the case to the trial court for further proceedings.

The U.S. District Court for the Northern District of New York followed suit.[9] Like the 2nd Circuit in *Utica v. Munich Re*, the District Court noted key differences between the reinsurance agreement at issue in the case before it and the reinsurance agreements in *Bellefonte*.

Once again, consistent with well-established contract law, the court focused on the particular terms at issue rather than any purported presumption on which the reinsurer relied. As in *Utica v. Munich Re*, the court found the terms ambiguous and denied the reinsurer's motion for partial summary judgment. The parties then reached a settlement in principle.[10]

THE *CENTURY–ONEBEACON* CASE

The most recent decision on this issue came from the Philadelphia Court of Common Pleas after a bench trial in *Century Indemnity Co. v. OneBeacon Insurance Co*.[11] The bench trial followed the court's earlier decision denying the reinsurer's motion for summary judgment, which sought a ruling that the reinsurance accepted amount limited the reinsurer's liability.[12]

In the summary judgment decision, the court followed *Utica v. Munich Re* and refused to apply any presumption that the reinsurance accepted amount capped liability. It construed the terms of the reinsurance agreements and found them ambiguous.

At trial, the insurers introduced testimony from their former underwriters about the companies' policies and practices to purchase facultative reinsurance that was "concurrent" with the insurers' own policies for which it was buying the reinsurance.

In other words, if the insurer's own policies covered defense costs in addition to limits, the insurer purchased reinsurance to similarly cover defense costs in addition to the "limits" in the reinsurance agreements. The court also heard from industry experts who opined on custom and practice.

After the trial, the court decided that the reinsurance accepted amounts applied only to the reinsurer's share of settlements and did not establish a cap on the reinsurer's liability.

The court also concluded that the reinsurance agreements provided coverage for defense costs in addition to the reinsurance accepted amounts, just like the insurers' policies provided coverage for defense costs in addition to the limits in those policies.

The decision in *Century v. OneBeacon* is important because it was the first bench trial to address the reinsurance limits issue after the 2nd Circuit's decision in *Utica v. Munich Re*. With the benefit of a full record — including testimony from individuals involved in purchasing reinsurance and expert opinions about custom and practice — the court correctly rejected the one-size-fits-all approach that some reinsurers advocate. Instead, it carefully evaluated the specific contract terms and the evidence about the parties' intent, taking an approach that more courts should follow.

A series of recent rulings have properly focused on the specific terms of the reinsurance agreement and have found that reinsurance accepted amounts do not necessarily cap reinsurers' liability.

NOTES

[1] *See Bellefonte Reinsurance Co. v. Aetna Cas. & Sur. Co.*, 903 F.2d 910 (2d Cir. 1990). This reinsurance limits dispute concerns "facultative reinsurance," which applies to one specific policy. It does not concern "treaty reinsurance," which applies to a group of policies like property insurance policies.

[2] *See* Eugene Wollan, *Sing a Song of Reinsurance*, ARIAS-U.S. Quarterly (First Quarter Review 1999) ("Many members of the reinsurance community were shocked by *Bellefonte* and *Unigard*, not because they were inherently horrifying decisions, but because they ran in the face of long-standing industry practice."); Michael H. Goldstein, *For Whom Does Bellefonte Toll? It Tolls for Thee*, 9 Mealey's Litig. Rep.: Reins. 12
(Aug. 13, 1998) (noting that commentators criticized *Bellefonte* as "utterly at odds with decades-old custom and practice").

[3] Goldstein, *supra* note 2 (noting that *Bellefonte* "has been roundly criticized in the reinsurance industry"); *see also* Michael H. Goldstein, *Bellefonte Lives*, 8 Mealey's Litig. Rep.: Reins. 9 (Sept. 24, 1997) (noting that *Bellefonte* "was met by almost universal condemnation and in some quarters ridiculed by insurance and reinsurance claims people").

[4] P. Jay Wilker & Edward K. Lenci, *Much Ado About Nothing: A Response Regarding Bellefonte's Reach*, 9 Mealey's Litig. Rep.: Reins. 16 (Sept. 24, 1998) (expressing frustration that reinsurers rely on *Bellefonte* as the rule "from sea to shining sea").

[5] *See, e.g.*, *Utica Mut. Ins. Co. v. Munich Reinsurance Am.*, 976 F. Supp. 2d 254, 264 (N.D.N.Y. 2013), *rev'd*, 594 F. App'x 700 (2d Cir. 2014).

[6] *See Pac. Emp'rs Ins. Co. v. Global Reinsurance Corp. of Am.*, No. 11-cv-6301, ECF No. 1 at Ex. 1 (S.D.N.Y. Sept. 9, 2011) (panel's arbitration award).

[7] *See Pac. Emp'rs Ins. Co. v. Global Reinsurance Corp. of Am.*, No. 09-cv-6055, 2010 WL 1659760 (E.D. Pa. Apr. 23, 2010), *rev'd on other grounds*, 693 F.3d 417, 421 (3d Cir. 2012).

[8] *Utica Mut. Ins. Co. v. Munich Reinsurance Am.*, 594 F. App'x 700 (2d Cir. 2014).

[9] *Utica Mut. Ins. Co. v. R&Q Reinsurance Co.*, No. 13-cv-1332, 2015 WL 4254074 (N.D.N.Y. June 4, 2015).

[10] *Id.*, ECF No. 103.

[11] *Century Indem. Co. v. OneBeacon Ins. Co.*, No. 02928, *order and findings of fact issued* (Pa. Ct. Com. Pl. Feb. 23, 2016).

[12] *Id.*, 2015 WL 10436083 (Mar. 27, 2015).



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