

Following The Money To Resolve Policy Disputes

Law360, New York (August 20, 2012, 1:20 PM ET) -- The United States Court of Appeals for the First Circuit supported an interpretation of arguably ambiguous policy language by considering whether that interpretation made “economic sense.” *OneBeacon America Insurance Co. v. Commercial Union Assurance Co. of Canada*, No. 11-2072, 2012 U.S. App. LEXIS 14205, 1st Cir. (July 11, 2012).

The disputed policy language concerned whether the direct insurer was reinsured. For the policy years in dispute, extrinsic evidence showed that the direct insurer retained all of the direct premiums and ceded none. The U.S. Court of Appeals for the First Circuit rejected arguments from the direct insurer that a claimed policy ambiguity precluded summary judgment.

The First Circuit noted that economic realities foreclosed any interpretation allowing the direct insurer to keep all of the direct premiums yet bear no risk.

Direct Policy Language in Dispute

OneBeacon and Aviva USA both issued direct insurance to different subsidiaries of a common corporate entity, *Harrisons & Crosfield Teas Inc.* OneBeacon insured the U.S.-based subsidiaries while Aviva insured the Canadian division.

For the 1980 term, the OneBeacon policy issued to *Harrisons U.S.* contained an endorsement providing that the policy or any renewal thereof was 100 percent reinsured by Aviva. The 1980 Aviva policy to *Harrisons Canada* acknowledged the reinsurance arrangement between Aviva and OneBeacon.

For 1981, however, the OneBeacon and Aviva policies differed. The court noted tension between the terms of the policies issued by OneBeacon and Aviva. The 1981 Aviva policy issued to *Harrisons Canada* stated that *Harrisons U.S.* was “excluded” from the policy and that the policy did not “inure to [the] benefit” of *Harrisons U.S.*

The Aviva policy, however, did not expressly mention reinsurance one way or another. The 1981 OneBeacon policy issued to *Harrisons U.S.* stated that it was a “renewal” of the 1980 *Harrisons U.S.* policy, which — as mentioned above — stated that it and “any renewals” were reinsured by Aviva. The 1982 policies were treated as having substantially the same language as the 1981 policies.

Reinsurance Certificate

There was other evidence before the First Circuit. For example, Aviva issued to OneBeacon a reinsurance certificate evidencing the facultative reinsurance in place for 1980 (facultative certificate).

The First Circuit took notice that no similar certificate issued for the 1981 or 1982 policy years.

Underlying Lawsuit and Ensuing Reinsurance Coverage Dispute

OneBeacon received notice of lawsuits against Harrisons U.S. for asbestos-related injuries implicating the 1980 through 1982 policy terms. OneBeacon assumed defense obligations for those lawsuits. OneBeacon requested full reinsurance indemnification of defense costs.

Aviva responded that it would reimburse OneBeacon for only one-third of defense costs (for 1980), stating that it did not reinsure OneBeacon for 1981 or 1982.

OneBeacon sued Aviva in the United States District Court for the District of Massachusetts. Both parties cross-moved for summary judgment.

The district court ruled in favor of Aviva, finding no reinsurance in favor of OneBeacon after 1980. On appeal, OneBeacon argued that the 1980 OneBeacon and Aviva policies specifically stated that Aviva reinsured “any renewals,” the 1981 Harrisons U.S. Policy was a renewal of the 1980 Harrisons U.S. Policy (and the 1982 Harrisons policy was a renewal of the 1981 Harrisons U.S. policy), and because the 1981 and 1982 Aviva policies did not preclude or address reinsurance, Aviva was therefore contractually obligated to reinsure OneBeacon 100 percent.

OneBeacon also argued in opposition to Aviva’s motion that, in the alternative, the policy language was at least ambiguous as to reinsurance for 1981 and 1982.

First Circuit’s Reasoning

The First Circuit relied on both the direct policy language and extrinsic evidence to affirm the lower court’s decision awarding summary judgment to Aviva.

Given that the direct policies issued to Harrisons & Crosfield were not agreements between OneBeacon and Aviva — the parties to the reinsurance dispute — and given that the First Circuit noted certain terms of those policies were “arguably” ambiguous as to reinsurance obligations, the First Circuit considered extrinsic evidence.

The court focused on whether its policy interpretations meshed with the economic realities as shown by the extrinsic evidence.

The Policy Language

The First Circuit began its analysis by considering the competing policy language. It explained that the

direct policies at issue supported Aviva's argument that there was reinsurance in place only for 1980 but not for 1981 and 1982.

As the court stated:

"[E]ven if we assume arguendo that the 1980 Aviva and OneBeacon policies formed the parties agreement in 1980, this does not help OneBeacon. For if the various 1980 policies established the original agreement between the parties, the record makes clear that the parties changed the terms of their agreement in 1981."

As the court explained, "[I]n contrast to the 1980 OneBeacon Policy, 1981 and 1982 OneBeacon policies did not tell Harrison's U.S. that Aviva was standing behind OneBeacon as the reinsurer."

Extrinsic Evidence

The First Circuit also noted that to the extent any ambiguity existed in the policy language as to whether the 1981 and 1982 OneBeacon policies were reinsured, Massachusetts law allows the court to examine extrinsic evidence.

The First Circuit looked primarily at two pieces of evidence to support their interpretation of the policies.

First, the court noted the absence of a facultative certificate between Aviva and OneBeacon for the second and third policy years. This suggested to the First Circuit that the relationship between the two companies changed after the 1980 term.

Secondly "and most importantly" the court relied on OneBeacon's ledgers, which showed that while direct premium paid by Harrison's was shared between OneBeacon and Aviva in 1980, this was not the case for 1981 and 1982.

For those terms, there was no evidence that OneBeacon ceded any premium and, correspondingly, there was no evidence that Aviva received premium from OneBeacon for the Harrison's risk at issue. As the court stated, a finding that OneBeacon kept all the premiums for the 1981 and 1982 policy years yet bore none of the risk "would defy economic sense."

The First Circuit drove home its economic reality message by pointing out that the same premium ledgers also showed the presence of a "reinsurance code" for 1980, but that no such code was shown in OneBeacon's ledgers for 1981 and 1982.

Analysis

This case is notable because the court examined premium flow to resolve a claimed ambiguity in policy language. Possibly Aviva might have prevailed on its motion for summary judgment based only on the language of the direct policies — or lack thereof — and the absence of reinsurance certificates for the relevant years, or at least defeated summary judgment in OneBeacon's favor.

The First Circuit's opinion, however, seems to draw substantial comfort in its grant of summary judgment to Aviva over the claim of ambiguity by OneBeacon from the extrinsic evidence in the record.

The undisputed evidence that OneBeacon kept all premiums for the 1981 and 1982 terms put the court over the top and allowed it to set aside concerns about the intent of the “or any renewal thereof” wording in the 1980 OneBeacon policy. OneBeacon kept all the premiums in 1981 and 1982 so there couldn’t be any reinsurance — it wouldn’t make “economic sense” — and OneBeacon’s ledger proved this.

In the correct case, “following the money” might assist a court in determining how to interpret contested policy language and could even overcome an arguable claim of ambiguity.

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