DOES A SERVICE OF SUIT CLAUSE IN A REINSURANCE CONTRACT BAR REMOVAL OF A DISPUTE TO FEDERAL COURT?

by
Robert M. Hall

[*Mr. Hall is a former law firm partner, a former insurance and reinsurance company executive and acts as a reinsurance and insurance consultant and expert witness as well as an arbitrator and mediator of insurance disputes. The views expressed in this article are those of the author and do not reflect the views of his clients.* *Additional background on the author and his other publications can be found on his website: robertmhall.com.*]

I. Introduction

State credit for reinsurance laws and regulations govern the circumstances under which ceding insurers can take financial statement credit for reinsurance. With respect to reinsurers which are unlicensed or unauthorized in a state in which the ceding insurer is licensed, a number of specific provisions are required to be inserted into the reinsurance contract. Among these provisions is an agreement by the reinsurer to consent to service of suit in any court of competent jurisdiction *i.e.* in the United States.[1] To those, such as the author, who have spent many years negotiating, drafting and applying credit for reinsurance laws and regulations, the purpose of the service of suit clause is to obtain personal jurisdiction over non-US reinsurers so that a US cedent is not required to travel to distant jurisdictions to litigate their claims (if arbitration is not the remedy of choice) or to enforce the awards of arbitration panels.

Unfortunately, the service of suit clause can create confusion when it placed in a reinsurance contract that also contains a mandatory arbitration provision. The issue is whether or not the service of suit clause waives the right of a reinsurer to remove the dispute to federal district court where arbitration can be ordered under the Federal Arbitration Act. This confusion is exemplified by two recent decisions of issued by the US District Court for the Southern District of New York reaching opposite results. In *Dinallo v. Dunav Ins. Co.*, 2009 U.S. Dist. Lexis 10833 (S.D.N.Y.)[2] the court found that the service of suit clause waived any right of removal. However, a few months earlier another judge in the same court ruled that any waiver of removal had to be explicit and found an essentially identical service of suit clause ambiguous. *B. D. Cooke v. Certain Underwriters at Lloyd's London*, 2009 U.S. Dist. Lexis 27143 (S.D.N.Y.).

The purpose of this article is to review selected case law exemplifying the traditional rule (*i.e.* that waiver of removal will be enforced) and certain exceptions to this rule including the Foreign Sovereign Immunity Act ("FISA"), 28 U.S.C. § 1603 and Congress' ratification in 1970 of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("Convention").

II. The Traditional Rule

City of Rose City v. Nutmeg Ins. Co., 931 F.2d 13 (5th Cir. 1991) involved a policy issued by a Connecticut domestic insurer which contained a service of suit clause. When a suit was filed, the insurer attempted to remove it and the insured resisted. The court found that the service of suit clause waived removal:

> On its face, the endorsement is unambiguous. It plainly requires that the insurer submit to the jurisdiction of any court of the policyholder's choosing. Nutmeg agreed to "submit to the jurisdiction of any court", to "comply with all

> requirements necessary to give such court jurisdiction," and to "abide by the final decision of such court." Thus, while the provision does not specifically mention the right of a defendant to remove an action from state to federal court, the language of the clause makes clear that the policyholder shall enjoy the right to choose the forum in which any dispute will be heard.[3]

The *City of Rose* court distinguished *Delta America Re v. National Distillers & Chemical Corp.*, 900 F.2d 890 (6th Cir. 1990) (*infra*, section III) on the basis that the latter case involved a non-US reinsurer.

Another case involving a service of suit clause in a policy issued by a US domestic insurer is *Russell Corp. v. American Home Assurance Co.*, 264 F.3d 1040 (11th Cir. 2001). The court held that the clause was a waiver of removal:

> [E]very federal court (excluding those addressing removal under the Foreign Sovereign Immunities Act) interpreting this clause has determined that language essentially identical to that contained in the First State policy constitutes a waiver of the right to remove. (citations omitted.) Thus, the collective holdings of all federal courts that have addressed similar service of suit clauses would support a remand in this case because First State consented to be sued in any jurisdiction chosen by [the insured] thereby waiving its right to remove this case to federal court.[4]

Foster v. Chesapeake Ins. Co., 933 F.2d 1207 (3rd Cir. 1991) was a suit by the receiver of an insurance company against a US domestic reinsurer. Pursuant to credit for reinsurance laws, the reinsurance contract contained a service of suit clause. The court ruled that such clause waived the reinsurer's removal rights.

A reinsurance contract containing a service of suit clause with a London-based reinsurer was at issue in *Travelers Ins. Co. v. Certain Underwriters at Lloyd's London*, 1993 U.S. Dist. Lexis 491 (S.D.N.Y.) *aff'd on other grounds* 996 F.2d 1485 (2nd Cir. 1993). In finding a waiver of removal rights, the court cited many cases invoking the traditional rule. In addition, the court distinguished *McDermott International, Inc. v. Certain Underwriters at Lloyd's London*, 944 F.2d 1199 (5th Cir. 1991) (*infra*, section IV) on the bases: (1) the contracts involved in this case covered periods of time before the Convention on the Recognition of Foreign Arbitral Awards was adopted by Congress; and (2) the reinsurers in this case should have been aware from their involvement in prior litigation wherein the courts ruled that the service of suit clause waived the right of removal.

It should be noted that there is a line of cases holding that a service of suit clause does not constitute a waiver of removal rights even when the exceptions described in the following sections are not present. *See e.g. Credit General Ins. Co. v. John Hancock Mutual Life*, 2000 U.S. Dist. Lexis 9009 (N.D.Ohio) and cases cited therein. The *Credit General* court ruled:

> [T]he Arbitration clause and the Service of Suit clause do not conflict. All the above cases found that the Service of Suit clause is intended to be used to enforce

> an arbitration award, since an arbitration award is not self-enforcing. . . . Neither clause conflicts, and each clause has an effect.[5]

III. **Foreign Sovereign Immunity Act**

Delta America Re Ins. Co. v. National Distillers & Chemical Corp., 900 F.2d 890 (6th Cir. 1990) involved an insolvent Kentucky-domiciled reinsurer ("Delta Re") which sought recoverables from a retrocessionaire owned by a foreign sovereign. The retrocessionaire sought to remove the action to federal court based on 28 U.S.C. § 1141 (d) which states: "Any civil action brought in a State court against a foreign state as defined in section 1603 (a) of this title may be removed by the foreign state to the district court of the United States for the district and division embracing the place where such action is pending."

In addressing the waiver of removal issue, the court first noted that the above language was "standard" in all the relevant contracts and was not negotiated. (Apparently, the court was not informed that the language, or some variation thereof, was mandatory if the reinsurance was to have the intended financial statement impact.) The court viewed this factor as weighing against waiver.[6]

Next the court developed a standard for judging a waiver based on the significance of section 1441 (d) of the FSIA:

> It enables foreign states, at their option, to avoid any local bias or prejudices possibly inherent in state court proceedings and also to avoid trial by jury. These are not insignificant concessions, given the restrictions on foreign sovereign immunity mandated by the FSIA. Although Congress made it very clear that foreign states have the right of removal, this does not mean, of course , that they may not waive that right. Against the backdrop of the FSIA, however, the principle that waiver must be clear and unequivocal assumes even greater significance.[7]

The court then observed that the service of suit language was less a forum selection clause than it was a "submit to the jurisdiction of a U.S. court" clause *i.e.* creating *in personam* jurisdiction. Thus, removal does not impinge on *in personam* jurisdiction. [8] Based on all of the above factors, the court found that waiver of removal rights had to be "explicit," which it was not in this case.[9]

IV. **Convention on the Recognition and Enforcement of Foreign Arbitral Awards**

The leading case applying the Convention to the issue of waiver of removal rights is *McDemott International, Inc. v. Certain Underwriters at Lloyd's London*, 944 F.2d 1199 (5th Cir. 1991) which involved an insurance policy with a service of suit and mandatory arbitration clause. The court recognized two readings of these clauses which do not require waiver of removal: (1) the service of suit clause applies to suits involving enforcement of an arbitration award; and (2) the service of suit clause is intended, merely, to create personal jurisdiction in the United States. The latter point allowed the court to distinguish a case handed down by the same court earlier in the year in which the insurer was a U.S. domestic: *City of Rose City v. Nutmeg Ins. Co.*, 931 F.2d 13 (5th Cir. 1991) (*supra*, section II). After a long analysis of the Convention and its enabling

legislation, the court held that any waiver of the right of removal had to be explicit to be effective.

Suter v. Munich Reinsurance Co., 223 F.3d 150 (3rd Cir. 2000) involved an effort by a non-US domiciled reinsurer to remove a dispute under a reinsurance contract that contained the service of suit clause required by credit for reinsurance laws. The precedential context was *Foster v. Chesapeake Ins. Co.*, 933 F.2d 1207 (3rd Cir. 1991) (*supra*, section II), which found a waiver for a US domestic reinsurer and two non-insurance cases finding that a waiver under the FSIA must be explicit. After analyzing the policy similarities behind the FSIA and the Convention, the court adopted a "clear and unambiguous language" standard for waiver commenting:

> In sum, four of the "peculiar" considerations noted by this Court in Foster as a basis for waivers of removal rights under the FSIA differently than waivers of removal rights under the diversity statute are equally present under the Convention Act: (1) the broad removal statute; (2) the purpose of avoiding local bias and prejudice possibly inherent in state court proceedings; (3) the "drastic departure" from a previously long-standing rule; and (4) the interest in uniformity.[10]

V. Conclusion

Service of suit clauses are contained in reinsurance contracts because they are, in effect, required by credit for reinsurance laws and regulations if the reinsurer is unlicensed or unauthorized in the states in which the cedent is licensed. These clauses are intended to give the cedent *in personam* jurisdiction over the reinsurer in the United States to avoid the necessity of litigating or enforcing an arbitration award in a non-US jurisdiction. Therefore, it is inappropriate for the courts to treat a service of suit clause as a voluntary or negotiated-for waiver of a right of removal.

Nonetheless, under the traditional rule, the courts do exactly that, depriving reinsurers of a federal forum due to state credit for reinsurance laws and regulations which are intended to make easier collection of reinsurance recoverables. Under the *Credit General* line of cases, however, the courts can enforce both the service of suit and arbitration clauses in a manner that preserves the rights of both cedents and reinsurers.

The Foreign Sovereign Immunity Act exception largely preserves a federal forum for reinsurers owned by foreign nations but there are very few such reinsurers and, as a result, this line of cases serves primarily as an analogy. The Convention on the Recognition and Enforcement of Foreign Arbitral Awards exception is much more useful for non-US reinsurers however, it does not close the gap for US-domiciled reinsurers which are not licensed or authorized in each and every state in which a cedent is licensed. Ironically, the Convention exception results in better removal rights on the part of non-US reinsurers than for some US –domiciled reinsurers.

ENDNOTES

1 Robert M. Hall, *Should Reinsurance Contracts be Construed Against Reinsurers?* § II B. XI Mealey's Reins. Rpt. No. 3 at 22 (2000) also available at the author's website: robertmhal.com.

2 Reconsideration denied, 2010 U.S. Dist. Lexis 7958 (S.D.N.Y.).

3 931 F.2d 13 at 15.

4 264 F.3d 1040 at 1047.

5 2000 U.S. Dist. Lexis*15.

6 *Id.* at 893.

7 *Id.*

8 *Id.*

9 *Id.* at 894

10 223 F.3d 150 at 159.