Arbitration – global insurers' last line of defence against jurisdiction in the United States

1. Introduction

In two recent cases, US courts have asserted jurisdiction over non-US based insurers in coverage disputes relating to global insurance policies governed by foreign law and concluded with non-US based parent companies. At the same time, in a strong endorsement of international arbitration, the courts refused to assert jurisdiction in relation to global policies which provided for the resolution of disputes through international arbitration outside of the United States. Global insurers may, therefore, no longer be left with any other choice than to include arbitration as the means of dispute resolution in their global insurance policies in order to avoid the risk and additional cost of coverage litigation in the United States.

2. International insurance programmes

International insurance programmes have become routine daily business in today's increasingly globalized world. These programmes are commonly structured around a centrally coordinated master insurance policy entered into between a parent company and a lead insurer in their common country of establishment. The international subsidiaries of the parent company are not parties to the master policy, but are usually included in the scope of the master policy as additional insureds. In addition, the lead insurer arranges for local fronting insurers, as part of the master programme, to issue local policies to the parent's subsidiaries in the relevant jurisdictions worldwide. Limited coverage under the local policies is supplemented by broader excess coverage under the master policy.

An important feature of these international programmes is that lead insurers seek to limit their exposure to coverage litigation to coverage issues under the master policy to be determined by a court or arbitral tribunal in the lead insurer and parent company's common country of establishment in accordance with the familiar laws of that country. Coverage issues under the local policies should be determined by a court or arbitral tribunal in the relevant local jurisdiction in accordance with the laws of that jurisdiction. The lead insurer should normally not be a party to such local coverage actions since it is not a party to the local policies.

Moreover, the local court or arbitral tribunal should not normally have jurisdiction over the master policy since the local subsidiary is not a party to the master policy. In this manner, the lead insurer seeks to avoid disputes regarding the broader coverage under the master policy being determined in unfamiliar jurisdictions where the cost and risk of litigation may be much higher than in the insurer's own jurisdiction. This conventional understanding of the extent of the lead insurer's exposure to coverage litigation has been turned on its head by the two cases outlined below.

3. ESAB Group v Zurich Insurance[1]

ESAB Group was a South Carolina-based manufacturer of welding materials and equipment. From 1989 to 1994, ESAB Group operated as a subsidiary of the Swedish company ESAB AB. In 1994, ESAB Group was sold to the British company Charter plc. Throughout this time, ESAB maintained its principal place of business in Florida, South Carolina, where it had a manufacturing plant, executive offices, and sales, engineering, and research development divisions. Between 1989 and 1996, the Swedish insurer Trygg Hansa issued seven global liability insurance ("GLI") policies to ESAB AB. Under the master policies, Trygg-Hansa agreed to provide coverage to ESAB AB and its subsidiaries. Special endorsements in the master policies specifically extended coverage to ESAB Group and its predecessors and pursuant to the territory clauses in the master policies, the policies applied to occurrences "worldwide". Five of the master policies, from 1989 to 1993, contained arbitration clauses providing for the resolution of disputes by arbitration in Sweden in accordance with Swedish law. The other master policies, from 1994-1995, included Swedish choice-of-law provisions, but did not include arbitration clauses. Trygg Hansa transferred its obligations under the policies to Zurich Insurance Company through a 1998 loss portfolio transfer agreement. Zurich Insurance Company then transferred the obligations to Zurich Insurance plc ("ZIP"), an Irish insurer, in 2005.

A series of product liability suits were brought against ESAB Group arising from alleged personal injuries caused by exposure to welding consumables manufactured by ESAB Group and its predecessors. These suits are proceeding in numerous state and federal courts in the United States. As of 12 June 2009, ESAB Group had incurred more than $54 million in defense costs and suffered adverse verdicts in excess of $25 million. ESAB Group requested that its insurers defend and indemnify it in these product liability actions. Several insurers, including ZIP, refused coverage. As a result, ESAB Group brought a coverage action against its insurers in the South Carolina state court. The case was removed to the United States District Court for the District of South Carolina, where ZIP challenged the court's jurisdiction on the grounds that (i) the Court lacked personal jurisdiction over ZIP, (ii) the Court was required to enforce the arbitration clauses, and (iii) a more convenient forum was available in Sweden under the doctrine of forum non conveniens.[2]

Personal jurisdiction

In its submissions to the Court, ZIP emphasized its limited contacts with South Carolina. It had no offices or other facilities in South Carolina, owned no property there, was not licensed as an insurer by South Carolina, and did not regularly conduct business in the state. Although the scope of the ZIP master policies was worldwide and thus extended coverage to ESAB Group, ZIP argued that this was an insufficient basis for personal jurisdiction because the contracts were negotiated, drafted and executed in Sweden by two Swedish companies, ESAB AB and Trygg Hansa. In response, ESAB Group pointed to the fact that each master policy applied to occurrences "worldwide" and further contained specific endorsements whereby ESAB Group and its predecessors were added as additional insureds. According to ESAB Group, these facts demonstrated that ZIP had purposefully availed itself of the privilege of doing business in South

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[1] See the ESAB Group v Zurich Insurance plc et al, United States District Court District of South Carolina Florence Division, No. 4:09-cv-01701-JMC-TER.

[2] Ibid.

Carolina. The Court held that, based on the facts of the case, ZIP had sufficient minimum contacts with South Carolina and that, while there was some burden on ZIP having to litigate the action in South Carolina, the exercise of personal jurisdiction was reasonable and did not offend traditional notions of fair play and substantial justice.[3]

Arbitration clauses

ZIP argued that the Court was required to enforce the arbitration clauses in accordance with the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “Convention”) and its implementing legislation, Chapter Two of the Federal Arbitration Act (the “Convention Act”)[4]. The Court cited the Convention as providing that each signatory nation “shall recognize in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration”[5]. The Court further cited Article II(3) of the Convention which provides “[t]he court of a Contracting State, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed.”

ESAB Group did not contest the fact that five of the seven ZIP master policies at issue contained arbitration clauses. However, because the arbitration clauses were contained within insurance policies, ESAB argued that the Convention and the Convention Act were reverse-preempted by §15-48-10(b)(4) of the South Carolina Code, which provides that South Carolina Uniform Arbitration Act “shall not apply to … any insured or beneficiary under any insurance policy or annuity contract.” Generally, under the Supremacy Clause in the US Constitution, treaties trump any inconsistent state law that otherwise might be applicable[6].

However, the Mc Carran-Ferguson Act[7] commits the regulation of insurance to state law. Under the Mc Carran-Ferguson Act, any state law enacted for the purpose of regulating insurance will trump, or reverse-preempt, any contrary federal statute that does not relate specifically to insurance. Section 1012(b) of the Mc Carran-Ferguson Act provides that “[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance … unless such Act specifically relates to the business of insurance.” South Carolina courts had regularly applied McCarran-Ferguson to reverse preempt domestic arbitration clauses in insurance contracts[8], but the question of whether the act could reverse preempt international arbitration agreements had never before been addressed.

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[3] Opp cit *ESAB*, pp. 16-23.
[4] 9 U.S.C. § 201, et seq.
[5] Article II(1).
[6] U.S. Constitution, Article VI, clause 2.
[7] 15 U.S.C. § 1011, et seq.
[8] See e.g. Cox 347 S.C. at 468, 556 S.E.2d at 402; Skanska USA Building Inc v Lexington Ins. Co. No. 2:06-2554-PMD, Order p.6 (D.S.C. Dec. 19, 2006); American Health and Life Ins. Co. v. Heyward, 272 F.Supp.2d 578, 581 (D.S.C. 2003).

The Court held that the plain language of the Mc Carran-Ferguson Act limits reverse-preemption by a state law to "Act[s] of Congress". The Mc Carran-Ferguson Act was found to be inapplicable to the Convention because the Convention is a treaty, not an act of Congress, and the Mc Carran-Ferguson Act was found to be inapplicable to the Convention Act because it did not interfere with a state's regulation of insurance matters. The Court, therefore, held that all matters arising out of the GLI policies from 1989-1993 were to be submitted to arbitration in Sweden in accordance with Article II(3) of the Convention and in accordance with the terms of the relevant arbitration clauses.

Forum non conveniens

The Court never ruled on ZIP's argument that South Carolina was not the proper forum given the nature of the claims, the availability of arbitration in Sweden and the choice of law clauses requiring the application of Swedish law.

Appeal

The case was appealed to the United States Court of Appeals for the Fourth Circuit and judgment was given on 9 July 2012.[9] The Court of Appeals affirmed the District Court's decision regarding the enforcement of the arbitration clauses in accordance with the terms of the Convention. It was held that the 1989-1993 GLI policies contained valid arbitration clauses subject to the Convention and the Convention Act and hence the District Court had properly compelled arbitration in Sweden of ESAB Group's claims under these policies.

Regarding the 1994-1995 master policies, ZIP once again submitted that the District Court lacked personal jurisdiction over it. ZIP argued that, although the ESAB Group and its predecessors were covered under the policies, its contacts with the state were too weak to provide a basis for jurisdiction. Moreover, the exercise of jurisdiction was unreasonable taking into account, inter alia, the fact that the contracts designated Swedish law as the governing law.

The Court of Appeals applied a three-part test to determine whether the exercise of personal jurisdiction over ZIP conformed with due process considering "(1) the extent to which the defendant purposefully availed itself of the privilege of conducting activities in the State; (2) whether the plaintiff's claims arise out of those activities directed at the State; and (3) whether the exercise of personal jurisdiction would be constitutionally reasonable."[10] To meet the first prong, the Court had to find that ZIP had established "minimum contacts" with South Carolina by "purposefully availing itself of the privilege of conducting business under the [state's] laws".[11]

In this regard, the Court referred to the fact that South Carolina was encompassed by the worldwide policy territory and that ESAB Group and its predecessors, companies based in South Carolina, were identified as additional insureds under specific endorsements to the master policies. The court inferred that "ZIP obtained financial benefits, in the form of higher premiums, for agreeing to provide this coverage" and found these facts to demonstrate that "ZIP targeted the forum state

[9] United States Court of Appeals for the Fourth Circuit, No. 11-1243, 9 July 2012.
[10] Opp cit *ESAB*, p. 25 quoting ALS Scan. Inc. V. Digital Serv. Consultants Inc., 293 F.3d 707, 712 (4th Cir.2002).
[11] Ibid.

and purposefully availed itself of the privilege of conducting business under South Carolina law."[12] Accordingly, the first prong, minimum contacts, was satisfied. The parties agreed that the suit arose out of these contacts, thus fulfilling the second prong. As regards the third prong, the court acknowledged that requiring a party to defend itself in a foreign legal system imposes unique burdens, but stated that by contracting to defend ESAB Group worldwide under the GLI policy, ZIP had indicated that the burden of appearing in a forum in South Carolina was not exceedingly onerous. The Court, therefore, concluded that "the burden on ZIP of litigating in South Carolina is not so great – particularly in relation to the interests of South Carolina and of the ESAB Group – to render the exercise of jurisdiction unreasonable."[13] The Court of Appeals accordingly dismissed ZIP's appeal and affirmed the District Court's decision to assert personal jurisdiction

4. Sandvik v Continental, If, Skandia et al[14]

This case concerned a coverage action decided upon in the Superior Court of New Jersey in 2011 where Sandvik, Inc. and Sandvik AB (collectively "Sandvik") sought to recover costs for investigation, defense, and indemnity in connection with claims arising from pollution at a facility owned and operated by Sandvik, Inc. in Clarks Summit, Pennsylvania. The action was brought against two Swedish insurance companies, Försäkringsaktiebolaget Skandia (publ) ("Skandia") and If Skadeförsäkring AB (publ) ("If"), as well as five U.S. insurance companies which issued primary local policies or (in one case) a specialty "pollution legal liability" insurance policy to Sandvik Inc. Skandia issued GLI policies during the period from May 25, 1976 to January 1, 1986 to Sandvik AB, Sandvik's parent company, which provided insurance coverage in excess of certain local policies issued in countries, including the United States. Sandvik, Inc. was an additional insured under the master GLI policies.

As part of a global portfolio transfer in 1998-1999, If assumed all of Skandia's rights, obligations, and liabilities in connection with the GLI Policies. Sandvik AB, Skandia and If are Swedish companies located in Sweden. Sandvik was denied coverage on the grounds of an environmental pollution exclusion clause in the GLI policies.

If and Skandia sought dismissal of the action on the grounds that the New Jersey Court lacked personal jurisdiction because the GLI policies were negotiated, executed, and delivered to Sandvik AB in Sweden. If and Skandia maintained that they were not subject to the general jurisdiction of the Court since neither If nor Skandia had any substantial, continuing or systematic contacts with New Jersey. Neither If nor Skandia were authorized to transact business in New Jersey. Neither company had offices, bank accounts, operations, assets, property, employees, or agents in New Jersey. They did not rent or lease property in New Jersey or anywhere else in the United States and did not pay taxes or solicit business in New Jersey or anywhere else in the United States. Nor was either company licensed to transact business in New Jersey.

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[12] Opp cit *ESAB*, p. 27.
[13] Opp cit *ESAB*, p.27.
[14] Sandvik Inc and Sandvik AB v Continental Insurance Company, Försäkringsaktiebolaget Skandia (publ), If Skadeförsäkring AB (publ) et al, No. BER-L-11103-09, Decision of the Superior Court of New Jersey Law Division: Bergen County, June 22 2011.

Accordingly, neither If nor Skandia had and the requisite “minimum contacts” with New Jersey and the action did not arise out of any activity that If or Skandia purposefully directed at New Jersey. In the alternative, If and Skandia sought dismissal of the action based on forum non conveniens arguing that the GLI master policies are Swedish insurance contracts, written in Swedish, which were negotiated, executed, and delivered in Sweden; the premiums were paid to Skandia in Sweden and the current dispute with respect to coverage under these policies for the environmental claims at issue should be resolved in Sweden. If and Skandia further argued that a Swedish court is in a better position to interpret the GLI policies than an American court, since a key issue in dispute was the meaning of a Swedish term in the pollution exclusion in the policies.

Despite these facts, the Court held that it had personal jurisdiction over both If and Skandia. The New Jersey Court also applied a three-part test to determine whether jurisdiction could be asserted. First, the Court examined whether If had “minimum contacts” with New Jersey. In finding that Skandia and If had multiple contacts with New Jersey, the Court asserted that Skandia and If had directly insured Sandvik Inc in New Jersey for over thirty years and that each of those insurance contracts had “foreseeable future consequences” in New Jersey.[15] Pursuant to those insurance contracts and the GLI programme to which they were a part, the Court highlighted the fact that Skandia and If had (i) participated in meetings in New Jersey, (ii) arranged for fronting policies to be issued to Sandvik Inc in New Jersey, (iii) participated in the handling and defense of claims, and (iv) paid claims directly to Sandvik Inc. In applying the second part of the test, the Court went on to weigh the sufficiency of these contacts concluding that If did indeed have sufficient minimum contacts with New Jersey.

In the third and final part of the test, the Court assessed whether asserting jurisdiction complied with “fair play and substantial justice”. The Court found no evidence that If or Skandia would suffer any burden by having to defend themselves in New Jersey; “[d]efending a suit in one of the United States … is not as burdensome as it once might have been, given that air transport can bring the principals of a business here within hours and instantaneous communication allows an ongoing dialogue with counsel in this country”.[16]

Dismissing If and Skandia's assertions that the Swedish courts were the appropriate forum for a dispute concerning a contract concluded in Sweden between two Swedish companies, the Court stated that “the evidence and legal issues were mainly located and best resolved in the United States”.[17]

The Court found significant interest on behalf of New Jersey in adjudicating the dispute on the grounds that Sandivk Inc had been a New Jersey resident for fifty years and was a named additional insured under the GLI master policies. The Court further rejected If and Skandia's argument that the dispute would not be efficiently resolved since a decision from the New Jersey court would not be enforceable in Sweden. Accordingly, the Court held that If and Skandia had

[15] Ibid, p.17.
[16] Opp cit *Sandvik*, p. 21, citing Nicastro, 201 N.J. At 76
[17] Op cit *Sandvik*, p. 22.

failed to sustain the burden of showing that an assertion of jurisdiction would violate fair play and substantial justice.

The New Jersey Court then went on to find that the Court also had general jurisdiction over If and Skandia. General jurisdiction is to be distinguished from specific jurisdiction insofar as the latter requires the plaintiff’s claim to arise out of specific minimum contacts between the defendant and the forum state. General jurisdiction, on the other hand, applies when a defendant's contacts with the forum are “continuous and systematic” regardless of whether the plaintiff's claim arises out of those contacts or not. In asserting general jurisdiction over If, the Court highlighted, inter alia, the fact that If collected premiums from Sandvik Inc and other entities in New Jersey and conducted insurance business in New Jersey; that If denied claims in New Jersey; and that Skandia US had arranged local fronting policies for Sandvik Inc in New Jersey.

As regards the forum non conveniens argument, the Court found that Sweden was not an adequate alternative forum for the dispute. Although If and Skandia were amenable to process in Sweden, the other US defendant insurers were not. A transfer of the dispute to Sweden would therefore result in fragmented parallel litigations in Sweden and the United States. The Court rejected If's contention that this was a case between Swedish entities disputing a Swedish contract and instead gave considerable deference to Sandvik's choice of its home forum, which “should rarely be disturbed”.[18]

The Court found no evidence that the trial would be reached more expeditiously in Sweden and emphasized that the majority of the evidence in the case was located in New Jersey. If's assertion that a US judgment would not be enforceable in Sweden was found not to be persuasive. As regards choice of laws considerations, the Court stated that if Swedish law needed to be analyzed, the Court was “confident that New Jersey Judges are capable of determining any choice of law issues presented and applying foreign law if required.”[19] The Court denied If's motion to dismiss.

5. Consequences for global insurers

The two cases of ESAB and Sandvik have potentially far-reaching consequences for the international insurance industry. It is now quite clear that US courts have little reluctance in asserting jurisdiction over non US-based lead insurers in the context of international insurance programmes. In both the ESAB case and the Sandvik case, the lead insurers in question had no offices, bank account, operations, assets, property, employees, or agents in the forum US state. They were not licensed, did not pay taxes and did not solicit business in the state. The Courts were not deterred by the fact that the master policies in both cases were negotiated, executed and delivered in Sweden between Swedish insurance companies and Swedish parent companies. It did not matter that the master policies in the ESAB case included Swedish choice of law provisions. Neither did it matter that the dispute in the Sandvik case concerned the interpretation of a Swedish term in the pollution exclusion of the master policies.

[18] Opp cit *Sandvik*, p. 28, citing Varo, 400 N.J. Super. at 523.
[19] Opp cit *Sandvik*, p. 31.

The Courts were willing to assert jurisdiction on essentially one material fact alone: The master GLI policies provided by the lead insurers extended coverage to residents of the forum states. All other circumstances relied upon by the Courts in support of jurisdiction stemmed from the extension of coverage to residents of the forum states as additional insureds under the master policies. The New Jersey Court in the Sandvik case pointed to other facts, such as; Skandia having arranged fronting policies to be issued to Sandvik by local insurers; If having denied claims made by Sandvik Inc in New Jersey under the GLI polices; and If having employed a US lawyer to advise on the claims. However, each of these circumstances stem solely from the extension of coverage under the GLI policy to Sandvik Inc. It is, therefore, clear that non US-based global insurers run a serious risk of being subjected to personal jurisdiction in the United States solely by virtue of their adding a US based subsidiary as an additional insured under a global master policy. This risk arises irrespective of whether the insurer has any other contacts whatsoever with the United States, irrespective of whether the master policy was concluded outside the United States between non US companies, indeed irrespective of whether the master policy was governed by foreign law.

So what should global insurers do? Stop writing global insurance policies? Fortunately, there is a less drastic solution. Global insurers should include arbitration clauses in their master policies. In the ESAB case, the South Carolina State Court and the United States Court of Appeals both upheld the arbitration clauses in the 1989-1993 master policies. In so doing, the Court of Appeals strongly endorsed the application of the New York Convention. In holding that the Convention Act is not subject to reverse preemption under the Mc Carran-Ferguson Act, the Court quoted that "[i]f the United States is to be able to gain the benefits of international accords and have a role as a trusted partner in multilateral endeavors, its courts should be most cautious before interpreting its domestic legislation in such manner as to violate international agreements."[20]

The Court further stated that "to allow "parochial refusal[s]" to enforce foreign arbitration agreements would frustrate the very purpose for which the Convention was drafted: achieving the predictability and orderly resolution of disputes "essential to any international business transaction" and ensuring parties are not haled into hostile or inappropriate forums."[21] The Court of Appeal's decision is binding within the federal district courts of the Fourth Circuit (Maryland, Virginia, West Virginia, North Carolina and South Carolina) and may be considered persuasive in all other federal district courts. It thus sets a strong precedent for US courts enforcing clauses in global master insurance policies providing for the resolution of disputes by international arbitration outside of the United States.

This conclusion is further supported by the facts in the Sandvik case. Sandvik brought its action in the New Jersey Courts based on the GLI master policies entered into between May 25 1976 and 1 January 1986. These policies did not include any forum selection or choice of law clauses. However, Skandia and subsequently If continued to insure Sandvik for twenty years after 1 January 1986 and many of the master policies issued during this later period contained arbitration clauses. The GLI master policy issued by Skandia to Sandvik AB for the period from January 1,

[20] Vimar Seguros y Reaseguros, S.A. v M/V Sky Feefer, 515 U.S. 528, 539 (1995).
[21] Opp cit *ESAB*, p.23 refering to Scherk v Alberto-Culver Co., 417 U.S. 506, 516-17 (1974).

1986 to January 1, 1987 included a Swedish choice of law clause and a provision requiring resolution of disputes through arbitration in Stockholm. During the period from January 1, 1998 through December 31, 2004, arbitration became the standard dispute resolution mechanism. Each GLI master policy issued by Skandia and later If to Sandvik AB during this period contained the following provision:

19. Procedure in the event of a dispute
Any dispute, controversy or claim arising out of or in connection with this contract, or the breach, termination or validity thereof, shall be finally settled by arbitration in accordance with the Insurance Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce.

Accordingly, the GLI policies for 1986 and for the period from 1998 through 2004 clearly contemplated the resolution of disputes between Sandvik AB and Skandia or If through arbitration in Sweden while any disputes with respect to the local policies would be resolved in a separate forum in the local country. One can only assume that the presence of these arbitration clauses influenced Sandvik in its decision to limit its action against Skandia and If in the New Jersey Court to the earlier period when the GLI policies did not include any forum selection or choice of law.

6. Conclusion

In conclusion, non US-based insurers would be well advised to include arbitration clauses in the master policies of their international insurance programmes. This applies in particular where coverage is extended to a US based subsidiary given the likelihood of personal jurisdiction being asserted even in cases where the insurer has in effect no other contacts with the United States. It cannot, however, be ruled out that courts in other countries may be equally willing to assert jurisdiction over international insurers in the context of international insurance programmes. It may, therefore, be advisable to include arbitration clauses in master policies in all international insurance programmes irrespective of whether or not they provide coverage in the United States. In this way, insurers can avoid the risk and additional cost of coverage litigation in foreign jurisdictions and insurance customers can avoid resulting premium increases.

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