UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

RELIANCE INSURANCE COMPANY OF ILLINOIS, Plaintiff, v. RAYBESTOS PRODUCTS COMPANY, Defendants/Third Party Plaintiffs, v. UNITED STATES FIDELITY AND GUARANTY COMPANY, WESTCHESTER FIRE INSURANCE COMPANY and NATIONAL UNION FIRE INSURANCE COMPANY, Third Party Defendants.	)	CAUSE NO. IP97-0027-C-Y/B

Memorandum of Law in Support of Raybestos Products Company's Motion to Vacate Arbitration Award

I. INTRODUCTION

Raybestos Products Company ("Raybestos") submits this Memorandum of Law in support of their Motion to Vacate Arbitration Award. Raybestos respectfully requests this Court to vacate the arbitration award rendered in the case of Raybestos Products Company v. United States Fidelity and Guaranty Company and Westchester Fire Insurance Company, AAA Case No.: 51 195 Y 02181 04, dated June 27, 2006 (the "Award") (attached hereto as Exhibit 1) as to

Westchester Fire Insurance Company ("Westchester").[1] A Memorandum & Order on Cross-Motions for Summary Determination, dated August 10, 2005, was issued by the arbitration panel (the "Panel"). A copy of that decision is attached hereto as Exhibit 2 ("Decision").

The Arbitration Award must be vacated on the following grounds:

1. The Panel specifically refused to apply substantive law to reach its decision, although it was admittedly aware of the law and that it applied to this case.

2. The Panel so imperfectly executed their powers that the Award is a manifest disregard of the law and violates public policy.

A. Statement of Facts

In 1996, the Indiana Department of Environmental Management ("IDEM") notified Raybestos of alleged contamination in Shelly Ditch, which is property that is located adjacent to Raybestos' manufacturing facility in Crawfordsville, Indiana. Raybestos notified one of its insurers, Reliance Insurance Company of Illinois ("Reliance"), of the allegations made by IDEM. On January 9, 1997, Reliance instituted a declaratory judgment action against Raybestos requesting that this Court declare that the insurance policies Reliance issued to Raybestos did not provide coverage for the alleged environmental contamination (the "Reliance Action").

On January 19, 2000, by Memorandum and Order, this Court determined several key issues in the Reliance Action, including: (1) Indiana state substantive law applied to the interpretation of the policies issued by Reliance; and (2) under Indiana law, the absolute

[1] Raybestos has settled its disputes with both United States Fidelity & Guaranty Company ("USF&G") and National Union Fire Insurance Company ("National Union"). Accordingly, by Order of this Court, both USF&G and National Union have been dismissed from this court action.

pollution exclusion in Reliance's insurance policies was unenforceable as a matter of law and would not bar coverage for Raybestos' claim.[2]

When Reliance became insolvent and this Court stayed proceedings, Raybestos thereafter filed a third-party complaint against United States Fidelity & Guarantee Company ("USF&G"), Westchester Fire Insurance Company ("Westchester") and National Union Insurance Company ("National Union") on February 12, 2002. The action against USF&G, Westchester and National Union sought a declaration seeking recovery from these insurers for the clean up of Shelly Ditch under the insurance policies issued to Raybestos.

On May 14, 2002 and July 3, 2002, USF&G and Westchester respectively moved this Court to stay the action and to compel arbitration under Sections 3 and 4 of the Federal Arbitration Act ("FAA"), because of arbitration clauses in their respective policies. This Court denied those motions. USF&G and Westchester appealed, and by opinion dated August 27, 2004 (amended August 30, 2004), the Seventh Circuit Court of Appeals reversed and directed this Court to order the parties to arbitrate. Reliance Ins. Co. v. Raybestos Products Co., 382 F.2d 676 (7th Cir. 2004). On October 18, 2004, this Court entered an Order directing the parties to arbitrate "in accordance with the Rules of the American Arbitration Association and the Federal Arbitration Act." Raybestos thereafter filed its Demand for Arbitration under Indiana Law, a copy of which is attached hereto as Exhibit 4.

Each party filed a Motion for Summary Determination together with briefs and necessary supporting papers asking the Panel to determine which state's substantive law applied to the underlying dispute.[3] Westchester and USF&G also moved that the Panel enter an award in their

[2] A copy of this Court's opinion is attached hereto as Exhibit 3.
[3] Raybestos' Motion for Summary Determination and exhibits is attached hereto as Exhibit 5.

favor based on the absolute pollution exclusion in their policies.[4] The Panel heard oral argument on July 6, 2005. On August 10, 2005, the Panel issued its Decision (Exhibit 2) granting Westchester's Motion for Summary Determination and denying Raybestos' Motion for Summary Determination as moot. The Panel held that it need not apply any law to the dispute between the parties. Rather, the Panel held that it was free to interpret the contract according to its collective best judgment and determined that the absolute pollution exclusion barred Raybestos' claim. (Decision, Exhibit 2 at 4, 6).[5]

As a result of the Panel's ruling, Raybestos is unable to obtain reimbursement from Westchester[6] for costs incurred for the defense and environmental clean-up of Shelly Ditch, which are in excess of Twenty-Three Million ($23,000,000.00) Dollars.

Although Raybestos argued that arbitrators are required to follow substantive law, and the Panel recognized this duty, it refused to apply any substantive law to the underlying dispute. (Transcript, attached hereto as Exhibit 10). The Panel's refusal to apply the law to this dispute mandates that the Award be vacated.

B. Jurisdiction and Venue

Jurisdiction and venue are proper in this Court because this Federal Court has independent grounds to exercise original subject matter jurisdiction over this claim. 28 U.S.C. §1332. Complete diversity exists between the parties and the amount in controversy exceeds $75,000.00, exclusive of interest and costs. Personal jurisdiction exists over Westchester

[4] Westchester's Motion for Summary Determination and exhibits is attached hereto as Exhibit 6. Raybestos' Memorandum in Opposition to Westchester's Motion for Summary Determination is attached hereto as Exhibit 7. Westchester Memorandum in Opposition to Raybestos' Motion for Summary Determination is attached hereto as Exhibit 8. Raybestos' Memorandum in Reply to Westchester's Responsive Brief is attached hereto as Exhibit 9.

[5] Westchester, Raybestos and Raytech entered into a Stipulated Award which makes the final Arbitration Award applicable to Raytech as if Raytech were a party to the underlying Arbitration. The Stipulated Award is attached hereto as Exhibit 10.

[6] As previously noted, this case has been settled with USF&G and National Union.

because it provided liability insurance coverage for Raybestos' facility located in Crawfordsville, Indiana. Venue is proper in this judicial district under 28 U.S.C. § 1391 (a) and (c) because Westchester is deemed to reside in this judicial district.

Because this particular Court had original subject matter jurisdiction over this case, and a declaratory judgment action was filed before this Court in January of 1997, this Court now has "continuing jurisdiction to review the award as it relates to [the declaratory judgment] proceeding." Lefkowitz v. Wagner, 291 F. Supp. 2d 764, 768 (N.D. Ill. 2003). Once a court obtains jurisdiction in an action and enters an order compelling arbitration, that court retains jurisdiction with respect to subsequent motions related to the arbitration including motions to confirm or vacate any award or determination. Amgen, Inc. v. Kidney Ctr. of Delaware County, Ltd., 95 F.3d 562 (7th Cir. 1996); American Patriot Ins. Agency, Inc. v. Mutual Risk Mgt. Ltd., 364 F.3d 884 (7th Cir. 2004).

II. LEGAL STANDARD

Arbitration awards can be vacated or modified pursuant to specific statutory grounds. In addition, two judicially created grounds exist to allow a court to vacate an award: (1) where the award is in manifest disregard of the law; and (2) where the award violates public policy. Huntington Hospital v. Huntington Hospital Nurses Assoc., 302 F. Supp. 2d 34 (E.D.N.Y. 2004).

A. The Panel Acted in Manifest Disregard of the Law.

Manifest disregard of the law is a common law ground to vacate an arbitration award. In order for this Court to vacate the Award on this basis, Raybestos must show that "(1) the arbitrator knew of a governing legal principle yet refused to apply it or ignored it altogether, and (2) the law ignored by the arbitrator was well-defined, explicit and clearly applicable to the

case." Health Servs. Mgmt. Corp. v. Hughes, 975 F.2d 1253, 1267 (7th Cir. 1992). See also, Koveleskie v. SBC Capital Mkts., Inc., 167 F.3d 361 (7th Cir.), cert denied, 528 U.S. 811 (1999).

The Panel was required to apply substantive law to the underlying dispute in reaching its decision. If substantive law is improperly interpreted, or the Panel reaches a decision that a court may not have reached, an award would likely not be vacated. However, this Panel never got that far. It recognized the law, recognized that it was the governing legal principle, recognized that it was well-defined, explicit and clearly applicable to the case, and then ignored it altogether. Instead the Panel relied on its "collective judgment" to reach the decision. The Panel was wrong and the Award must be vacated.

1. Arbitrators Must Apply Substantive Law

Federal courts interpreting the FAA have imposed a duty upon arbitrators to follow substantive law. Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 232 (1987); see also Livingston v. Assoc. Fin., Inc., 339 F.3d 553 (7th Cir. 2003); Koveleskie v. SBC Capital Markets, Inc., 167 F.3d 361 (7th Cir. 1999). The United States Supreme Court has held that when parties agree to arbitrate disputes, they do not relinquish their substantive rights under statutes or laws; they merely designate an arbitral, rather than a judicial forum for resolution of their claims. See Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991); see also Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985). Parties who agree to arbitrate have "no reason to assume at the outset that arbitrators will not follow the law; or comply with the requirements of the statute." Shearson, 428 U.S. at 232.

Substantive law cannot be disregarded in arbitration, and courts will not enforce arbitration awards that demonstrate a manifest disregard of the applicable law. National Wrecking Co. v. Int'l Broth. of Teamsters, Local 731, 990 F.2d 957, 961 (7th Cir. 1993), citing

Health Services Mgt. Corp. v. Hughes, 975 F.2d 1253, 1267 (7th Cir. 1992). If arbitrators are free to disregard the applicable law in favor of a "just and equitable" standard, this doctrine would not exist. Arbitrators cannot craft "just and equitable" awards that contravene the law. See School City of East Chicago v. East Chicago Found. of Teachers, 422 N.E.2d 656 (Ind.Ct.App. 1981) (Even when AAA rules apply, an arbitration award of punitive damages for a breach of contract would not be upheld in contravention of Indiana law); Country Mut. Ins. Co. v. Nat'l Bank of Decatur, 248 N.E.2d 299 (Ill.App.Ct. 1969) (Arbitration award vacated because statute of limitations had run for wrongful death claim); Liberty Mut. Ins. Co. v. Open MRI of Morris & Essex, L.P., 813 A.2d 621 (N.J. Super. Ct. Law. Div. 2002) (Arbitrator's award vacated because it violated New Jersey law). Allcity Ins. Co. v. American Home Assoc. Co., 2003 WL 21203093 (NY.Civ.CT.2003) (Arbitration award vacated because arbitrator failed to apply proper statute of limitations).

As set forth above, an arbitration award is subject to judicial review to determine if it is in manifest disregard of the law, therefore, arbitrators *must* determine the law to be applied to the proceedings. In the present case, although the Panel recognized the relevant substantive law applicable to this dispute, they found they were not bound by the law but instead were free to interpret the underlying insurance policies based on their "collective experience." The Panel stated:

> For purposes of interpreting the pollution exclusion, the proper construction of the arbitration provision permits the panel to use its collective best judgment, expertise, and experience in determining the meaning of the contract, ***without regard to the substantive laws*** of any particular jurisdiction.
>
> The panel has already concluded that it is neither bound by substantive law nor the District Court's decision [Judge Young's Memorandum and Order in the case of Reliance Insurance Co. of Illinois v. Raybestos Products Co., Cause No.: IP 97-0027-C Y/G dated January 19, 2000].

Decision, Exhibit 2 at 6. (emphasis added)

The Panel relied on the Seventh Circuit's opinion in Baravati v. Josephthal, Lyon & Ross, Inc., 28 F.3d 704 (7th Cir. 1994) to determine that they were not compelled to apply the substantive law of any particular jurisdiction, or any substantive law at all. Decision, Exhibit 2 at 4. The Panel misreads the application of Baravati. Baravati makes a clear distinction between the process by which arbitrators determine the rights of the parties on one hand, and the process by which the Panel formulates remedies on the other. When formulating remedies, the Panel is free to rely on its collective experience. However, when determining whether a party should receive an award or whether a remedy should be implemented at all, the Panel must be guided by the law and cannot merely rely on its collective judgment.

In Baravati, the court essentially held that the Panel may not ignore the well established law of defamation and decide based on its collective judgment whether an award may be issued. As to what is relevant and decisive regarding the rights of the plaintiff and defendant in a defamation action, state law controls the arbitrators' decision. After following the law, if the Panel is lead to the conclusion that an award should be made, the Panel may then use its collective judgment to fashion an appropriate award.

Similarly, the interpretation of the insurance contract by the Panel is bound by well established substantive law of Indiana. As the U.S. Supreme Court has held, "the streamlined procedures of arbitration do not entail any consequential restriction on substantive rights." Shearson, 428 U.S. at 232, citing Mitsubishi Motors. Baravati supports the application of the substantive law of Indiana.

> "It would be surprising if in authorizing the arbitration of their disputes the parties had intended the arbitrators to make up a law . . . . More likely they were expected to apply the defamation law of some state..."

Baravati, 28 F.3d at 707.

Similarly, it is expected that the Panel would apply the insurance contract law of some state, and not "make up a law." However, in manifest disregard of the law, the Panel stated:

> The Panel has already concluded that it is not required to apply the law of a particular jurisdiction to interpret the pollution exclusion, and that given our interpretation of the arbitration provision, it is not necessary to undertake a choice-of-law analysis to determine which state substantive law would apply.

Decision, Exhibit 2 at 8.

The Panel openly and deliberately disregarded the law. As far as the Panel was concerned, they were bound by nothing. The Panel was wrong. They did not interpret or apply the law incorrectly, they simply ignored the applicable law and made up their own law based on their "collective judgment." The purpose behind arbitration is for a quick and less expensive resolution of legal disputes, not to change or waive the substantive rights of the parties.

2. The Applicable Law Is Well-Defined, Explicit and Clearly Applicable

Seventh Circuit case law with respect to the manifest disregard of the law standard supports this Court's vacatur of the Award because the Panel disregarded the applicable substantive law in reaching its decision. In the Seventh Circuit, "the arbitrators must, to manifestly disregard the law and their duties, have deliberately disregarded what they knew to be the law." Holden v. Deloitte & Touche LLP, 390 F. Supp. 2d 752, 774 (N.D. Ill. 2005).

The Panel here "acknowledged that a rule of law was applicable and governed, but . . . [chose] to follow a different course. . . . Simply put, [this] case, sub judice . . . involve[s] a situation where the [Panel] has effectively repudiated the adjudicatory role and manifested that

[it] is going to simply render an award 'rooted in [its] own personal idea of industrial justice.'" Id., at *19, quoting Anheuser-Busch, Inc. v. Local Union No. 744, 280 F.3d 1133, 1144 (7th Cir. 2002).

The Panel's Award contains repeated references that it knew of the governing principles of Indiana law but chose to ignore this law – or any other law – "on a personal whim, or a subjective sense of 'street justice', or on the basis of willful or manifest disregard of the law." Holden, 390 F.Supp. 2d at 776.

The Panel clearly knew the law:

> Indiana. . . has declared the pollution exclusion ambiguous and, as a matter of law, unenforceable to bar claims arising out of a government-mandated environmental clean-ups[sic]. . . On January 19, 2000, the District court [sic] held that it was compelled to apply the choice-of-law rules of its forum, Indiana; that under those rules Indiana law applied; and that under Indiana law the pollution exclusion was ambiguous and unenforceable as a matter of law. (These conclusions were repeated by the District Court in subsequent orders entered September 27, 2000, and February 2, 2002.)

Decision, Exhibit 2 at 2.

In spite of the above statement, the Panel openly disregarded the well settled law:

> …the traditional approach of arbitrators, in the panel's collective experience, allows an arbitrator to interpret the contract ***without regard to substantive law***.

Decision, Exhibit 2 at 4 (emphasis added).

> …the arbitrators [are authorized] to determine, without a traditional choice-of-law analysis, what criteria to apply in reaching a just and equitable decision.

Decision, Exhibit 2 at 5.

> …arbitrators are free to resolve a dispute and fashion a remedy without regard to the strictures of judicial procedures and substantive law.

Decision, Exhibit 2 at 9.

The Panel's knowing, deliberate and intentional disregard of the applicable law clearly constitutes "manifest disregard of the law" and the Award must be vacated.

3. Indiana Law Should Have Been Applied

It is well settled that the interpretation of the terms of an insurance policy is a question of state contract law. Erie Ins. Group v. Sear Corp., 102 F.3d 889, 892 (7th Cir.1996) (citing Tate v. Secura Ins., 587 N.E.2d 665, 668 (Ind.1992)). The interpretation of an insurance policy is a question of law for the court, Colip v. Claire, 26 F.3d 712, 716 (7 Cir. 1994).

As previously stated, federal courts interpreting the FAA require that arbitrators follow substantive law. The AAA rules are not "substantive laws." The AAA rules are, instead, merely rules of procedure. See Discount Trophy & Co., Inc v. Plastic Dress-Up Co., 2004 WL 350477 *3 (D.Conn. 2004); Tatibouet v. Ellsworth, 54 P.3d 397, 406 n.6 (Haw. 2002). Consequently, these rules cannot determine the substantive rights of the parties. The Panel here was required to apply substantive law, and that law should have been Indiana.

This arbitration arose out of a declaratory judgment action filed in the Southern District of Indiana.[7] The Southern District of Indiana retains jurisdiction over the parties, and Westchester's Motion to Compel Arbitration was filed in the declaratory judgment action in Indiana.[8]

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[7] Pursuant to the FAA, the arbitration took place in the Southern District of Indiana.

> [Any] party aggrieved by the alleged failure, neglect or refusal of another to arbitrate under a written agreement for arbitration may petition any United States District Court which, save for such agreement, would have jurisdiction under Title 28, in a civil action … for an order directing that such arbitration proceed in the manner provided for in such agreement…. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed.

FAA, 9 U.S.C. § 4. The AAA has no office in Indiana. After the initial submission, for the convenience of the lawyers and arbitrators, the AAA directed that the hearings take place in Chicago, Illinois.

[8] Therefore, Westchester selected Indiana as the forum to arbitrate in. It could have moved to compel arbitration in many other federal courts that also had jurisdiction under the FAA. It did not.

The Panel was, therefore, bound by the Indiana choice of law rules.[9] Travelers Indem. Co. v. Summit Corp. of Am., 715, N.E.2d 926, 931 (Ind.Ct.App. 1999) ("Summit"); Hartford Accident & Indemnity Co. v Dana Corp., 690 N.E.2d 285, 291 (Ind.Ct.App. 1998) ("Dana"). As the U.S. Supreme Court recognized in Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995).

"If a similar contract, without a choice-of-law provision, had been signed in New York and was to be performed in New York, presumably, "the laws of the State of New York" would apply even though the contract did not expressly so state." That rule is no less applicable in the present case. Here, the arbitration clause had no choice-of-law provision. The location of Raybestos' insured risk is clearly situated in Crawfordsville, Indiana. All of the contamination and all of the remediation occurred in Indiana. Finally, the insurance proceeds will be put to use in Indiana to reimburse Raybestos for the over Twenty Three Million ($23,000,000.00) Dollars it spent to clean up Shelly Ditch and defend against the IDEM and EPA actions. All of these factors required the Panel to apply Indiana's choice-of-law rules.

As Judge Young correctly explained:

> In a situation like this—where the contract contains no choice of law provision, the parties are from different states, and the parties have negotiated without meeting in person—the place of performance is usually given controlling weight. As the Dharma [Micro Data Base Systems, Inc. v. Dharma Systems, Inc., 148 F.3d 649, 653 (7th Cir. 1998)] Court explained:
>
> > …in a case in which the contract is made as it were nowhere because the parties are in different states (or countries) and the

[9] Even if the Panel applied the choice of law principals of Illinois, Indiana law would still apply. Westchester Fire Ins. Co. v. G. Heileman Brewing Co., 321 Ill.App.3d 622, 747 N.E.2d 955 (Ill.App. 1 Dist. 2001) (in a dispute concerning a commercial general liability insurance policy ("CGL"), the court used §193 of the Restatement of Conflicts of Laws for a choice of law analysis); Employers Ins. of Wausau v. Ehlco Liquidating Trust, 309 Ill.App.3d 730, (Ill.App. 1 Dist.1999) (with respect to a CGL, §193 of the Restatement (Second) Conflicts of Laws applied); Jupiter Aluminum Corp. v. Home Ins. Co., 255 F.3d 868, 874 (7th Cir. 2000)(significant contacts analysis is used with the controlling factor in determining which state's law will apply being the location of the risk).

> contract is negotiated without a face-to-face meeting, but is entirely performed in one state, the parties will expect the law of that state to govern any contractual dispute that arises during the performance (for what other state would be a more plausible candidate?) unless they specify otherwise in the contract.
>
> Id. See also Dohm & Nelke v. Wilson Foods Corp., 531 N.E.2d 512, 514 (Ind.Ct.App. 1988) (finding the place of performance to be the dispositive factor in determining whose law to apply).

Judge Young's Order, Exhibit 3, at 13.

Judge Young correctly determined that Indiana law applied. If the Panel had engaged in a choice-of-law analysis, as it was required to do, it would have reached the same result: It would have applied Indiana substantive law to the underlying dispute. The Panel's failure to do so further illustrates their complete indifference to the applicable substantive law.

4. The Requirement that the Panel Apply Substantive Law is not Negated by the Arbitration Clause

The Supreme Court and other federal courts have recognized the distinction between issues of arbitrability, remedies, and the role of substantive law in commercial arbitration. The Supreme Court holds that when arbitration proceeds pursuant to a broad arbitration clause, the FAA, together with this broad clause, determines the power and authority of the arbitrators to determine what is arbitrable and to fashion remedies – *nothing more*. Mastrobuono, 514 U.S. at 63-64. See also Todd Shipyards Corp. v. Cunard Line, Ltd., 943 F.2d 1056, 1062 (2d Cir. 1991). The FAA's rules combined with this arbitration clause *do not* work to displace substantive law. Substantive law defines the rights and duties of the parties. Mastrobuono, 514 U.S. at 59.

The arbitration clause[10] in this case is typical and not different in any significant way from the arbitration clauses in the cases cited herein. Yet, the Panel stated that because the arbitration clause in this case fails to specify the application of specific substantive law, and incorporates the AAA rules,[11] the parties "impliedly authorized the arbitrators to determine, without a traditional choice-of-law analysis, what criteria to apply in reaching a just and equitable decision." Decision, Exhibit 2 at 5. This conclusion clearly contravenes the federal law of arbitration. See generally, Mastrobuono.

The Panel's Award demonstrates that the Panel:

1. Was aware of the law;

2. Knew the law clearly applied to the contract; and,

3. Chose to ignore the law.

Their conduct is in direct contravention to the federal law of arbitration and their failure to apply substantive law to the interpretation of insurance policies has deprived the parties of their *substantive* legal rights.

If this Court were to confirm the Panel's Award, thus accepting the Panel's invention of its own law, we are left with the inevitable result that arbitrators who make up the law as they go "will only cause parties to shun arbitration as a preferred method of dispute resolution because it will expose them to virtually [the most unpredictable and unforeseeable outcome] without any

[9] The arbitration clause in the Westchester policy provides in part:

> Should any dispute arise out of or relate to this endorsement and contract of insurance which cannot be resolved in the normal course of business with respect to the validity or interpretation of this insurance contract, or the performance of the respective obligations of the parties to this insurance contract, then, upon written demand of either party to the contract, the matter or matters upon which agreement cannot be reached shall be settled by arbitration in accordance with the rules of the American Arbitration Association, ... It is agreed that no award for punitive damages may be made in any arbitration proceedings regardless of the rules of the arbitration program selected.

[11] When the arbitration was filed, the DRI no longer provided arbitration services. Accordingly, the only arbitration program available was the AAA.

meaningful recourse from the courts." MedValUSA Health Programs v. Memberworks, Inc., 872 A.2d 423, 450 (Conn. 2005) (Zarella, J. dissenting).

5. Res Judicata and Collateral Estoppel Apply Here

The Panel was bound by the preclusive effect of Judge Young's Order in reaching its decision. Federal courts uniformly hold that arbitrators are bound by the preclusive effect of prior federal court decisions and that collateral estoppel and res judicata apply with equal force to arbitration proceedings. See, e.g., Miller v. Runyon, 77 F.3d 189, 193 (7th Cir. 1996, Posner, J.) and cases cited therein. All of the elements of collateral estoppel exist here and the decision reached by this Court should have been applied by the Panel.[12] The insurance policies issued by Westchester and Reliance contain identical pollution exclusion clauses,[13] and neither policy contains a choice of law provision. For purposes of issue preclusion, Westchester had the same interests in the arbitration as Reliance in the court proceeding. Judge Young's decision to apply Indiana law was sufficiently firm and was applicable throughout the remainder of the case, which eventually involved Westchester. Simply because Westchester arbitrated its dispute does not nullify a federal court's decision.[14]

[12] In order for collateral estoppel to apply: (1) the issue sought to be precluded must be the same as that involved in the prior action; (2) the issue must have been actually litigated; (3) the determination of the issue must have been essential to the final judgment; and (4) the party against whom estoppel is invoked must be fully represented in the prior action. In re Grand Jury Proceedings of the Specia Apr. 2002 Grand Jury, 347 F.3d 197, 201-202 (7th Cir. 2003). When these elements have been met, collateral estoppel can be used in an offensive or defensive manner. Parklane Hosiery Co., Inc. v. Shore, 439 U.S. 322 326 n.4 (1979).

[13] Compare Reliance's Brief in Support of All Coverage Issues and portions of Appendix of Exhibits, Vol. 1 (the "Reliance Brief"), Exhibit __ at 6 and Westchester policies contained in Raybestos Products Company Demand for Arbitration Under Indiana Law dated October 21, 2004, Exhibits __.

[14] Miller Brewing Co. v. Jos. Schlitz Brewing Co., 605 F.2d 990, 996 (7th Cir.1979), citing Restatement (Second) of Judgments § 41 cmt. g. stated:

> [T]he court should determine that the decision to be carried over was adequately deliberated and firm even if not final in the sense of forming a basis for a judgment already entered. This preclusion should be refused if the decision was avowedly tentative. On the other hand, that the parties were fully heard, that the court supported its decision with a reasoned opinion, that the decision was subject to appeal are factors supporting the conclusion that the decision is final for the purposes of issue preclusion.

Therefore, if this Court does not wish to re-invent the wheel and re-visit the choice of law issue, only to reach the conclusion that Indiana law applies, and under that law, the pollution exclusion is not enforceable, it may apply the prior decision of this Court. Either way, the result will be the same.

B. Indiana Law and Public Policy Forbid the Enforcement of the Pollution Exclusion.

A court may vacate an arbitration award when it violates a well-defined and dominant public policy. Even when the award is within the scope of the arbitrator's authority and "is based on the arbitrator's interpretation of the agreement, [a court] will vacate the award if it is repugnant to the established norms of public policy." Chicago Fire Fighters Union Local No. 2 v. City of Chicago, 751 N.E.2d 1169, 1175 citing American Federation of State, County & Municipal Employees v. State of Illinois, 124 Ill.2d 246, 154 (1988). In order for an award to be vacated for a violation of public policy, the court must determine "whether a well-defined and dominant public policy can be identified. If so, [the court] must then determine whether the arbitrator's award, as reflected in his interpretation of the Agreement, violated the public policy. To ascertain the existence of public policy, [the court] look[s] to [state] constitution, statutes, and relevant judicial opinions." County of DeWitt v. American Federation of State, County and Municipal Employees, Council 31, 298 Ill.App.3d 634, 637 (1998).

Questions of public policy are left to the courts, not to the arbitrators. A court cannot delegate its responsibility to protect the public interest to an arbitrator. County of DeWitt, 298 Ill.App.3d at 639.

As previously discussed in Section A3, *supra*, Indiana law should have been applied by the Panel. Under Indiana law, pollution exclusions in insurance policies are not enforceable. This has been the law in Indiana, as pronounced by its Supreme Court, at least since 1996. This

law is well-defined and established in the State. See, e.g., American States Ins. Co. v. Kiger, 662 N.E.2d 945 (Ind. 1996); Seymour Mfg. Co., Inc. v. Commercial Union Ins. Co., 665 N.E.2d 891, 892 (Ind. 1996); Freidline v. Shelby Ins. Co., 774 N.E.2d 37 (Ind. 2002). See also Travelers Indemnity Co. v. Summit Corp., 715 N.E.2d 926 (Ind.Ct.App. 1999).

The Kiger decision and its progeny make clear that pollution exclusions in insurance policies violate the public policy of Indiana. See, e.g., American States Ins. Co. v. Kiger, 662 N.E.2d 945 (Ind. 1996); Seymour Mfg. Co., Inc. v. Commercial Union Ins. Co., 665 N.E.2d 891 (Ind. 1996); Travelers Indem. Co. v. Summit Corp., 715 N.E.2d 926 (Ind.Ct.App. 1999); Hartford Accident & Indem. Co. v. Dana Corp., 690 N.E.2d 285 (Ind.Ct.App. 1997); Employers Ins. of Wausau v. Recticel Foam Corp., 716 N.E.2d 1015 (Ind.Ct.App. 1999); General Housewares v. National Sur. Corp., 741 N.E.2d 408 (Ind.Ct.App. 2000); Allstate Ins. Co. v. Dana Corp., 759 N.E.2d 1049 (Ind. 2001).

The Indiana law regarding pollution exclusions is so well recognized that the Insurance Institute of Indiana lobbied for legislation that would "attempt to repair the commercial insurance market place before the impact of two Supreme Court decisions is felt. . . . The Indiana Supreme Court in two recent decisions [Kiger and Seymour] have created serious consequences for the commercial insurance market in Indiana." As a result of this effort, legislation that codified the pollution exclusion language was drafted, but eventually vetoed by the Governor. The Governor said that the legislation "could adversely affect large and small Indiana businesses who manufacture or use products that would be considered pollutants under this bill. . . . The insurance industry can address the problem by drafting a clear and unambiguous contractual pollution exclusion." Government Interinsurance Exchange v. City of Angola, 8 F. Supp.2d 1120, 1128 n.3 (N.D. Ind. 1998).

The public policy reasons for not enforcing the pollution exclusion have been identified by the Governor of the State and adopted as part of its laws. Westchester, and the other insurance carriers, could have amended their pollution exclusion to be more specific and unambiguous, but they chose not to. The above opinions of the Indiana courts, and the Governor's pronouncements, put these insurance carriers on notice of the law of Indiana. To allow them to come forward now and argue that law does not apply to an insured risk in Indiana is a clear violation of the public policy of the State. Therefore, the Panel was obligated to follow that law, and this Court must vacate the Award that ignored the public policy.

III. CONCLUSION

For the reasons set forth herein, Raybestos respectfully requests this Court to vacate the Award.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 10th day of July, 2006, a copy of the foregoing was filed electronically. Notice of this filing will be sent to the following parties by operation of the Court's electronic filing system and by first class mail to those parties not registered to receive electronically. Parties may access this filing through the Court's system.

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