UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

RELIASTAR LIFE INSURANCE COMPANY OF NEW YORK,	)	Civil Action No. 06-cv-10186
Petitioner,	)	
-against-	)	
EMC NATIONAL LIFE COMPANY, f/k/a NATIONAL TRAVELERS LIFE COMPANY,	)	
Respondent.	)	

RESPONDENT EMC NATIONAL LIFE COMPANY'S MEMORANDUM OF LAW IN SUPPORT OF COUNTER-PETITION TO VACATE ARBITRATION AWARD AND REQUEST FOR ORAL ARGUMENT

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INTRODUCTION

This case concerns an arbitration award rendered in an arbitration between Reliastar Life Insurance Company of New York ("RLNY") and EMC National Life Company ("EMCNL"). The award should be vacated pursuant to 9 U.S.C. § 10(a)(4) because the Panel exceeded its authority in awarding attorneys' fees and expenses in direct contravention of the express agreement of the parties that they will each bear the expenses of their respective arbitrators and attorneys' fees and equally share in the expenses of the third arbitrator. EMCNL does not seek to vacate any other portion of the award and has satisfied the award in all other respects.

STATEMENT OF THE CASE

On or about December 31, 1997, National Travelers Life Insurance Company[1] ("NTL") and RLNY entered into two separate but related modified coinsurance agreements: (1) a Modified Coinsurance Agreement relating to certain RLNY Cancer Policies which were in force as of January 1, 1998; and (2) a Modified Coinsurance Agreement relating to certain RLNY Cancer Policies to be issued on or after January 1, 1998. For purposes of the Arbitration and the present action, the two coinsurance agreements contain essentially the same terms and conditions, and will be referred to collectively as the "Coinsurance Agreements." (Petition, Exs. A & B).

[1] During late 2002, NTL and Employers Modern Life Insurance Company ("EML") began negotiations which led to the 2003 merger of the two companies into a new company, EMCNL. Consequently, EMCNL is the successor in interest to NTL with respect to the reinsured Cancer Policies covered by the Coinsurance Agreements, and references to EMCNL and NTL are interchangeable, except as context otherwise requires.

The arbitration clause in the Coinsurance Agreements provides in pertinent part:

> 10.3 Expenses of Arbitration. Each party shall bear the expense of its own arbitrator (whether selected by that party, or by the other party pursuant to the procedures set out in Section 10.1) and related outside attorneys' fees, and shall jointly and equally bear with the other party the expenses of the third arbitrator.
>
> 10.4 Applicable Law. Any arbitration instituted pursuant to this Article shall be held in New York, New York, or another site mutually agreed upon by the parties and the laws of the State of New York and to the extent applicable, the Federal Arbitration Act, shall govern the interpretation and application of this Agreement.

Disputes falling within the arbitration clause of the Coinsurance Agreements arose between the parties. Because the parties were unable to resolve these disputes, EMCNL initiated arbitration proceedings ("the Arbitration") pursuant to Article X of the Coinsurance Agreements, seeking a declaration that the Coinsurance Agreements had been terminated and also requesting resolution of certain issues underlying the method and manner in which the terminal accounting would be conducted. RLNY asserted that the Coinsurance Agreements had not been properly terminated and therefore remained in force, and alternatively requested the Arbitration Panel order the terminal accounting to proceed under a different method and manner more favorable to RLNY than that proposed by EMCNL.[2]

[2] The reinsured block of cancer policies had become unprofitable following NTL's 2002 Notice of Termination, whether because of RLNY's mismanagement (as asserted by NTL), or because of market forces for that type of policy (as asserted by RLNY), or some combination of those factors. Because the reinsured block of cancer policies was unprofitable, it was RLNY's position that NTL should share in the losses, whether as an ongoing partner or through the terminal accounting process.

Following discovery, a two week arbitration hearing was held in May 2006. The Arbitration Panel entered an Interim Award (Petition, Ex. C) on August 4, 2006, essentially finding that the Coinsurance Agreements remained in force. The Panel awarded RLNY past due monthly settlements under the Coinsurance Agreements, directed the parties to meet and confer to resolve issues related to resumption of the ongoing relationship under the Coinsurance Agreements (EMCNL's 95% share of losses), and also awarded RLNY its attorneys' fees and arbitration costs.

On August 30, 2006, EMCNL paid in full the $21,960,692 plus interest awarded in Paragraph 2 of the Interim Award for past due monthly settlements. Thereafter, the parties met, pursuant to the Panel's order, to try to reach an agreement on the remaining issues set forth in the Interim Award. The parties were able to reach a settlement of all outstanding disputes and issues regarding the current and future relationship between the parties, with the exception of the amount of attorneys' fees and arbitration costs. (See Ex. 1 to the Declaration of Denny M. Dennis submitted with this memorandum ("Dennis Declaration")). Consequently, the issues addressed by Paragraphs 1-5 of the Interim Award were resolved by the settlement agreement.

The parties were unable to reach agreement, however, with respect to the Panel's majority decision to award to RLNY its attorneys' fees and arbitration costs as set forth in the sixth (unnumbered) paragraph of the Interim Award. The parties specifically excepted this issue from the settlement and commutation encompassing the other disputes between the parties. (Dennis Declaration, Ex. 1, p. 2). The parties agreed to resubmit the attorneys' fees and arbitration costs issue to the Panel, subject to EMCNL's reservation

of the right to challenge the award of such relief in court. (Dennis Declaration, Ex. 2, at para. 4). After subsequent briefing on the attorneys' fees and arbitration costs issue, the Panel entered a Final Award (Petition, Ex. D) on October 20, 2006, in which a majority of the Panel again awarded RLNY its attorneys' fees and arbitration costs, together with interest "at the prime rate plus the New York statutory rate, 9%" and compounded monthly. RLNY then filed a Petition in this Court to confirm the Final Award of attorneys' fees and arbitration costs, and EMCNL filed a Counter-Petition to vacate the Final Award, insofar as it awarded RLNY attorneys' fees and arbitration costs

ARGUMENT

I. The Arbitration Panel exceeded its authority in awarding attorneys' fees and arbitration costs.

An arbitration award should be set aside where the Arbitration Panel exceeded its powers. 9 U.S.C. § 10(a)(4). In making this determination, the Court's inquiry focuses on whether the arbitrators had the power based upon the arbitration agreement to reach a certain issue. *Banco de Seguros del Estado v. Mutual Marine Office Inc.*, 344 F.3d 255, 262 (2d Cir. 2003). As noted above, the arbitration clause provides that each party will bear its own attorneys' fees and the expenses of its arbitrator and shall "jointly and equally bear with the other party the expenses of the third arbitrator." Further, the Coinsurance Agreements also stipulate: "the laws of the State of New York and to the extent applicable, the Federal Arbitration Act, shall govern the interpretation and application of this Agreement." (Petition, Exs. A & B, at § 10.4).

Throughout the Arbitration, EMCNL consistently asserted that the Panel lacked authority under the Coinsurance Agreements to award either party attorneys' fees or arbitration costs. Despite EMCNL's arguments, however, in its Interim Award, a majority of the Panel ruled that EMCNL "shall pay to RLNY its attorney fees and costs, including but not limited to arbitrator fees, expert fees, travel and lodging, vendor expenses and court reporter fees, incurred in this action." (Petition, Ex. C, sixth unnumbered para.).

The parties then submitted additional briefs to the Panel on the issues of whether the Coinsurance Agreements permitted such an award, and if so, whether the amounts claimed by RLNY were reasonable. The submission preserved EMCNL's right to challenge the award of attorneys' fees and costs in court. (Dennis Declaration, Ex. 1, p. 2; Ex. 2, para. 4). In this regard, it is undisputed that EMCNL has not waived and has expressly reserved its right to maintain this action seeking to vacate the award of attorneys' fees and costs. (*Id.*). A majority of the Panel then entered its Final Award, which stated in relevant part:

> 4. Pursuant to the sixth (unnumbered) paragraph in the Interim Award, the majority of the Panel, because it views the conduct of Petitioner as lacking good faith, orders NTL to pay RLNY $3,169,496 in attorney and arbitrator fees, including a reduction from the total fees by $3,264.00 in travel related expenses of the umpire in connection with the hearing, and $691,903.75 in costs, plus interest at the prime rate accrued from the date of payment by RLNY of each such fee and cost compounded monthly, until the date of payment. In the event that such amount is not paid within 20 business days, interest shall accrue at the prime rate plus the New York statutory rate, 9%, until the date of payment.

(Petition, Ex. D, para. 4).

The Panel did not have the authority to award attorneys' fees and costs associated with the Arbitration. The language of the Coinsurance Agreements is clear and unambiguous. The Coinsurance Agreements require each party to bear its own attorneys' fees, arbitrator expenses, and related costs in any arbitration. The Coinsurance Agreements do *not* provide for any exceptions, including any of those advocated by RLNY before the Arbitration Panel (or likely before this Court).

In evaluating whether the Arbitration Panel's award of attorneys' fees and related costs exceeded its authority, this Court must begin by noting that the underlying arbitration is governed by the Federal Arbitration Act (FAA). The United States Supreme Court has consistently stated that the central principle underpinning the FAA is the concept that the parties to any contract with an arbitration clause can agree as to what issues can be submitted for resolution, and on what terms:

> Arbitration under the Act [the FAA] is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit. Just as they may limit by contract the issues which they will arbitrate, so too may they specify by contract the rules under which that arbitration will be conducted.

Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford, 489 U.S. 468, 479, 109 S. Ct. 1248, 1256 (1989) (citation omitted); *accord Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627-28, 105 S. Ct. 3346, 3354-55 (1985) ("Thus, as with any other contract, the parties' intentions control…." and "Nothing, in the meantime, prevents a party from excluding statutory claims from the scope of an

agreement to arbitrate."). Here, where the parties specifically agreed in the Coinsurance Agreements to exclude awards of attorneys' fees and costs, the Arbitration Panel was bound by that agreement. Consequently, the Panel's contrary award of attorneys' fees and costs exceeded its authority, and the award must be vacated under 9 U.S.C. 10(a)(4).

RLNY also argued to the Panel that attorneys' fees and costs should be awarded because of what it claims was "bad faith" and "frivolous" conduct by EMCNL in pursuing the Arbitration; the Panel majority apparently relied upon this argument by making an explicit reference to "bad faith" in its Final Award. The arbitration clause's allocation of responsibility for attorneys' fees and costs, however, does not provide for any exceptions. Further, RLNY's argument to the Panel on this point was based on a misinterpretation of and improper reliance on one case, *Mighty Midgets v. Centennial Insurance Co.*, 47 N.Y.2d 12, 416 N.Y.S.2d 559, 389 N.E.2d 1080 (N.Y. 1979). In *Mighty Midgets*, the court overturned an award of attorney fees in a declaratory judgment action brought by an insured policyholder against its liability insurer seeking to compel coverage for a claim. 389 N.E.2d at 1085. The court did mention, in passing, that the case was distinguishable from cases where attorney fee awards had been affirmed:

> It is the rule in New York that such a recovery [of attorney fees] may not be had in an affirmative action brought by an assured to settle its rights, but only when he has been cast in a defensive posture by the legal steps an insurer takes in an effort to free itself from its policy obligations.

Id. (citations omitted).

RLNY suggested to the Panel that *Mighty Midgets* supported an award of attorneys' fees by equating the Coinsurance Agreements to a typical insurer-insured

relationship, rather than recognizing the fundamentally different relationship inherent in a reinsurer-insurer relationship, which is more akin to a business partnership than an actual insurance contract. In any event, RLNY's reliance on *Mighty Midgets* in its arguments before the Panel was misplaced; the New York courts have limited *Mighty Midgets* to situations where a "duty to defend" clause is invoked (as was present in *Mighty Midgets*), which is not the case in the present arbitration. *Employers Mutual Cas. Co. v. Key Pharmaceuticals, Inc.*, 871 F. Supp. 657, 674 (S.D.N.Y. 1994), *aff'd* 75 F.3d 815, 824 (2d Cir. 1996) (excess insurer attempted to avoid contribution to settlement of tort claim by pursuing declaratory judgment action; although insurer lost on the merits, district court and court of appeals each held that *Mighty Midgets* did not apply and attorneys' fees could not be awarded). In fact, a New York court has specifically held that *Mighty Midgets* did not apply to a reinsurance dispute where a reinsurer unsuccessfully attempted to avoid its obligation to indemnify its cedant insurer. *Folksamerica Reinsurance Co. v. Republic Ins. Co.*, 2004 WL 2423539, No. 03-Civ.-0402 (S.D.N.Y. 2004) (unreported) ("Absent a clear indication of a "duty to defend" clause in Republic's reinsurance contract, under the *Mighty Midgets* exception and its progeny, attorneys' fees cannot be awarded.").

In other words, the New York courts still require an express contractual agreement to permit an award of attorneys' fees, even under *Mighty Midgets*. Here, where the express contractual language bars such awards, *Mighty Midgets* provided the Panel with no authority to enter an award of attorneys' fees and costs.

Moreover, had the parties intended to incorporate a "bad faith" exception into their agreement regarding attorneys' fees and expenses, they clearly could have done so. They obviously chose not to include any such exception, and thus the Panel exceeded its authority in basing its award on this exception.

CONCLUSION

The arbitration agreement at issue expressly bars an award of attorneys' fees and expenses in any arbitration proceeding. The FAA requires full enforcement of the parties' contractual agreements related to arbitration issues. Consequently, the Arbitration Panel's award of attorneys' fees and expenses exceeded its authority and was unsupported by any contractual or legal authority. Therefore, this Court must vacate the Panel's award of attorneys' fees and expenses.

REQUEST FOR ORAL ARGUMENT

Respondent EMCNL requests the opportunity to be heard by the Court in oral argument.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true copy of the foregoing instrument was served upon one of the attorneys of record for all parties to the above-entitled cause by serving the same on such attorney at his/her respective address/fax number as disclosed by the pleadings of record herein, on the ____ day of _____, 2007 by:

☐ U.S. Mail ☐ FAX
☐ Hand Delivered ☐ UPS
☐ Federal Express ☐ Other_____