2018 IL App (4th) 180240-U

NO. 4-18-0240

IN THE APPELLATE COURT

OF ILLINOIS

FOURTH DISTRICT

FILED
September 10, 2018
Carla Bender
4th District Appellate
Court, IL

ONKEN'S AMERICAN RECYCLERS, INC. f/k/a OIL FILTER RECYCLERS, INC. and OAR TRUCKING, INC. f/k/a OFR TRUCKING, INC.,	)	Appeal from the Circuit Court of Mason County No. 16L8
Plaintiffs-Appellees, v. CALIFORNIA INSURANCE COMPANY, CONTINENTAL INDEMNITY COMPANY, APPLIED UNDERWRITERS CAPTIVE RISK ASSURANCE COMPANY, INC., APPLIED UNDERWRITERS, INC., and APPLIED RISK SERVICES, INC.,	)	
Defendants-Appellants, and CLEMENS & ASSOCIATES, INC.,	)	Honorable Michael L. Atterberry, Judge Presiding.
Defendants.	)	

JUSTICE DeARMOND delivered the judgment of the court.
Presiding Justice Harris and Justice Steigmann concurred in the judgment.

ORDER

¶ 1 *Held*: The appellate court affirmed the trial court's judgment, finding the court did not err in granting summary judgment in favor of plaintiffs and denying appellants' motion to compel arbitration.

¶ 2 In December 2016, plaintiffs, Onken's American Recyclers, Inc. and OAR Trucking, Inc., filed a complaint against defendants, California Insurance Company, Continental Indemnity Company, Applied Underwriters Captive Risk Assurance Company, Inc., Applied Underwriters, Inc. (Applied Underwriters), Applied Risk Services, Inc. (collectively, the Applied

defendants), and Clemens & Associates, Inc. (Clemens), relating to workers' compensation and employer's liability insurance policies. The Applied defendants demanded arbitration and then moved to compel arbitration. Both parties filed motions for summary judgment. In March 2018, the trial court granted summary judgment in favor of plaintiffs and denied the Applied defendants' motion to compel arbitration.

¶ 3 In this interlocutory appeal, the Applied defendants argue the trial court erred in (1) holding further proceedings in light of plaintiffs' failure to challenge specific provisions of the parties' agreement and (2) applying Nebraska law to invalidate the arbitration provision in the agreement. We affirm.

¶ 4 I. BACKGROUND

¶ 5 In early 2012, plaintiffs sought to purchase workers' compensation insurance with an effective date of April 15, 2012. At that time, plaintiffs were advised by their insurance broker, Clemens, that, due to a prior loss, they had limited options as to insurance providers for their workers' compensation coverage. Clemens advised plaintiffs they could obtain the coverage from the residual market or through the EquityComp program offered by the Applied defendants.

¶ 6 Clemens explained that, to obtain the guaranteed-cost workers' compensation and employer's liability policies the Applied defendants offered under the EquityComp program, plaintiffs would also have to agree to enter into a reinsurance participation agreement (reinsurance agreement), which was a mechanism where the parties would share premiums paid for and losses arising from the guaranteed-cost workers' compensation and employer's liability policies. Plaintiffs entered into two reinsurance agreements, the first in 2012 and the second in 2015.

¶ 7 The dispute resolution clause in section 13 of the 2012 reinsurance agreement provides, in part, as follows:

> "(A) It is the express intention of the parties to resolve any disputes arising under this Agreement without resort to litigation in order to protect the confidentiality of their relationship and their respective businesses and affairs. Any dispute or controversy that is not resolved informally pursuant to sub-paragraph (B) of Paragraph 13 arising out of or related to this Agreement shall be fully determined in the British Virgin Islands under the provisions of the American Arbitration Association.
>
> (B) All disputes between the parties relating in any way to (1) the execution and delivery, construction or enforceability of this Agreement, (2) the management or operations of the Company, or (3) any other breach or claimed breach of this Agreement or the transactions contemplated herein shall be settled amicably by good faith discussion among all of the parties hereto, and, failing such amicable settlement, finally determined exclusively by binding arbitration in accordance with the procedures provided herein. The reference to this arbitration clause in any specific provision of this Agreement is for emphasis only, and is not intended to limit the scope, extent or intent of this arbitration clause, or to mean that any other provision of this Agreement shall not be fully subject to the terms of this arbitration

clause. All disputes with respect to any provision of this Agreement shall be fully subject to the terms of this arbitration clause.

* * *

(G) *** Judgment upon the award rendered by the arbitrator or arbitrators may be entered by any court of competent jurisdiction in Nebraska or application may be made in such court for judicial acceptance of the award and an order of enforcement as the law of Nebraska may require or allow."

* * *

(I) All arbitration proceedings shall be conducted in the English language in accordance with the rules of the American Arbitration Association and shall take place in Tortola, British Virgin Islands or at some other location agreed to by the parties.

* * *

(L) Punitive damages will not be awarded. The arbitrator(s) may, however, in their discretion award such other costs and expenses as they deem appropriate, including, but not limited to, attorneys' fees, the costs of arbitration and arbitrators' fees.

(M) Participant acknowledges and agrees that it will benefit from this Agreement and that a breach of the covenants herein would cause Company irreparable damages that could not

> adequately be compensated by monetary compensation. Accordingly, it is understood and agreed that in the event of any such breach or threatened breach, Company may apply to a court of competent jurisdiction for, and shall be entitled to, injunctive relief from such court, without the requirement of posting a bond or proof of damages, designed to cure existing breaches and to prevent a future occurrence or threatened future occurrence of like breaches on the part of the Participant. It is further understood and agreed that the remedies and recourses herein provided shall be in addition to, and not in lieu of any other remedy or recourse which is available to Company either at law or in equity in the absence of this Paragraph including without limitation the right to damages."

The Applied defendants refer to section 13(B) and 13(I) as delegation provisions. The 2012 reinsurance agreement also contains a choice-of-law provision, stating it "shall be exclusively governed by and construed in accordance with the laws of Nebraska and any matter concerning this Agreement that is not subject to the dispute resolution provisions of Paragraph 13 hereof shall be resolved exclusively by the courts of Nebraska without reference to its conflict of laws."

¶ 8 In December 2016, plaintiffs filed a complaint against defendants, alleging (1) violations of the Consumer Fraud and Deceptive Business Practices Act (815 ILCS 505/1 to 12 (West 2016)), (2) violations of the Uniform Deceptive Trade Practices Act (815 ILCS 510/1 to 7 (West 2016)), (3) fraud in the inducement, and (4) rescission based on procedural and substantive unconscionability.

¶ 9 Plaintiffs alleged the Applied defendants fraudulently induced them to purchase

eight insurance policies on the basis of deceptive marketing materials and insurance proposals that promised a "no claims cost" price for such insurance that the Applied defendants never intended to honor.

¶ 10 Plaintiffs claimed they entered into two reinsurance agreements with the Applied defendants, both of which were procured by and placed through Clemens. The first reinsurance agreement was effective for the three-year term beginning April 15, 2012, and running through April 15, 2015. The second reinsurance agreement was effective for a three-year term beginning April 15, 2015. According to plaintiffs, the Applied defendants conditioned their agreement to provide the coverage afforded by the guaranteed-cost policies on plaintiffs' agreement to the nonnegotiable terms of the applicable reinsurance agreement. The reinsurance agreements modified multiple terms of the guaranteed-cost policies, including, but not limited to, the premium that plaintiffs were to pay in consideration for the coverage provided. Plaintiffs alleged the Applied defendants relied on the terms of the reinsurance agreements to bill and collect monies from plaintiffs significantly in excess of the amounts represented in its marketing materials and proposals as the "no claims cost," notwithstanding plaintiffs did not make any claims for recovery under any insurance policy issued to them by the Applied defendants.

¶ 11 Plaintiffs claimed the proposal the Applied defendants provided for the reinsurance agreement corresponding to the six guaranteed-cost policies that plaintiffs purchased for the three successive one-year periods beginning on April 15, 2012, and ending on April 15, 2015, stated, absent any claims, the cost of that insurance would be $536,358. Plaintiffs have paid approximately $1.3 million and have been billed for another approximately $290,000 in relation to those six insurance policies.

¶ 12 In January 2017, Applied Underwriters served the American Arbitration

Association and plaintiffs with its demand for arbitration against plaintiffs, claiming $290,862 allegedly due under the EquityComp program. Plaintiffs refused to arbitrate, and the parties agreed to hold the arbitration in abeyance pending the resolution of motion practice regarding the reinsurance agreements.

¶ 13 In February 2017, plaintiffs moved to stay the pending arbitration under section 2(b) of the Illinois Uniform Arbitration Act (Illinois Arbitration Act) (710 ILCS 5/2(b) (West 2016)), arguing no valid agreement to arbitrate existed between the parties because the arbitration provision found in the 2012 reinsurance agreement was procedurally and substantively unconscionable. The Applied defendants filed a motion to compel arbitration under the Federal Arbitration Act (9 U.S.C. § 1 *et seq.* (2012)), arguing the delegation clause in the 2012 reinsurance agreement required any challenge to the enforceability or scope of the arbitration go first to the arbitrator.

¶ 14 The trial court conducted a hearing on the motion to compel in June 2017. Plaintiffs' attorney asserted the hearing centered on three issues: (1) whether the Federal or Illinois Arbitration Acts applied, (2) whether the arbitration provision in the reinsurance agreement delegated questions of the arbitrability and validity of that provision to the arbitrators or the courts, and (3) whether the arbitration provision was invalid due to procedural and substantive unconscionability. During arguments, the court first asked whether plaintiffs challenged the delegation provision and, if they did, the court would then determine the validity of the agreement. Counsel for the Applied defendants argued plaintiffs failed to "challenge the delegation clause specifically and directly." Plaintiffs' counsel disagreed, arguing he "challenged the validity and unconscionability of the delegation clause itself."

¶ 15 In its September 1, 2017, order, the trial court found the 2012 reinsurance

agreement contained an arbitration provision, which included a delegation clause, and concluded plaintiffs adequately challenged that clause. The court stated it would hold an evidentiary hearing to determine "the validity and enforceability of the delegation provisions and arbitration clause" in the 2012 reinsurance agreement.

¶ 16 That same month, the Applied defendants filed a motion for summary judgment compelling arbitration because no genuine issue of material fact existed as to the validity and enforceability of the delegation clause and the arbitration provision in the 2012 reinsurance agreement. Plaintiffs filed a cross-motion for summary judgment contending the arbitration provision and the delegation clause found in the 2012 reinsurance agreement were both procedurally and substantively unconscionable.

¶ 17 On November 29, 2017, plaintiffs filed a reply in support of their cross-motion for summary judgment, arguing the arbitration provision and the delegation clause contained in the 2012 reinsurance agreement were procedurally and substantively unconscionable and invalid under Nebraska law. Plaintiffs relied on *Citizens of Humanity v. Applied Underwriters, Inc.* (*Citizens I*), 226 Cal. Rptr. 3d 1 (Cal. Ct. App. 2017), a decision of the California court of appeal that had been decided on November 22, 2017. There, the court ruled an arbitration provision in a reinsurance agreement that Applied Underwriters issued to another EquityComp insured, which contained language identical to the language found in paragraph 13(B) of the arbitration provision in this case, was unenforceable under section 25-2602.01(f)(4) of the Nebraska Uniform Arbitration Act (Nebraska Arbitration Act) (Neb. Rev. Stat. § 25-2602.01(f)(4) (2016)). The trial court asked for additional briefing on the *Citizens I* decision.

¶ 18 The Applied defendants responded, arguing the Nebraska Arbitration Act did not apply to the 2012 reinsurance agreement and *Citizens I* was wrongly decided. The Applied

defendants argued (1) the Federal Arbitration Act governed the arbitration provision and the delegation clause; (2) the Nebraska Arbitration Act did not apply to conduct outside Nebraska and the Federal Arbitration Act preempted application of the Nebraska Arbitration Act in this case; and (3) even if the Nebraska Arbitration Act applied, it would not apply to the arbitration provision and the delegation clause because the 2012 reinsurance agreement was not an agreement concerning or relating to an insurance policy.

¶ 19 In their response, plaintiffs raised the December 5, 2017, decision in *Milmar Food Group II, LLC v. Applied Underwriters, Inc.*, 68 N.Y.S.3d 645, 58 Misc. 3d 497 (N.Y. Sup. Ct. 2017), which ruled an arbitration provision in a reinsurance agreement that Applied Underwriters had issued to an EquityComp insured, containing language identical to that found in paragraph 13(B) of the arbitration provision in this case, was unenforceable under the Nebraska Arbitration Act. Plaintiffs argued the plain language of the 2012 reinsurance agreement made it clear that the Nebraska choice-of-law provision applies to the agreement in its entirety, including the arbitration provision. Further, the relevant provision of the Nebraska Arbitration Act reverse preempted the Federal Arbitration Act pursuant to the McCarran-Ferguson Act (15 U.S.C. §§ 1011 to 1015 (2012)) because it regulates the business of insurance. As the 2012 reinsurance agreement was an agreement concerning or relating to an insurance policy, plaintiffs argued the arbitration provision, and the delegation clause contained within it, were invalid pursuant to the Nebraska Arbitration Act.

¶ 20 In March 2018, the trial court held a hearing on the motions for summary judgment. Plaintiffs asked the court to hold the arbitration provision and the delegation clause found in the 2012 reinsurance agreement invalid as a matter of law because Nebraska law applied to the contract. The Applied defendants argued plaintiffs waived their argument by

raising it "at the eleventh hour." The court found nothing foreclosed plaintiffs from arguing the applicability of Nebraska law to void the arbitration provision and the delegation clause in the 2012 reinsurance agreement.

¶ 21 In ruling on the summary judgment motions, the trial court stated it had to construe and interpret the validity and enforceability of the delegation clause and the arbitration provision in the 2012 reinsurance agreement. In doing so, the court first considered whether the McCarran-Ferguson Act reverse preempted the Federal Arbitration Act. The court found the Nebraska Arbitration Act was enacted for the purpose of regulating the business of insurance and, if the Federal Arbitration Act were to be applied in this case, it would operate to invalidate or impair the Nebraska Arbitration Act. Thus, the court found the Nebraska Arbitration Act applied in this case, and the combination of that law and the McCarran-Ferguson Act reverse preempted the application of the Federal Arbitration Act.

¶ 22 In considering the Applied defendants' argument that a state may not regulate activities carried on beyond its borders, the trial court found the Nebraska Arbitration Act did not do so and, moreover, it applied because the parties contractually agreed to its applications. The court also found the arbitration provision in the reinsurance agreement was invalid and unenforceable under the Nebraska Arbitration Act, which provided that any agreement concerning or relating to insurance, other than a contract between insurance companies, may not be subject to arbitration. Thus, the court granted summary judgment in favor of plaintiffs and denied defendants' motion to compel arbitration.

¶ 23 The Applied defendants filed this interlocutory appeal pursuant to Illinois Supreme Court Rule 307(a)(1) (eff. Nov. 1, 2017). See *Equistar Chemicals, LP v. Hartford Steam Boiler Inspection & Insurance Co. of Connecticut*, 379 Ill. App. 3d 771, 774, 883 N.E.2d

740, 744 (2008) (noting "[a] motion to compel or stay arbitration is analogous to a motion for injunctive relief and therefore is subject to an interlocutory appeal").

¶ 24 II. ANALYSIS

¶ 25 A. Jurisdiction

¶ 26 Initially, plaintiffs contend this court lacks jurisdiction to review the trial court's September 1, 2017, order, where it stated it would hold an evidentiary hearing to determine "the validity and enforceability of the delegation provisions and arbitration clause" in the 2012 reinsurance agreement. We disagree. "Rule 307 allows this court to review any prior error that bears directly upon the question of whether an order on appeal was proper." *Glazer's Distributors of Illinois, Inc. v. NWS-Illinois, LLC*, 376 Ill. App. 3d 411, 420, 876 N.E.2d 203, 211 (2007). In the case *sub judice*, the court did not rule on the validity or enforceability of the arbitration or delegation provisions in the September 1, 2017, order, but it set an evidentiary hearing on the issue. It then ruled on the motion to compel arbitration in March 2018, the order from which the Applied defendants timely appealed. Thus, we have jurisdiction.

¶ 27 B. Standard of Review

¶ 28 The interpretation of an arbitration agreement is a question of contract law, which we review *de novo*. *Carr v. Gateway, Inc.*, 241 Ill. 2d 15, 20, 944 N.E.2d 327, 329 (2011). A trial court's decision on a choice-of-law issue is also subject to *de novo* review. *Bridgeview Health Care Center, Ltd. v. State Farm Fire & Casualty Co.*, 2014 IL 116389, ¶ 14, 10 N.E.3d 902. However, whether a trial court erred in choosing not to find a party waived an argument is reviewed under the abuse-of-discretion standard. *Kovera v. Envirite of Illinois, Inc.*, 2015 IL App (1st) 133049, ¶ 47, 26 N.E.3d 936; see also *Hanley v. City of Chicago*, 343 Ill. App. 3d 49, 54, 795 N.E.2d 808, 813 (2003) (applying the abuse-of-discretion standard to the trial court's

decision to allow the defendant to raise an affirmative defense for the first time in a summary judgment motion). "An abuse of discretion occurs only when the trial court's decision is arbitrary, fanciful, or unreasonable or where no reasonable person would take the view adopted by the trial court." *Seymour v. Collins*, 2015 IL 118432, ¶ 41, 39 N.E.3d 961.

¶ 29 C. Plaintiffs' Challenge to the Delegation Clause

¶ 30 The Applied defendants argue the trial court was required to compel arbitration because plaintiffs failed to specifically and directly challenge the delegation clause. We disagree.

¶ 31 "An agreement to submit to arbitration is a matter of contract." *Country Preferred Insurance Co. v. Whitehead*, 2012 IL 113365, ¶ 29, 979 N.E.2d 35. Our supreme court has found the parties' decision to arbitrate has been "regarded as an effective, expeditious, and cost-efficient method of dispute resolution." *Salsitz v. Kreiss*, 198 Ill. 2d 1, 13, 761 N.E.2d 724, 731 (2001). When parties have agreed to arbitration, challenges to the validity of the underlying contract are for the arbitrator to decide. *Preston v. Ferrer*, 552 U.S. 346, 353 (2008); *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 446 (2006). Challenges to the validity of the arbitration clause itself, however, are generally matters for the court to decide in the first instance. *Rent-A-Center, West, Inc. v. Jackson*, 561 U.S. 63, 71 (2010).

¶ 32 As noted, the Applied defendants refer to section 13(B) of the 2012 reinsurance agreement as one of the delegation clauses, and it states as follows:

> "(B) All disputes between the parties relating in any way to (1) the execution and delivery, construction or enforceability of this Agreement, (2) the management or operations of the Company, or (3) any other breach or claimed breach of this

> Agreement or the transactions contemplated herein shall be settled amicably by good faith discussion among all of the parties hereto, and, failing such amicable settlement, finally determined exclusively by binding arbitration in accordance with the procedures provided herein. The reference to this arbitration clause in any specific provision of this Agreement is for emphasis only, and is not intended to limit the scope, extent or intent of this arbitration clause, or to mean that any other provision of this Agreement shall not be fully subject to the terms of this arbitration clause. All disputes with respect to any provision of this Agreement shall be fully subject to the terms of this arbitration clause."

¶ 33 In arguing the delegation clause precluded judicial determination of arbitrability in this case, the Applied defendants rely, in large part, on the United States Supreme Court's decision in *Rent-A-Center*. In that case, the Supreme Court stated a "delegation provision is an agreement to arbitrate threshold issues concerning the arbitration agreement," and "parties can agree to arbitrate 'gateway' questions of 'arbitrability,' such as whether the parties have agreed to arbitrate or whether their agreement covers a particular controversy." *Rent-A-Center*, 561 U.S. at 68-69.

¶ 34 The Supreme Court noted a party may raise two types of challenges to the validity of the contract under federal law: "the agreement to arbitrate and the contract as a whole." *Rent-A-Center*, 561 U.S. at 70. "[O]nly the first type of challenge is relevant to a court's determination whether the arbitration agreement at issue is enforceable" because "a party's

challenge to another provision of the contract, or to the contract as a whole, does not prevent a court from enforcing a specific agreement to arbitrate." *Rent-A-Center*, 561 U.S. at 70-71.

¶ 35 The provision at issue in *Rent-A-Center* was a delegation "provision that gave the arbitrator 'exclusive authority to resolve any dispute relating to the … enforceability … of this Agreement.' " *Rent-A-Center*, 561 U.S. at 71. The respondent "challenged only the validity of the contract as a whole" and did not mention the delegation provision. *Rent-A-Center*, 561 U.S. at 72. In the district court, the respondent argued "the 'entire agreement' favors Rent-A-Center and that the limitations on discovery further his 'contention that the arbitration agreement as a whole is substantively unconscionable.' [Citation.]" *Rent-A-Center*, 561 U.S. at 74. At oral arguments before the Supreme Court, the respondent again argued the entire agreement was unconscionable. *Rent-A-Center*, 561 U.S. at 75. While he argued in his brief that the delegation provision itself was substantively unconscionable, the Supreme Court found "[h]e brought this challenge to the delegation provision too late" and would not consider it. *Rent-A-Center*, 561 U.S. at 75-76.

¶ 36 Thus, in this case, the question centers on whether plaintiffs specifically challenged the delegation clause of the 2012 reinsurance agreement. If they did, the trial court had the authority to consider the challenge to arbitrability. If they did not, the court was required to give effect to the agreement and compel arbitration.

¶ 37 In February 2017, the Applied defendants filed a motion to compel arbitration, asking the trial court to compel plaintiffs to arbitrate their claims concerning the 2012 reinsurance agreement "in accordance with the arbitration provision" of that agreement. A month later, plaintiffs filed a motion in opposition, arguing the arbitration provision was procedurally and substantively unconscionable. Moreover, plaintiffs contended the arbitration

provision did not delegate authority to the arbitration panel to determine whether the parties ever entered into an agreement to arbitrate.

¶ 38 In their March 2017 reply in support of the motion to stay, plaintiffs disagreed with the Applied defendants' argument that presupposed the delegation clause in the arbitration provision vested the arbitration panel with jurisdiction to decide whether a valid agreement to arbitrate exists. Plaintiffs argued the trial court had the authority to determine whether a stay of arbitration was warranted based on the fact that no agreement to arbitrate existed. Plaintiffs believed *Rent-A-Center* was irrelevant to their case because the delegation clause of the arbitration provision did not purport to encompass contract formation issues or issues as to whether the arbitration provision was void or voidable. Also, plaintiffs believed they had "no obligation to challenge the delegation clause specifically in order to ask this Court to decide the issue whether a valid agreement to arbitrate exists."

¶ 39 At the June 5, 2017, hearing on the motion to compel, plaintiffs' counsel stated they had "challenged the validity and the unconscionability of the delegation clause itself." Counsel for the Applied defendants disagreed, asserting plaintiffs challenged the arbitration provision, but not the delegation clause. Plaintiffs' counsel responded they have "more than sufficiently raised in our papers unconscionable aspects of the delegation clause itself," and "the next step would be the summary trial on the unconscionability of the delegation clause."

¶ 40 The trial judge found plaintiffs' counsel devoted a "substantial amount of argument" to cases "that get to the validity of the delegation clause" and "make a distinction between arbitrability and the validity of that delegation." In response to the Applied defendants' counsel's contention that plaintiffs did not discuss the delegation clause or the American Arbitration Association's rules or make a specific challenge in their response to the motion to

compel, the judge responded, "I just don't believe that's accurate." In his concluding remarks, the judge found the 2012 reinsurance agreement contained an arbitration provision, which included a delegation clause, which "has been challenged by the plaintiff[s] for purposes of the *Rent-A-Center* procedure."

¶ 41 We find plaintiffs sufficiently challenged the delegation clause in the trial court. While perhaps not as explicitly as desired by the Applied defendants, plaintiffs argued the arbitration provision, including the delegation clause, was unenforceable. Plaintiffs did not raise this issue for the first time on appeal, which was the death knell for the respondent in *Rent-A-Center*. Instead, by arguing the issue at the trial level, both sides had a full and fair opportunity to litigate the matter. See *Citizens of Humanity, LLC v. Applied Underwriters Captive Risk Assurance Co.* (*Citizens II*), 909 N.W.2d 614 (Neb. 2018) (finding the appellant had challenged the delegation of arbitrability at the trial level, in contrast to the challenge in *Rent-A-Center*); *Minnieland Private Day School, Inc. v. Applied Underwriters Captive Risk Assurance Co.*, 867 F.3d 449, 456 (4th Cir. 2017) (finding the plaintiff's assertion that the district court must consider the validity of the arbitration provision was "an argument relevant only to the enforceability of the delegation provision"). Accordingly, we find the court did not abuse its discretion in refusing to compel arbitration.

¶ 42 D. The Trial Court's Application of the Nebraska Arbitration Act

¶ 43 The Applied defendants argue the trial court erred in applying the Nebraska Arbitration Act to invalidate the arbitration provision in the 2012 reinsurance agreement. We disagree.

¶ 44 The 2012 reinsurance agreement contains a choice-of-law provision and states as follows:

> "16. This Agreement shall be exclusively governed by and construed in accordance with the laws of Nebraska and any matter concerning this Agreement that is not subject to the dispute resolution provisions of Paragraph 13 hereof shall be resolved exclusively by the courts of Nebraska without reference to its conflict of laws."

The agreement also provides that "[a]ll arbitration proceedings shall be conducted in the English language in accordance with the rules of the American Arbitration Association."

¶ 45 1. *The Federal Arbitration Act*

¶ 46 The Federal Arbitration Act "reflects the fundamental principle that arbitration is a matter of contract." *Rent-A-Center*, 561 U.S. at 67. In pertinent part, it provides "[a] written provision in *** a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract *** shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2 (2012). Thus, courts are "to enforce agreements to arbitrate according to their terms," unless the Federal Arbitration Act's "mandate has been 'overridden by a contrary congressional command.' " *CompuCredit Corp. v. Greenwood*, 565 U.S. 95, 98 (2012) (quoting *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220, 226 (1987)).

¶ 47 2. *The McCarran-Ferguson Act*

¶ 48 Congress passed the McCarran-Ferguson Act to overturn a United States Supreme Court decision under the commerce clause that threatened the continued supremacy of states to regulate "the activities of insurance companies in dealing with their policyholders." *Securities & Exchange Comm'n v. National Securities, Inc.*, 393 U.S. 453, 459 (1969). Section 1012(b) of the

McCarran-Ferguson Act (15 U.S.C. § 1012(b) (2012)) provides, in part, as follows:

> "No 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, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance."

"Thus, the McCarran-Ferguson Act gives rise to the doctrine of 'reverse preemption,' which, if applicable, can cause state insurance laws to trump federal laws that interfere with them." *Western Insurance Co. v. A & H Insurance, Inc.*, 784 F.3d 725, 727 (10th Cir. 2015).

¶ 49 3. *The Nebraska Arbitration Act*

¶ 50 "Although state laws vary on whether or not agreements to arbitrate future disputes under an insurance policy are enforceable, a provision in Nebraska's Uniform Arbitration Act, § 25-2602.01(f)(4), decidedly limits the enforceability of mandatory arbitration of future policyholder claims." *Citizens II*, 909 N.W.2d at 625. Generally, section 25-2602.01(b) of the Nebraska Arbitration Act provides for the enforcement of arbitration agreements and states, in part, as follows:

> "(b) A provision in a written contract to submit to arbitration any controversy thereafter arising between the parties is valid, enforceable, and irrevocable, except upon such grounds as exist at law or in equity for the revocation of any contract, if the provision is entered into voluntarily and willingly." Neb. Rev. Stat. § 25-2602.01(b) (2016).

However, subsection (f)(4) of section 25-2602.01 removes from this provision "any agreement

concerning or relating to an insurance policy other than a contract between insurance companies including a reinsurance contract." Neb. Rev. Stat. § 25-2602.01(f)(4) (2016).

> "In other words, where applied, § 25-2602.01 provides that agreements to arbitrate existing and future agreements are valid and enforceable except in specified circumstances sometimes referred to as 'antiarbitration provisions.' [Citation.] Agreements to arbitrate 'concerning or relating to an insurance policy' are one such circumstance where arbitration is not permitted. Such agreements would be invalid, and contrary contract provisions agreed to by the parties do not control over this statutory bar to enforcement of arbitration." *Citizens II*, 909 N.W.2d at 625.

¶ 51 4. *The Validity of the Arbitration Provision*

¶ 52 The validity of the arbitration provision in the 2012 reinsurance agreement turns on whether the McCarran-Ferguson Act applies, whether section 25-2602.01(f) of the Nebraska Arbitration Act applies, and whether those two statutes together reverse preempt the Federal Arbitration Act. See *Citizens I*, 226 Cal. Rptr. 3d at 8.

> "Courts apply a three-part test for determining whether the McCarran-Ferguson Act causes a state law to reverse preempt a federal statute: (1) whether the federal statute to be preempted specifically relates to the business of insurance, (2) whether the state law was enacted for regulating the business of insurance, and (3) whether application of the federal statute operates to invalidate, impair, or supersede the state law." *Citizens I*, 226 Cal. Rptr. 3d at

8.

See also *Humana Inc. v. Forsyth*, 525 U.S. 299, 307 (1999); *Citizens II*, 909 N.W.2d at 626; *Milmar*, 58 Misc. 3d at 501; *Monarch Consulting, Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA*, 47 N.E.3d 463, 470 (N.Y. 2016).

¶ 53 Courts have found the Federal Arbitration Act is a federal law that does not specifically relate to the business of insurance. *Citizens II*, 909 N.W.2d at 626; *Citizens I*, 226 Cal. Rptr. 3d at 8 (finding the Federal Arbitration Act "does not regulate the business of insurance"); *Kong v. Allied Professionals Insurance Co.*, 750 F.3d 1295, 1303 (11th Cir. 2014); *Munich American Reinsurance Co. v. Crawford*, 141 F.3d 585, 590 (5th Cir. 1998) (finding "no question" the Federal Arbitration Act "does not relate specifically to the business of insurance"). Moreover, they have found section 25-2602.01(f)(4) of the Nebraska Arbitration Act "is a state statute enacted to regulate the business of insurance." *Citizens II*, 909 N.W.2d at 626; *Citizens I*, 226 Cal. Rptr. 3d at 9. Thus, if the Nebraska Arbitration Act applies here, by operation of the McCarran-Ferguson Act, it reverse preempts the Federal Arbitration Act.

¶ 54 The Applied defendants argue the trial court erred by allowing a generic choice-of-law clause to trump the 2012 reinsurance agreement's incorporation of the American Arbitration Association's rules. They contend the Federal Arbitration Act and the American Arbitration Association's rules, not the Nebraska Arbitration Act, govern the 2012 reinsurance agreement. In support, the Applied defendants rely on the Third District's decision in *LRN Holding, Inc. v. Windlake Capital Advisors, LLC*, 409 Ill. App. 3d 1025, 949 N.E.2d 264 (2011), and the United States Supreme Court's decision in *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 64 (1995).

¶ 55 In *LRN Holding*, 409 Ill. App. 3d at 1033, 949 N.E.2d at 270-71, the Third

District noted "courts have held where parties to a contract agree to arbitrate in accordance with state law, the [Federal Arbitration Act] does not apply, even where interstate commerce is involved." The defendant, however, argued the arbitration provision at issue indicated arbitration would proceed under the rules of the American Arbitration Association and not the Illinois Arbitration Act. *LRN Holding*, 409 Ill. App. 3d at 1033, 949 N.E.2d at 271. The appellate court found the contract "contained a generic state choice-of-law clause but also incorporated the [American Arbitration Association] rules of arbitration. As such, we cannot find that the parties explicitly intended, by the mere inclusion of the generic choice-of-law clause, that disputes encompassed by the arbitration agreement be settled pursuant to the Uniform Arbitration Act." *LRN Holding*, 409 Ill. App. 3d at 1035, 949 N.E.2d at 272.

¶ 56 In *Mastrobuono*, 514 U.S. at 64, the United States Supreme Court stated "the choice-of-law provision covers the rights and duties of the parties, while the arbitration clause covers arbitration." Moreover, "*Mastrobuono* has been read to mean that a general choice of law provision in a contract will not extend to the arbitration clause, absent specific evidence that the parties intended it to do so." *State Farm Mutual Automobile Insurance Co. v. George Hyman Construction Co.*, 306 Ill. App. 3d 874, 881, 715 N.E.2d 749 (1999).

¶ 57 Like the Applied defendants in this case, a similar argument was made in *Citizens I*, 226 Cal. Rptr. 3d at 10, where the defendants contended an identical general choice-of-law provision in an identical reinsurance agreement "constitute[d] an agreement to apply Nebraska law to resolve the parties' substantive claims only, and not to incorporate state law rules limiting arbitration." The California court of appeal stated as follows:

> "*Mastrobuono* is distinguishable because it involved two provisions that on their face pointed to different bodies of law with

> conflicting rules regarding the availability of punitive damages. The Supreme Court drew the distinction between 'substantive principles' of law and 'special rules limiting the authority of arbitrators' solely as a means of 'giv[ing] effect' to both provisions. [Citation.] Here, however, the [reinsurance agreement] has a single provision that unambiguously provides that the [reinsurance agreement] 'shall be exclusively governed by and construed in accordance with the laws of Nebraska.' Although the [reinsurance agreement] does refer to the [American Arbitration Association] rules, those rules—unlike the competing arbitration rules in *Mastrobuono*—do not conflict with Nebraska law. Because there is no need to give effect to any competing provision, there is no basis not to give effect to its plain language incorporating *all* of the laws of Nebraska, including its substantive law prohibiting the arbitration of insurance-related disputes." (Emphasis in original.) *Citizens I*, 226 Cal. Rptr. 3d at 10.

See also *Milmar*, 58 Misc. 3d at 504 (finding *Mastrobuono* concerned only the scope of a valid arbitration agreement and its analysis only applies to agreements covered by the Federal Arbitration Act).

¶ 58 We agree with the cases finding *Mastrobuono* distinguishable under the facts of this case. We also find the Applied defendants' reliance on *LRN Holding* unavailing. In that case, the court held the plaintiffs' claim that the entire contract was "void *ab initio*" because the contract violated the Illinois Brokers Act fell under the jurisdiction of the arbitrator. *LRN*

Holding, 409 Ill. App. 3d at 1028-31, 949 N.E.2d at 267-69. However, *LRN Holding* did not involve the application of a statute regulating the business of insurance and its holding is inapplicable here. Also, it does not involve finding an entire contract void, but merely finding an arbitration clause void.

¶ 59 We agree with the trial court that the Nebraska Arbitration Act applies in this case and the application of the McCarran-Ferguson Act reverse preempts the Federal Arbitration Act. See *Citizens II*, 909 N.W.2d at 633; *Citizens I*, 226 Cal. Rptr. 3d at 12; *Milmar*, 58 Misc. 3d at 520. Other courts have also found the Federal Arbitration Act is reverse preempted under state laws related to insurance. *American Bankers Insurance Co. of Florida v. Inman*, 436 F.3d 490, 493-94 (5th Cir. 2006) (finding the Federal Arbitration Act was reverse preempted by a Mississippi statute prohibiting arbitration of disputes regarding uninsured and underinsured motorist coverage); *McKnight v. Chicago Title Insurance Co.*, 358 F.3d 854, 858-59 (11th Cir. 2004) (finding the Federal Arbitration Act was reverse preempted by Georgia law prohibiting arbitration clauses in insurance contracts); *Standard Security Life Insurance Co. of New York v. West*, 267 F.3d 821, 823-24 (8th Cir. 2001) (finding the Federal Arbitration Act was reverse preempted by the Missouri Arbitration Act prohibiting arbitration clauses in insurance contracts). We also agree section 25-2602.01(f) of the Nebraska Arbitration Act applies to the 2012 reinsurance agreement and renders the arbitration provision contained therein unenforceable. Accordingly, we find the court did not err in denying the Applied defendants' motion to compel arbitration.

¶ 60 III. CONCLUSION

¶ 61 For the reasons stated, we affirm the trial court's judgment.

¶ 62 Affirmed.