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Tips for Effective Management of Insurance Industry Arbitrations

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THERE'S BEEN AN UPTICK IN insurance industry arbitrations in recent years. These proceedings involving corporate insureds can raise complex and time-consuming issues. But early and focused efforts by the insurer and the insured can help provide for a fair and efficient process.

Arbitration works best when all parties have a clear meeting of the minds on important provisions contained in the arbitration clause and work together to avoid unnecessary complications. The best time to address management of the arbitration process is not after a disagreement has arisen, but when the insurance policy is being negotiated. While insurance companies typically draft the arbitration clause contained in the policy, an informed risk manager or in-house counsel for the insured may be able to negotiate specific and important changes to the provision. The following are a few important areas that should considered.

First, the scope of the arbitration clause will determine whether a particular dispute is subject to arbitration. Some insurance policy arbitration clauses limit their scope to simply valuation of damaged property whereas others are broadly drafted to include any and all disputes arising under the policy. A broadly drafted clause

gives an arbitration panel authority to consider all issues arising under the policy, including coverage questions and "arbitrability"—i.e., the question of what issues are covered by the arbitration clause. Failure to specify the scope of the arbitration clause frequently results in added delay and litigation costs.

Next, choice of law is an important but frequently overlooked topic. In fact, which state's law governs may determine the outcome of some arbitrations. Frequently, the law of the state of incorporation of the insurer or the insured govern the proceeding. This designation can be negotiated and should be made only after careful consideration by the insurance professionals involved with assistance of counsel. Again, failure to include a choice of law determination in an arbitration clause can result in delay and increased costs.

Which procedures and rules will be used in the arbitration proceeding are also important considerations. Although cost savings and efficiency are goals of arbitration, the ultimate goal of the Federal Arbitration Act is to enforce agreements resolving disputes. So, in a large complex insurance dispute, the parties probably should determine which procedures and rules will allow for sufficient discovery and motion practice to adequately develop their case. Most ADR providers, such as JAMS and AAA, have comprehensive commercial arbitration rules that can be applied if an ADR provider is included in the arbitration clause.

The comprehensive arbitration rules offered by JAMS and AAA also provide procedures for selection of neutrals and methods for dealing with nominations and objections. Without such procedures in place, selection of members of the arbitration panel can be extremely difficult. Another issue that arises in the insurance industry is a provision in the arbitration clause that sets forth required qualifications for the prospective arbitrators. For example, some provisions require arbitrators to have a certain amount of management or adjusting experience in the insurance industry. Insureds generally feel this type of provision tilts the playing field in the insurer's favor. Regardless of its consequences, such language severely limits the pool of potential arbitrators and makes selection of a panel difficult. The best choice may well be to allow each party maximum flexibility in selecting an arbitrator without regard to predetermined qualifications.

Another provision that can be negotiated is the forum-selection clause designating the place where the arbitration will take place. Again, the home state of the insurer or the insured are frequent choices, but there is another option that should be considered. If the insurance policy covers occurrences that would involve large numbers of witnesses and parties, the forum where the claim or occurrence arises might make the most sense when considering convenience and costs.

These are some of the important considerations both an insurer and insured should keep in mind when negotiating the terms of an arbitration clause in an insurance policy. Too often, these matters are overlooked or given little thought. When these terms are negotiated at the outset, the parties will have a fair and efficient alternative dispute resolution mechanism for resolving potential disputes.