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Reinsurer and Corporate Officer Held Liable Under Chapter 93A for Disavowing Reinsurance Agreement and “Stringing Along” the Cedent

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In an important decision with implications for cedents and reinsurers alike, the District Court for the District of Massachusetts, after a two-week bench trial, has held a reinsurer and its controlling officer liable under Chapter 93A (Massachusetts Unfair and Deceptive Trade Practices Act) for their bad-faith disavowal of a reinsurance agreement.[1] *Trenwick Am. Reins. Corp. v. IRC, Inc.* reaffirms the court’s prior holding in *Seven Provinces*[2] that, where a “moving target” strategy is employed to coerce a favorable compromise of reinsurance obligations, it may constitute a violation of Chapter 93A. Judge Nancy Gertner’s decision, which found that the defendants here “turned what should have been a routine claim against a reinsurer into a tortuous marathon,” [3] also includes noteworthy discussion of the status of the Follow the Fortunes doctrine in Massachusetts.

The Compcare Program

The facts involve a complex set of insurance and reinsurance agreements put in place by Malcolm Swasey and corporations controlled by him, including IRC, Inc. and IRC Re, Limited (the Defendants). In 1994, through these companies, Swasey administered and underwrote a workers’ compensation insurance and employers’ liability insurance program known as Compcare. Swasey procured insurance for this program in 1996 from Reliance National Insurance Company (Reliance). Trenwick America Reinsurance Corporation (the Plantiff) reinsured 54% of Reliance’s risk. The parties disagreed as to whether a portion of the risk was then retroceded by Trenwick to IRC Re.[4]

The Reinsurance Claim

In the ensuing years, IRC Re received in excess of $1 million in net premiums from Trenwick.[5] A dispute arose when Trenwick’s reinsurance intermediary attempted to collect IRC Re’s outstanding balances in 2004 and into 2005. After making no progress with IRC Re for more than a year, the intermediary reached out to Swasey directly. Swasey requested various information, which was provided, and, after two months of negotiations, the parties were approximately $300,000 apart.

Swasey’s own calculations, however, acknowledged that at least $2.4 million was owed by IRC Re to Trenwick. The intermediary continued to press for payment until Swasey abruptly refused to speak with her, indicating that he would be sending her a fax shortly. The fax contested—for the first time—the very existence of the reinsurance agreement and “conditioned further discussions with [Trenwick’s intermediary] on her producing a written contract between IRC Re and Trenwick relative to [the

program]." [6]

Overwhelming Evidence of an Agreement

Despite the Defendants' contention that "there was, at most, only an 'agreement to agree,'" the court found "overwhelming" evidence of a contract in the writings between the parties.[7] The court found that IRC Re repeatedly acknowledged the existence of the agreement through its own documents, its dealings with all of the participants in the program, outside auditors, and government agencies, and by accepting millions of dollars in premiums. Indeed, the court noted that "the witnesses who testified on the behalf of the plaintiffs—even those without an interest in the outcome—were positively indignant that IRC Re and Swasey had the temerity to claim 'no contract.'" [8] The court also quickly dispatched the Defendants' Statute of Frauds arguments, finding that the correspondence between the parties, which contained the contract's essential terms, satisfied the writing requirement.

Expert Evidence Required to Imply the Follow the Fortunes Doctrine

In an apparent attempt to relitigate defenses that Trenwick raised in an underlying arbitration with Reliance, the Defendants further argued that, even if there were an agreement, the Follow the Fortunes doctrine did not apply given the absence of an express provision. The court found that it is not clear whether the Follow the Fortunes doctrine is recognized in Massachusetts. It defined the doctrine to include Follow the Settlements and to "require a reinsurer to cover the reinsured unless the reinsurer demonstrates that the original insurer's liability resulted from fraud or collusion, or unless the claim was not reasonably within the scope of the original policy." [9]

In light of that, the court held that determining whether a reinsurer's duty to follow the fortunes of its cedent is implied in a reinsurance agreement was a question of fact, which must be resolved through expert testimony; however, it was persuaded by Plaintiffs' expert who testified that the doctrine is a customary component of almost every reinsurance agreement, that all of the written contracts relative to the Compcare program had Follow the Settlements language, and that it would be extraordinary not to see a Follow the Settlements provision in the retrocessional agreement, had it been put to writing.[10]

Chapter 93A Liability

Previously, in her oft-cited *Seven Provinces* decision, Judge Gertner had held that a "moving target" strategy employed to "evade payment of reinsurance obligations" may constitute a Chapter 93A violation. The First Circuit affirmed that decision, noting that the "case did not involve a party whose only miscue was to decide (incorrectly, as matters turned out) to let the courts resolve a good-faith disagreement or to rely mistakenly on faulty legal argumentation." [11] "Instead, Seven Provinces' conduct—raising multiple, shifting defenses (many of them insubstantial) in a lengthy pattern of foot-dragging and stringing Commercial Union along, with the intent (as its own witnesses admitted) of pressuring Commercial Union to compromise its claim—had the extortionate quality that marks a 93A violation." [12]

Applying the same reasoning again here, Judge Gertner held that IRC Re, Swasey, and IRC, Inc. all violated, and were independently liable under, Chapter 93A. The court concluded that IRC Re plainly lacked a good-faith basis to dispute the existence of the contact and raised that defense, "contrived at the eleventh hour, to avoid paying." [13]

With respect to Swasey, the court noted, "Swasey's fingerprints are all over this case—the formation of the Reliance program, the company that administered it, the company that reinsured it. His acts cannot be disentangled from IRC Re." [14] In addition, the court found Swasey's prelitigation conduct was "compounded by his post-litigation antics," which included misrepresentations during his

deposition and even at trial.

The court also found IRC, Inc., a program manager and intermediary also controlled by Swasey, liable under Chapter 93A for supporting IRC Re's untenable position that there was no agreement. It held that IRC, Inc. was fully aware that it was not participating in a good-faith contract dispute, but rather was using its status as program manager and intermediary to frustrate the Plaintiffs' contractual rights.[15]

The court awarded the Plaintiffs the balance due under the IRC Re agreement, $4.2 million, plus the statutory rate of 12% interest from the commencement of the suit, an additional $1.9 million. Because Judge Gertner found that the Chapter 93A violations were willful and knowing, she also awarded double damages (including interest), plus attorneys' fees and cost of suit pursuant to the statute.

* * *

In light of this decision, albeit one involving several egregious facts, cedents, reinsurers, and their corporate officers must be mindful that where there is a *bona fide* dispute regarding a reinsurance cession, a court is unlikely to find a Chapter 93A violation. Where, however, the evidence shows that a reinsurer withheld payments owed under a reinsurance agreement, coupled with a moving target strategy, to extort a more favorable settlement of the claim, a court may find a Chapter 93A violation.

If you would like to discuss the *Trenwick* decision or other matters concerning insurance or reinsurance, please contact any member of Mintz Levin's Insurance & Reinsurance Practice Group.

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Endnotes

1 *Trenwick Am. Reins. Corp. v. IRC, Inc.*, ___ F. Supp. 2d ___, 2011 WL 570016, *24-28 (D. Mass. Feb. 16, 2011).

2 *Commercial Union Ins. Co. v. Seven Provinces Ins. Co., Ltd.*, 9 F.Supp.2d 49 (D.Mass. 1998).

3 *Trenwick*, 2011 WL 570016, at *3.

4 *Id.* at *1.

5 *Id.* at *8.

6 *Id.* at *5.

7 *Id.* at *9.

8 *Id*. at *24.

9 *Id.* at *28.

10 *Id.* at *16.

11 *Commercial Union Ins. Co. v. Seven Provinces Ins. Co., Ltd.*, 217 F.3d 33, 43 (1st Cir. 2000).

12 *Id.*

13 *Trenwick*, 2011 WL 570016, at *24.

14 *Id.* (emphasis in original).

15 *Id.* at *25-27.

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