IS THERE RHYME OR REASON TO THE SCOPE OF PERMISSIBLE REINSURANCE-RELATED DISCOVERY?

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Courts in numerous jurisdictions continue to consider whether reinsurance-related information is discoverable in insurance coverage litigation. Decisions go both ways. Some courts find that reinsurance information and communications are not relevant, or the requests for such information are too broad, and the reinsurance-related discovery is therefore precluded. Other courts, especially where a bad faith claim is alleged against an insurer, hold that reinsurance discovery is fair game. Is there any rhyme or reason to the various holdings? Does a claim for bad faith mean that, automatically, all reinsurance information must be produced? The answer to the latter question is no. The answer to the former question is maybe.

Decisions Precluding Discovery of Reinsurance Information

Two recent federal court decisions illustrate what limitations can be placed on the scope of reinsurance discovery and provide guidance to parties and their counsel when seeking, and opposing, reinsurance-related discovery.

In the first decision, *Indianapolis Airport Authority v. Travelers Property Casualty Co. of America*, 2015 WL 1548959 (S.D. Ind. Apr. 7, 2015), the court considered a non-party subpoena that the Indianapolis Airport Authority ("IAA") served on General Reinsurance ("Gen Re") seeking copies of Gen Re's claims and underwriting files. Specifically, the subpoena sought nine types of reinsurance-related documents, including reinsurance agreements, policies, and treaties issued by Gen Re to Travelers regarding IAA or the terminal project at issue in the coverage litigation; all documents regarding quotes for facultative reinsurance Gen Re sent to Travelers; documents

containing reinsurance analysis relating to IAA, the terminal project, or IAA's insurance policies; and all communications between Gen Re and Travelers relating to IAA or the terminal project. In all, the subpoena sought reinsurance discovery from Gen Re for a span of eight years.

Travelers moved to quash the subpoena on the grounds that such reinsurance information was not relevant to the claims in dispute and the requests were overly broad, unduly burdensome, and otherwise not discoverable. Travelers further argued that the reinsurance discovery sought contained sensitive business information not relevant to the coverage dispute.

The court granted Travelers' motion to quash and held that IAA was precluded from obtaining any discovery of such reinsurance documentation. The court found the subpoena was overly broad, unduly burdensome, and the reinsurance information was irrelevant. While the court recognized some circumstances where reinsurance information could be relevant and discoverable, for example, where ambiguous policy terms are at issue (*see e.g.*, *Cummins, Inc. v. Ace American Ins. Co.*, 2011 WL 130158 (S.D. Ind. Jan. 14, 2011) (finding reinsurance documents discoverable to aid in construing ambiguous policy terms in a coverage dispute)), limitations still applied on the permissible scope of such discovery. Because IAA's requests spanned more than eight years and focused "not only on communications related to the policy at issue, but also on pre-claim and pre-reinsurance policy issuance," the requests were unduly burdensome. 2015 WL 1548959, at *2.

The court further found that the overly-broad communications IAA sought contained "commercially sensitive information related to Gen Re," none of which was at issue in the case or relevant to even potentially ambiguous terms in the Travelers policy. *Id.* That commercially sensitive information included Gen Re's internal underwriting, quotations, ratings, and premiums. *Id.* at *2, n.2. The court therefore found that Gen Re's documents were not discoverable.

In the second decision, the court in *Utica Mutual Ins. Co. v. Clearwater Ins. Co.*, Case No. 6:13-CV-01178 (N.D.N.Y. Jan. 20, 2015) refused to compel the disclosure of

reinsurance information that was unrelated to the specific facultative reinsurance policies at issue in the case.

At issue was whether payment was due under reinsurance certificates issued by Clearwater to Utica Mutual for umbrella policies Utica Mutual issued to one of its underlying insureds. Utica Mutual settled its claim with its insured and sought payment from Clearwater under those reinsurance policies. Litigation on Clearwater's obligation to pay Utica Mutual's reinsurance claim then ensued.

In discovery, Utica Mutual sought to compel Clearwater to produce reinsurance contracts and other documents concerning contractual relationships Clearwater had with other insurers, arguing those documents were relevant to Clearwater's claim that Utica Mutual misled it into paying amounts due under the facultative reinsurance contracts at issue. In turn, Clearwater sought discovery that Utica Mutual claimed relate solely to other policies of insurance or reinsurance and which "involve different contractual terms than the reinsurance agreements at issue in this claim." Opinion at p. 3. Clearwater argued that such information was needed to determine damages, if any, and whether or not Utica Mutual wrote other primary policies without aggregate limits – an issue resolved as part of the underlying litigation and settlement with Utica Mutual's insured.

The court found that discovery of policies unrelated to the facultative reinsurance certificates at issue was "not germane" and "only faintly relevant" to the issues at bar. As such, the discovery "would lead to an unnecessary, burdensome, and confusing diversion from the real issues in dispute." Opinion at p. 8. The court therefore precluded the discovery of unrelated reinsurance contracts, stating: "In short, the Court finds the subject documents sought and interrogatories propounded . . . are not relevant to the claims and defenses in this action involving specific facultative reinsurance contracts, and are not reasonably calculated to lead to the discovery of admissible evidence." *Id.*[1]

[1] In precluding the scope of discovery Clearwater sought, the court specifically noted that Clearwater, as a reinsurer, could not re-litigate the underlying coverage dispute and settlement between Utica Mutual and its insured. Opinion at p. 7.

The *IAA* and *Utica Mutual* courts thus both rejected the scope of the reinsurance information sought, finding such information not discoverable when it did not relate to the specific policies or specific claims at issue in each case.

Decisions Allowing Discovery of Reinsurance Information

While the *IAA* and *Utica Mutual* courts rejected the scope of the reinsurance discovery sought, other courts have ordered the production of reinsurance-related information. Some courts, however, when ordering such discovery, focus on the objections made to the discovery requests and whether those objections are specifically tailored to the issues raised in the case. When the objections are not tailored, reinsurance discovery can be fair game.

In *Klein v. Federal Ins. Co.*, 2014 WL 3408355 (N.D. Texas July 14, 2014), for example, the court ordered the production of reinsurance discovery from Federal Insurance Company. Federal had withheld 25 documents from discovery on the basis that they contained reinsurance information. The plaintiffs argued that the requested information was relevant on the contested issue of notice under Federal's policy. Federal responded that:

> [C]ourts generally refuse a policyholder's discovery request regarding reinsurance agreements and reinsurance communications for the purpose of interpreting the underlying policy; that courts often protect reinsurance information from discovery because this information is a critical aspect of an insurance company's financial stability and must, consequently, be maintained in strict confidence and protected from discovery; and that an insurer's decision to purchase reinsurance is based on internal business considerations unrelated to the insurer's evaluation of a particular claim or interpretation of any particular term in the underlying policies. *Id.* at *7.

The court rejected each of Federal's arguments, finding the reinsurance information was relevant to the contested issue of notice. In rejecting Federal's arguments, the court specifically noted that "Federal addresses in only general terms the reasons courts refuse to allow the discovery of reinsurance agreements and communications. It does not show specifically why this discovery should be precluded

in this case … [Accordingly,] the reasons for foreclosing discovery appear to lack force in these circumstances." *Id.* (emphasis added).

In *National Union Fire Ins. Co. of Pittsburgh, Pa. v. Donaldson Co. Inc.,* 2014 WL 2865900 (D. Minn. June 24, 2014), the insured moved to compel National Union and American Home Assurance Company (collectively, the "Insurers") to produce internal underwriting files, loss reserve information, and communications with their reinsurers. The magistrate judge granted the motion to compel and directed the Insurers to produce all such information, concluding that it was relevant to the Insurers' "formulation of their position on coverage." *Id.* at *3.

The Insurers objected to the magistrate judge's order arguing, in part, that "they should not be compelled to produce communications with their reinsurers because courts *generally do not permit discovery of such communications* for the purpose of interpreting unambiguous insurance policies." *Id.* at *5 (emphasis added). As in *Klein*, however, the court rejected such general arguments as to the scope of permissible discovery:

> [The Insurers] do not address Donaldson's argument that such communications are potentially relevant to its claim for breach of the duty of good faith and fair dealing . . . Donaldson argues that communications with reinsurers will likely reveal what [the Insurers] knew and when about their plans for applying coverage under the policies because they `would have had an obligation to disclose known facts' to reinsurers. *Id.*

The *Donaldson* court concluded that the Insurers' communications with their reinsurers were relevant to the insured's claims for breach of the duty of good faith and fair dealing brought against the Insurers and were, therefore, discoverable. *Id.*

In ordering the Insurers to produce the reinsurance communications, the court acknowledged the split of authority on the issue of the discoverability of reinsurance information. *See Id.* (collecting cases). The court specifically noted, however, that "several courts have concluded that communications with reinsurers are relevant and discoverable in cases where a party brings a claim for bad faith against an insurer." *Id.* At the core of those decisions is the premise that communications between an insurer

and its reinsurer are likely to contain information that is relevant to the issue of the insurer's bad faith toward its insured, including valuable admissions. *See e.g., Imperial Trading Co., Inc. v. Travelers Property Cas. Co. of Am.*, 2009 WL 1247122, at *4 (E.D. La. May 5, 2009) (distinguishing cases involving bad faith with those involving only policy interpretation and finding that, in the former, reinsurance-related communications were without question, relevant).[2]

Does a bad faith claim, then, automatically open the door to the discovery of all reinsurance information?

Reinsurance Discovery When Bad Faith Is Alleged

As recognized in *Donaldson*, many courts have ordered reinsurance-related discovery when claims of bad faith are made against an insurer.

Recently, in *Phoenix Insurance Co. v. Cantex, Inc.*, 2015 WL 1740334 (D. Colo. Apr. 14, 2015), the court held that discovery requests and deposition designations seeking reserve and reinsurance information were relevant when claims of bad faith were brought against the insurers. Noting that the allegations of bad faith were "fact driven," the court found that the "manner in which the [i]nsurers evaluated the [u]nderlying [l]itigation" may reveal facts relevant to those bad faith claims. *Id.* at 3. In doing so, the court recognized that those bad faith claims were subject to pending motions to dismiss, but stated that because those motions had yet to be ruled upon, "the claims and underlying allegations remain in the case and subject to discovery." *Id.* at 2.

Similarly, in *Leevac Shipbuilders LLC v. Westchester Surplus Lines Ins. Co.*, 2015 WL 224890 (W.D. La. Jan. 15, 2015), the court held that reinsurance documents were relevant and discoverable where the insured brought a bad faith action against its insurer. Citing to the decision in *Imperial Trading, supra,* where the court held that both reinsurance agreements and communications were relevant and discoverable in cases where a plaintiff seeks bad faith penalties against an insurer, the *Leevac* court saw "no

[2] An insured's claim for breach of the implied warranty of good faith and fair dealing is recognized as the equivalent of a first-party bad faith claim. *See e.g., QBE Insurance Corp. v. Chalfonte Condo. Apt. Assoc., Inc.*, 94 So.3d 541, 549 (Fla. 2012). The *Donaldson* court's reasoning for permitting the reinsurance discovery at issue is therefore in line with those courts concluding that such reinsurance-related communications are discoverable when claims of bad faith are pending.

reason to break from such precedent." *Id.* at *5. The court therefore ordered Westchester to produce files and documents evidencing any reinsurance agreements or related communications. The court did limit such reinsurance discovery to only those documents that "pertain to Leevac's policy or claim that is the subject of the present lawsuit." *Id.*

Not all courts, however, find that a pending bad faith claim automatically justifies an open-door policy to reinsurance-related discovery. In *Broadrock Gas Services, LLC v. AIG Specialty Ins. Co.*, 2015 WL 916464 (S.D.N.Y. Mar. 2, 2015), the court held that certain reinsurance calculations were irrelevant, and therefore not discoverable, even where bad faith was alleged in the ongoing coverage litigation. At issue was certain reinsurance information that was redacted from "so-called executive claim summaries." *Id.* at *2. AIG Specialty Insurance Company ("ASIC") maintained that the redacted information concerned only material that "identified the treaty reinsurance percentage participation for the policy [at issue] and on that basis calculated the net exposure of ASIC as compared to the `gross exposure.'" *Id.* at *2. ASIC argued that such data was completely irrelevant to the claims and defenses at issue in the case, which concerned ASIC's declination of coverage under a pollution liability policy.

Seeing no reason to question the accuracy of ASIC's counsel's description of the redacted material, the court found no reason why "reinsurance information of the type described by defendant's counsel has any relevance to the parties' claims and defenses." *Id.* at *3. The court therefore declined to order the production of that redacted reinsurance information. *See also Flintkote Co. v. General Accident Assurance Co. of Canada*, 2009 WL 1457974, at *5-6 (N.D. Cal. May 26, 2009) (denying discoverability of reinsurance information, even where a bad faith claim against the insurer was pending, because the reinsurance agreements were not directly in dispute and the reinsurance information sought was not relevant to "determining the `state of mind' or actual knowledge of the insurer" regarding the claims at issue).

Take Away – The Discoverability of Reinsurance Information is Still a Hot Topic

Courts continue to consider the proper scope of reinsurance-related discovery and litigants continue to request and oppose this discovery. While decisions do go both

ways, the decisions discussed above certainly support the position that discovery requests for reinsurance information should relate to the insurance policies and claims actually at issue and objections to such discovery should be specifically tailored to the claims raised in the case. In addition, while many courts seem to favor the production of reinsurance information when there are bad faith claims against the insurer, especially communications between an insurer and its reinsurer, insureds should not presuppose that a pending bad faith claim means that any and all reinsurance discovery is fair game.

In the end, the discoverability of reinsurance-related information continues to be an important issue for insureds, insurers, reinsurers, and their counsel to be aware of.

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