CIRCUMSTANCES UNDER WHICH OFFSHORE OR OTHER UNAUTHORIZED INSURERS AND REINSURERS IN LITIGATION OR ARBITRATION ARE SUBJECT TO NEW YORK SECURITY REQUIREMENTS

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I. Introduction

In recent years, an increasing number of insurers and reinsurers have moved offshore for a variety of reasons, particularly to achieve a lower level of regulation. To be successful in this regard, it is essential that such insurers and reinsurers avoid acts that constitute "doing business" in the various states. Usually, this means not having a sales or administrative staff in the United States and negotiating and effectuating the insurance or reinsurance in an offshore domicile.

A cutting edge on this issue is New York statute (ISC§ 1213)[1] that requires that before an insurer or reinsurer can file a pleading in any court or arbitration proceeding, it must file a bond or obtain a license. The actions which would trigger such an obligation include the following, in New York by mail or otherwise: soliciting business; issuing or delivering policies to residents; collection of premium; and any other transaction of business. (*See n.* 1). One court described the purpose of the statute as follows:

> The statute addresses the 'concern that many residents of this state hold policies of insurance issued or delivered in this state by insurers while not authorized to do business in this state, thus presenting to such residents the often insuperable obstacle of resorting to distant forms for the purpose of asserting legal rights under such policies.' The principle purpose of the statute, then, is to subject unauthorized foreign and alien insurers who have transacted business in the state to the jurisdiction of the New York courts. The statute accomplishes this purpose by declaring that certain activities on the part of the foreign unauthorized insurer constitute the appointment of the New York Superintendent of its attorney for as its attorney for service of process. In addition, the statute requires the unauthorized insurer, before filing a pleading in a court action, to deposit money or file a bond to insure a fund for the payment of any judgment obtained in the action.[2]

The purpose of this article is to examine selected case law as to the circumstances under which offshore insurers and reinsurers are subject to the New York security statute.

II. Cases Requiring Off Shore and Other Unauthorized Insurers to Post Security

One troubling case in this category is *MF Global Holdings Ltd. v. Allied World Assur. Co.* 2017 Bankr. LEXIS 1585 (S.D.N.Y.). The insured secured insurance from a Bermudian insurer through a Bermudian broker which:

> [W]as responsible for the solicitation, negotiation, issuance and delivery of the policy, and the payment of premiums on the underlying policy. ('The Allied World policy was negotiated, underwritten, issued, delivered, and paid exclusively in Bermuda, through [Willis], a Bermuda-based broker that was acting on [the insured's] behalf in Bermuda.') It appears that Willis was then responsible for sending or delivering the policy to MF Global in New York.[3]

Thus, the Bermudian insurer argued that it did not fall within the language of the statute that since the security requirement applies to policies issued or delivered in New York. However, the court regarded the insurer's business model as a subterfuge:

> The court is unpersuaded that the New York legislature, in drafting section 1213(c), contemplated that foreign unlicensed insurance companies, such as Allied World, that are subject to personal jurisdiction in New York courts could so easily work around the bond requirement if they are parties to litigation in New York. The use of a broker or some other intermediary for the delivery of a policy, rather than delivering a policy directly to an insured, is not enough to skirt the bond requirement.[4]

While this decision was appealed and affirmed, this particular ruling was not appealed. *MF Global Holdings Ltd. v. Allied World Assurance. Co.*, 2017 U.S. Dist. LEXIS 101293 (S.D.N.Y.). Another far reaching case requiring reinsurers to post security is *Morgan v. Amer. Risk Management, Inc.*, 1990 U.S. Dist. LEXIS 9037 (S.D.N.Y.). In this case, the Kentucky liquidator of a reinsurer was suing retrocessionaires in New York. The reinsurer had offices in New York and was authorized to do business there but lost its authorization and closed its office when the reinsurer went into receivership.

Initially, the *Morgan* court rejected the retrocessionaires' arguments that § 1213 does not apply to reinsurance. Likewise, it rejected the argument that the non-resident liquidator was not entitled to invoke the boding requirement. Finally, the court rejected the argument that the reinsurer was no longer a New York resident:

> I agree with the [liquidator] that the fact that [the reinsurer] has not been authorized to do business and has not done business in New York since it was

> declared insolvent in 1985 is irrelevant to the court's exercise of jurisdiction over defendants in this action. When the retrocessionaires executed and delivered the Treaty to [the reinsurer] in New York, [the reinsurer] was present in New York and authorized to do business here. It is the transaction out of which this action arose that triggers the court's jurisdiction under § 1213 (b)(1), not the status of the plaintiff at the time the action was commenced.[5]

Another reinsurance dispute was the backdrop for *John Hancock Property & Cas. Ins. Co. v. Unversale Ins. Co.*, 147 F.R.D. 40 (S.D.N.Y. 1993). The cedent was domiciled in Boston and was licensed in New York and the reinsurer was domiciled in Switzerland and was not licensed in New York. Placement correspondence was not to or from New York but the cedent argued that security under § 1213 was required. The court agreed:

> [The reinsurer's] contention that delivery of a policy in New York is required to invoke section 1213 is also misplaced. N.Y. Ins. Law § 1101 (b)(2) specifically provides that such delivery is not essential before an entity is required to comply with section 1213. Rather, a reinsurance transaction 'effected by mail from outside [New York State] by an unauthorized foreign or alien insurer' triggers the section 1213 requirement. N.Y. Ins. Law § 1101 (b)(2). [The reinsurer] meets this test. [The reinsurer] is an unauthorized alien insurer that engaged in a reinsurance transaction that was effected by mail from outside New York. Consequently, [the reinsurer] was required to comply with section 1213.

The "policy" represented by § 1213, rather than its actual text, seems to be the basis of the ruling in *Marsh & McLennan Cos. v. Gio Ins. Ltd.,* 2013 U.S. Dist. LEXIS 110613 (S.D.N.Y.). The insured was domiciled in Delaware and was authorized to do business in New York. It secured errors and omissions insurance from an Australian insurer not licensed in New York. When a dispute arose, the insured sued the insurer in state court which denied the insurer's request to dismiss and ordered $1.5 million in security pursuant to § 1213 (c)(1). The reinsurer filed this action with the federal court seeking dismissal and a release of security. The federal court declined to do so ruling:

> New York has made clear that Section 1213's security requirement is designed to help New York residents avoid 'the often insuperable obstacle of resorting to distant forums for the purpose of asserting legal rights' under insurance contracts.' . . . [I]n deference to New York's public policy regarding unauthorized foreign insurers (particularly in light of GIO's run-off status and its ability to satisfy any potential aribitral award and judgment), the Court will not release the GIO's security pending the arbitration.[6]

III. Cases Not Requiring Off Shore and Other Unauthorized Insurers to Post Security

For some reason, the *MF Global Holdings Ltd* (*supra*) court did not cite a strikingly similar case from a year earlier in the same court: *Drennan v. Certain Underwriters at Lloyd's of London,* 563 B.R. 756. The plaintiffs in this action were representatives of several class actions and a

liquidating trust seeking to recover on the insurance purchased by a bankrupt purchaser and reseller of mortgage loans. The plaintiffs sued the Bermudian insurers that issued the policies and the insurers sought dismissal based on arbitration clauses in the policies.
The insured was advised by a Bermudian insurance broker that received the policies from the insurers and paid the premium for the policies to the insurers. Nonetheless, the insureds argue that the Bermudian insurers were subject to the security requirement of § 1213 because: (1) several insureds were authorized to do business in New York and one was domiciled there; (2) they insured business activities in New York; and (3) performed certain claim handling activities there. The court rejected the plaintiff's arguments and ruled:

> [T]he court finds that the bond requirement was not triggered under section 1213 (b)(1)(A). It is undisputed that the Bermuda Insurers' policies were issued in Bermuda and delivered in Bermuda to AON, the insurance broker acting as an intermediary between [the insured] and the Bermuda Insurers. In fact, the address of the insured on each policy lists [the insured's] Detroit, Michigan address.
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> Nor did the Bermuda Insurers trigger the bond requirements by transacting business in New York under Section 1213 (b)(1)(A). . . . The issuance and delivery of an insurance policy outside New York, in and of itself does not constitute "transaction of business" under CPLR § 302 (a)(1) or Insurance Law § 1213.[7]

The plaintiffs in *Associated Aviation Underwriters v. Arab Ins. Group (B.S.C),* 2003 U.S. Dist. LEXIS 6254 (S.D.N.Y.) included an unincorporated association of insurance companies, all of which were licensed in New York and two were domiciled there. They sued two reinsurers domiciled in Bahrain for recovery of certain 9/11-related losses. The defendants argued that they were not subject to the security requirement of § 1213 since they mailed the reinsurance contracts to New Jersey rather than New York. The court agreed with the defendants:

> Upon reading the statute as a whole, it is clear that merely issuing insurance outside this state to a New York citizen or insuring property that is fortuitously destroyed in New York is not enough. Rather, a defendant must also have purposeful contacts with New York state. The legislature determined that issuing or delivering a policy within or into New York qualifies as "purposeful contacts" so that a court may assert personal jurisdiction over the unauthorized foreign insurer.[8]

The *Associated Aviation* court found that purposeful activity did not include: (1) reinsuring New York insurance policies; (2) reinsuring cedents licensed or domiciled in New York; or (3) the fact that losses for which indemnity was sought took place in New York.
Ghose v. CNA Reins. Co. Ltd., 841 N.Y.S.2d 519 (S.C.App.Div. 2007) involved London insurers that issued a directors and officers liability policy to a Bermudian reinsurance company. The plaintiff, Ghose, was CEO of the insured, New Cap, and claimed to have been a resident of New York when the policy was issued. The plaintiff filed an action in New York for coverage and

asked for security under § 1213. The court granted the insurers' motion for *forum non conveniens* and commented:

> We note, however, that Insurance Law § 1213 (a) applies only to situations involving 'policies of insurance issued or delivered in this state by insurers while not authorized to do business in this state.' The purpose of the statute, *inter alia*, 'to assure that a foreign carrier's funds will be available in this State to satisfy any potential judgment.' Thus, insomuch as the policy was not issued or delivered in New York, the section is not applicable.[9]

In *Blau v. Allianz Life Ins. Co. of N. Am.,* 124 F.Supp.3d 161 (E.D.N.Y. 2015) a life insurance company issued a policy on the life of a particular individual to a trust in New York. The trust had arranged for the insurance through a New York broker and paid premiums from New York. However, the life insurer as not licensed in New York, had no agents there and delivered the policy in New Jersey. The court ruled that § 1213 did not apply since it does not confer jurisdiction over an insurer which insures the life of a New York resident via a policy issued in another state since the issue is the activities of the insurer, not those of party seeking to assert jurisdiction. The mere mailing of premium checks from New York is not sufficient to create jurisdiction.

IV. Commentary

There is an extraordinary range of case law concerning the insurers and reinsures that can be caught up in the security requirements of § 1213. Some of these cases suggest that any insurer or reinsurer can be required to post security if its insured or cedent was located in or authorized in New York at the time coverage was purchased. This goes far beyond the effort to secure the obligations of those entities that do business in New York without a proper license. While there is a good deal of better reasoned decisions, due process litigation will be necessary to create bright lines in this regard.

ENDNOTES

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[1] In pertinent part, ISC§ 1213 provides:

(a) The purpose of this section is to subject certain insurers to the jurisdiction of the courts of this state in suits by or on behalf of insureds or beneficiaries under certain insurance contracts. The legislature declares that it is a subject of concern that many residents of this state hold policies of insurance issued or delivered in this state by insurers while not authorized to do business in this state, thus presenting to such residents the often insuperable obstacle of resorting to distant forums for the purpose of asserting legal rights under such policies. In furtherance of such state interest, the legislature herein provides a method of substituted services upon such insurers and declares that in so doing it exercises its power to . . . [determine] what constitutes doing business in this state . . . .

(b) (1) Any of the following acts in this state, effected by mail or otherwise, by an unauthorized foreign or alien insurer:

(A) the issuance or delivery of contracts of insurance to residents of this state or to corporations authorized to do business therein,

(B) the solicitation of applications for such contracts,
(C) the collection of premiums, membership fees, assessments or other consideration for such contracts, or
(D) any other transaction of business,
[constitutes the appointment by the insurer of the superintendent of insurance as their attorney for service of process.]
. . . .
(c) (1) Before any unauthorized foreign or alien insurer files any pleading in any proceeding against it, it shall either:
(A) deposit with the clerk of the court in which the proceeding is pending, cash or securities or file with such clerk a bond with good and sufficient sureties, to be approved by the court, in an amount to be fixed by the court sufficient to secure payment of any final judgment which may be rendered in the proceeding, . . . or,
(B) procure a license to do an insurance business in this state.
. . . .
(3) Nothing in paragraph one of this subsection is to be construed to prevent an unauthorized foreign or alien insurer from filing a motion to set aside service made in the manner provided in paragraph two or three of subsection (b) hereon on the ground (i) that such unauthorized insurer had not done any act enumerated in paragraph one of subsection (b) of this section, ...

[2] *Morgan v. Amer. Risk Management, Inc.*, 1990 U.S. Dist. LEXIS 9037 (S.D.N.Y.) *18.

[3] 2017 Bankr. LEXIS 1586*7.

[4] *Id. at *20.*

[5] 1990 U.S. Dist. LEXIS 9037 *24-5.

[6] 2013 U.S. Dist. LEXIS 110613 *14-5.

[7] 563 B.R. 756 at 782.

[8] 2003 U.S. Dist. LEXIS 6254 *11-2.

[9] 841 N.Y.S.2d 519 at 524.