

CORRECTED: What AIG Deal With Berkshire Means For Policyholders

Law360, New York (March 1, 2017, 1:47 PM EST) -- Late last month, insurance giant American International Group announced that it would pay roughly \$10 billion to Warren Buffet's Berkshire Hathaway to assume certain of AIG's long-term risks under U.S. insurance policies written years, and in many cases, decades ago. From the parties' perspective, the deal is a win-win: AIG will reduce its outstanding risks, while Berkshire Hathaway will immediately increase its coffers by \$10 billion on the promise that someday in the future it may have to pay as much as \$20 billion toward AIG claims.

For AIG policyholders and the claimants who sue them, however, the consequences of the deal carry no such promised benefits. Instead, they may find their claims complicated and payments delayed as they become the latest group of insureds to face Berkshire Hathaway's attempt to maximize the policy "float" — the cash generated by the payment of reinsurance premiums today which will not be returned in the form of claim payments until years later, if ever.

Indeed, for the past several years, Warren Buffett and his companies have built a business model around the acquisition and preservation of float, particularly through the activities of reinsurer National Indemnity, the Berkshire-owned reinsurer at the center of the AIG deal. Indeed, in a 2009 letter to Berkshire Hathaway shareholders, Buffett touted the success of these efforts: "Our float has grown from \$16 million in 1967, when we entered the business, to \$62 billion at the end of 2009." By September of last year, that amount had reached \$91 billion, a figure which the AIG deal will increase by another \$10 billion. That float presents a ready source of cash for funding other Berkshire ventures and investments until and unless it is distributed as claim payments.

But that benefit for Berkshire comes at a cost for policyholders. To a certain extent, float is a natural byproduct of long-tail insurance, given the months or years between the time premiums are paid and claims arise under such policies. But Berkshire and National Indemnity have turned the preservation and extension of that naturally occurring float into an art form. In particular, they have actively sought to extend the float in connection with asbestos claims — the quintessential "long-tail" liability — by, among other things, delaying and litigating both underlying claims and coverage claims that insurers historically would have paid or settled. That increases not only the time the company holds the money, but also the ultimate amount of money it keeps. Even better for Berkshire, since any delay in or denial of



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payment will likely be attributed to the insurance company, rather than the reinsurer, the public relations costs of those efforts are minimal.

Those objectives are easier to achieve when the Berkshire reinsurer has the ability to control the amount and timing of claim payments. Accordingly, insurers who purchase reinsurance from Berkshire companies have in the past been required to cede control of claims handling and coverage litigation to National Indemnity and its claims arm, Resolute Management. In particular, Resolute has assumed full authority and control for such standard insurance company tasks as:

- Commencing, conducting, defending, pursuing prosecuting, settling, appealing or compromising claims and litigation filed by policyholders;
- Developing and implementing all of the strategic decisions in addressing issues raised by policyholders;
- Hiring the attorneys to represent the insurers in coverage litigation with their policyholders;
- Deciding whether, and for what amount, the insurer will resolve claims asserted against it by policyholders;
- Deciding whether, and to what extent, the insurer will assert contribution or subrogation rights against other insurance companies.

Resolute uses the broad authority ceded to it by the insurance companies to delay claims and underlying actions, outlasting policyholders and claimants and often forcing them to settle claims for far less than their true value. Even where the insurer has not ceded that broad control over claims decisions to Resolute, National Indemnity's financial "clout" as reinsurer for the claim gives it substantial influence over the way the coverage claim is handled, litigated and settled. That tactic has not gone unnoticed by policyholders, who in turn have tried to hold Resolute directly liable for the damages their delays have caused.

Resolute typically responds to those direct claims with the practical fiction that it is acting as the mere agent of the insurance companies, and thus cannot be sued independently for actions within the scope of that agency.[1] More recently, however, policyholders have begun to plead specifically that Resolute has used the unfettered claims handling authority it demanded from insurance companies not in service of its supposed "principals" — the reinsured companies — but for the benefit of National Indemnity and Berkshire. They also have alleged that in furtherance of that objective, Resolute, far from processing or handling claims, has actually interfered in the contractual relationship between insurer and insured.

For example, in *Celanese Corp. v. OneBeacon American Insurance Co.*, No. 3:14-cv-3985-L, 2015 U.S. Dist. LEXIS 83917 (N.D. Tex. May 27, 2015), the policyholder alleged specifically that in taking full control over OneBeacon's asbestos claims, Resolute was not fulfilling any role as OneBeacon's agent, but was acting solely on behalf of the interests of its parent, National Indemnity. It further alleged that Resolute had "handled" claims under the OneBeacon policies with the sole purpose of delaying payment of millions of dollars by National Indemnity. As a result, Celanese claimed that Resolute had induced OneBeacon to breach the insurance policy contract for the sole benefit of Resolute and its owners and affiliates, including National Indemnity and Berkshire Hathaway. Based on those allegations, the court held that Resolute and OneBeacon could not preclude the possibility that the policyholder would be able to recover on its tortious interference claim against Resolute, either by proving that Resolute was not acting as an agent of the insurers or, alternatively, that it was acting solely to advance its own interests.[2]

Celanese highlights the problem that long-tail policyholders face as a result of the Berkshire desire to maximize float — and a way forward for combating that problem. As long as the only risk that either the original insurer or the Berkshire reinsurers face is the prospect of paying insurance proceeds that they were required to pay in the first place, the incentive for delay and obstruction of claims remains. Policyholders need to be able to raise the stakes by creating a risk for Resolute or the insurance companies that they can be held liable for amounts in excess of the policy equal to or greater than the economic benefits of the float. For Resolute or the other Berkshire companies, claims of tortious interference with the original insurance policies hold that promise.

Where Resolute has not taken unfettered control for all claims handling decisions, policyholders can also up the ante by bringing bad faith claims against the insurance companies based on the improper delays of Resolute. Depending on the jurisdiction, such claims can allow the policyholder to recover from the insurance companies not only the damages it suffered from the bad faith claims handling by Resolute, but also the attorneys' fees it spends in pursuing insurance coverage. Also, since they adopt the Resolute fiction that its claims handling tactics are undertaken by Resolute solely in its role as an agent of the insurance companies — and that the insurance companies are therefore liable for the resultant harm — pleading bad faith in the alternative with the Resolute-direct claims increases the likelihood that any question as to Resolute's status cannot itself derail the policyholder's recovery of damages beyond the policy proceeds. Most importantly, such claims may serve to drive a wedge between the insurers and their Berkshire-related reinsurers, and give the insurers an incentive to back policyholder claims that Resolute acted not as the insurance companies' claims-handling agent, but for the benefit and at the behest of Berkshire and National Indemnity.

Finally, the "float" game highlights again the need for courts to counter the financial incentives — and ability — of insurers and reinsurers alike to complicate and delay resolution of significant coverage claims in order to maximize the insurers' ability to profit from retaining insurance proceeds they do not seriously dispute are due and owing. To level the playing field, courts should allow policyholders greater access to damages, including exemplary and punitive damages, sufficient to outweigh the financial benefits of artificial delays designed to enhance the insurers' access to float.

CORRECTION: A previous version of this article incorrectly assumed that AIG would cede its claims handling and litigation authority to Resolute, a Berkshire Hathaway company. This article has been corrected to reflect updated analysis from the authors.

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DISCLOSURE: McKool Smith has handled matters adverse to AIG, Berkshire Hathaway, OneBeacon, Resolute Management, and National Liability & Fire Insurance Company, a member of the National Indemnity Company group, including representation of Celanese Corp. in a case discussed in this article, Celanese Corp. v. OneBeacon American Insurance Co.

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[1] See, e.g., OneBeacon American Insurance Co. v. Colgate-Palmolive Co., 123 A.D.3d 222 (1st Dep't

2014) (dismissing policyholder direct claims against Resolute on grounds that its actions were “within the scope of its duties on behalf of the principal.”)

[2] OneBeacon was decided in the context of the policyholder’s motion to remand the action to state court after Resolute and OneBeacon removed the action to federal court. Because Resolute’s inclusion as defendant destroyed diversity, Resolute and OneBeacon argued that the policyholder could not bring any viable claim directly against Resolute.

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