

Honorable Engagement

Contributed by Edward P. Krugman, Cahill Gordon & Reindel LLP

In *PMA Capital Insurance Co. v. Platinum Underwriters Bermuda, Ltd.*,¹ the district court vacated the award of three respected reinsurance arbitrators² because, in the court's view, the award rewrote the parties' contract instead of interpreting and enforcing it. The underlying dispute involved the applicability of a deficit carryforward clause that, if applicable, could have required a decade or more of ongoing accounting adjustments between the parties. The arbitrators cut the Gordian Knot by directing a single, lump-sum payment from the cedent to the reinsurer, after which both parties' obligations under the clause would permanently end.

Anyone with experience in reinsurance would likely recognize the award as a practical solution to a potentially intractable problem. With the parties already at loggerheads on the deficit in 2009, how could they be expected to deal with the issue through 2021, as the clause arguably required? The reinsurer was actually asking the panel to retain jurisdiction through the years "to supervise this ongoing relationship!"³ A better choice, the panel likely concluded, would be to monetize the dispute now and let everyone get on with their lives.

The court, however, felt differently. The award was "completely irrational," it held, because the arbitrators "simply took the [deficit p]rovision" out of the contract. The lump-sum payment was further irrational because no contract term authorized it. "The Panel," the court held, "sought to 'balance' one irrational decision . . . with another."⁴ The court reached this result notwithstanding the acknowledged presence in the contract of an "honorable engagement" clause, which on its face

- told the arbitrators to interpret the reinsurance contract "as an honorable engagement and not merely as a legal obligation,"
- relieved the arbitrators of "all judicial formalities" and permitted them to "abstain from following the strict rules of law," and
- empowered the arbitrators to "make their award with a view to effecting the general purpose of the Agreement in a reasonable manner rather than in accordance with the literal interpretation of the language."⁵

The thesis of this article is not so much that the court in *Platinum Re* was wrong but that its entire approach to the powers of arbitrators under a broad "honorable engagement" clause⁶ was misguided. Arbitration under such a clause is not merely adjudication in a non-judicial forum; it is, in the truest sense of the phrase, alternative *dispute resolution*. So long as a businessperson would regard the award

© 2010 Bloomberg Finance L.P. All rights reserved. Originally published by Bloomberg Finance L.P. in the Vol. 4, No. 8 edition of the Bloomberg Law Reports—Insurance Law. Reprinted with permission. Bloomberg Law Reports[®] is a registered trademark and service mark of Bloomberg Finance L.P.

The discussions set forth in this report are for informational purposes only. They do not take into account the qualifications, exceptions and other considerations that may be relevant to particular situations. These discussions should not be construed as legal advice, which has to be addressed to particular facts and circumstances involved in any given situation. Any tax information contained in this report is not intended to be used, and cannot be used, for purposes of avoiding penalties imposed under the United States Internal Revenue Code. The opinions expressed are those of the author. Bloomberg Finance L.P. and its affiliated entities do not take responsibility for the content contained in this report and do not make any representation or warranty as to its completeness or accuracy.

as within the range of fair resolutions of the parties' dispute as a whole, it should not be subject to vacatur as substantively inappropriate.⁷ This view is derived not so much from the caselaw on honorable engagement, which tends not to plow terribly deeply, but from an examination of the history of the clause and the commercial context in which it arises.

The Historical Meaning of "Honorable Engagement"

The phrase "honourable engagement" goes back at least to the late eighteenth century in England. Its initial uses, however, were not in the arbitration context. Rather, the phrase referred to "obligations" — such as gambling debts⁸ or promises to make (or not revoke) a will in favor of another⁹ — that could not always be enforced by a court.¹⁰ A gentleman did not refuse to pay his wagers, or decline to leave a promised bequest, but if he was so crass as to do so, the courts could not intervene.

The usage appeared in insurance cases as well. In determining that a party had not satisfied an obligation to procure insurance, Cockburn C.J. said:

[S]lips were actually signed and issued, and this, according to the practice of insurance Companies and underwriters, is an honourable engagement, which never fails to be fulfilled when a proper claim is made. But when I ask myself whether such an engagement by the underwriter amounts to an insurance according to the terms of the agreement, I must say that it does not.¹¹

Historically, it was no small thing for a man "to incur the odium and consequences of repudiating his honourable engagements."¹² Not all obligations were enforced by courts of law; many — including many of the most important ones — were enforced by social pressure.

The concept of social pressure is central to an understanding of why and how the phrase "honorable engagement" first made its way into reinsurance arbitration clauses. The earliest located honorable engagement clause appears in a 1905 treaty between Aetna Indemnity and Munich Re, which instructed the arbitrators to "interpret the present contract rather as an honorable engagement than as a merely legal obligation."¹³ The treaty was written two decades before passage of the Federal Arbitration Act,¹⁴ at a time when pre-dispute arbitration clauses were not enforceable in most United States jurisdictions, including Connecticut. Such clauses were said to "oust the court of jurisdiction."¹⁵ The honorable engagement provision of the treaty was therefore not enforceable. Why then did Aetna and Munich Re include it?

The answer was most likely social pressure: the parties expected that they and their counterparties would behave honorably and would arbitrate as they had agreed to do. If they did not, they would find it difficult to do business in the future. And once the parties bowed to social pressure and actually submitted a case to the arbitrators, the resulting award *would* be enforceable — *that* rule had been settled in the United States at least since Justice Story's decision in *Kleine v. Catara*.¹⁶

Justice Story also made clear that, if requested by the parties, the arbitrators

are not bound to award upon the mere dry principles of law applicable to the case before them. They may decide upon principles of equity and good conscience, and may make their award *ex aequo et bono*.¹⁷

The Latin phrase "*ex aequo et bono*" means "according to what is equitable and good."¹⁸ It harkens back to the medieval Law Merchant, to merchant judges who "resolved disputes among itinerant merchants at regional fairs, markets, towns, and ports — outside the jurisdiction of courts and judges who administered the law of local princes."¹⁹ The ideal was fairness and practicality, so that itinerant merchants could receive expeditious justice without having to delay their journey. "In essence, the purpose of *ex aequo et bono* decision[s] was to use an informal, time and cost effective process so as to arrive at results that were 'fair' to the parties, not according to the law of the land, but in light of merchant usage and party practice."²⁰

All this sounds very much like the mandate of the broad honorable engagement clause, which directs the arbitrators to "make their award with a view to effecting the general purpose of the Agreement in a reasonable manner rather than in accordance with the literal interpretation of the language." So does the French term "*amiables compositeurs*," which appears in the very first reinsurance arbitration clause I have located. An 1850 treaty between a French cedent and an Italian reinsurer states:

Les trois arbitres seront dispensés de toutes formalités judiciaires et pourront s'abstenir de suivre du règlement du droit. Ils jugeront en dernier ressort sans appel et comme *amiables compositeurs*.²¹

What, exactly, were these companies doing when they provided for arbitration by "*amiables compositeurs*"? They were not pulling words out of the air; the concept is an ancient one. In 1272, Bishop Barthélémy and the elders of Cahors appointed "arbitres et *amiables compositeurs*" to settle their disputes regarding local customs.²² In 1334, Philippe de Valois was appointed "judge, arbitrator, and *amiable compositeur*" to resolve a dispute between the Duke of Brabant and various German princes.²³ International disputes are not always (a cynic would say not often) resolved in accordance with the strict tenets of international law, even if (cynic again) there is such a thing. Mostly, they are handled by finding a landing place that both sides can accept as fair, and the role of the "*amiable compositeur*" in the law of nations is to find such a landing place.²⁴

Nor was the role of *amiable compositeur* limited to disputes between nations. By the early nineteenth century it was well established in French commercial cases that parties could voluntarily submit their disputes to arbitrators "comme *amiable-compositeurs*,"²⁵ and it was being argued strenuously that they could do the same in pre-dispute arbitration clauses.²⁶ Arbitrators proceeding as *amiable compositeurs* could "dispense with observing the strict rules of law, so that they rule solely by following their conscience and the impulse of natural equity."²⁷ What the parties to the 1850 reinsurance treaty were doing, therefore, was providing a regime whereby their disputes would be resolved in a fair and commonsense business manner, not subject to what they might well have seen as artificial legal rules and requirements.

"Rewriting" the Parties' Agreement

With this historical background, we turn to the authority of a panel subject to an honorable engagement clause, or with the powers of *amiables compositeurs*, to "rewrite" the contract in the course of resolving the dispute. Is it possible? As a verbal matter, it should be: the core meaning of "*amiable compositeur*" is one who effects a settlement,²⁸ and the panel in *Platinum Re* did nothing more or less than effect a full and final settlement of the deficit issue.

These issues are addressed in a recent Québec case²⁹ that is conceptually very similar to *Platinum Re*. One family faction had bought another out of the family business, with a payout linked by a formula to the ongoing profitability of the business. The arbitration clause in the buyout agreement authorized the arbitrator to act as *amiable compositeur*. The business turned out to be highly profitable but there was no payout, principally because the formula did not adequately integrate future acquisitions into the calculation of "available funds." The *amiable compositeur* struck two provisions from the formula, determining that the definition in the formula "leads to a result neither of the parties had foreseen," that "the formula may be amended to ensure that the intent of the parties is fulfilled," and that the powers of *amiable compositeur* permitted him to do so.³⁰ "The point," he said, "is not to ignore the contract but to make it possible to fulfil[] the intent of the parties in concrete terms."³¹

The trial court, however, vacated the award, and the Court of Appeal affirmed. The opinion of the Court of Appeal contains a scholarly exegesis of the powers of the *amiable compositeur*, but ultimately the decision turned on statutory grounds. Article 944.10 of the Québec Code of Civil Procedure, which is based on the UNCITRAL Model Arbitration Law,³² gives effect to *amiable compositeur* designations but expressly states that the arbitrators "shall in all cases decide according to the stipulations of the contract."³³ The trial court and the Court of Appeal agreed that under prior law, which simply recognized the existence of the arbitrator *amiable compositeur*, the award would have been above reproach,³⁴ but the express adherence requirement of Article 944.10 was now controlling.³⁵ The parties *could* free the arbitrator from the adherence obligation,³⁶ but it would require explicit words to do so, and simply designating the arbitrator an *amiable compositeur* was not sufficient.³⁷

There is room to question whether the Court of Appeal was right to read Article 944.10 so restrictively,³⁸ but for our purposes the two key principles from its opinion are that (a) but for Article 944.10 the power of *amiable composition* **does** encompass some power to rewrite the parties' agreement, and (b) here, as elsewhere in the arbitration world, the parties are the masters of their own fate and *can* give the arbitrators the power to rewrite if they wish to do so.

With these principles in mind, we now leave Québec and *amiable composition* and return to the United States and honorable engagement. Under broad arbitration clauses, arbitrators in the United States probably do have the power to reform the parties' contract,³⁹ as at least three reinsurance arbitration cases have expressly held.⁴⁰ What is perhaps less clear is the extent to which such arbitral reformation must have some relationship to the classical (and stringent) requirements for reformation in equity. The New York Court of Appeals has gone back and forth on

this subject;⁴¹ the California Supreme Court has expressly held that some rewriting *is* permissible, at least as a remedy for breach.⁴² On the other hand, there has never been any dispute that arbitrators *can* write new clauses into the contract if the parties ask them to do so. The more restrictive of the New York decisions recognized as much,⁴³ and "interest" arbitration clauses in labor cases direct the arbitrator to write a new contract going forward when the parties reach impasse on mandatory subjects of collective bargaining.⁴⁴

So what does all this mean for the honorable engagement clause and the issue that confronted the court in *Platinum Re*? From our discussion above, the issue is not whether the parties *could* give the arbitrators the power to issue the ruling they did but rather whether they *did* give them that power. I think it is clear that they did. The clause not only expressly frees the arbitrators from adhering to the literal terms of the contract; it instructs them to focus on the "general purpose of the agreement" and to effect that general purpose "in a reasonable manner." Had the dueling factions of the Coderre family included such a provision in their arbitration agreement, the award of the *amiable compositeur* would surely have been upheld. With the clause present in *Platinum Re*, the district court's decision was simply wrong. The issue in *Platinum Re* was *timing* of payment — there was no dispute that the deficit would have been payable in cash in 2021; the arbitrators simply held that it should be paid now, so the parties would not have to confront the same issue over and over for the next 12 years. Even in a finite reinsurance contract, where cash flows have heightened importance, I do not think such a decision can be said to violate the "general purpose" of the contract.⁴⁵

Applying the Honorable Engagement Clause in Its Historical Context: Enforcing Behavioral Norms

The argument from the "general purpose" portion of the honorable engagement clause is sufficient to resolve the question posed by *Platinum Re*, but it does not fully capture the true meaning of the clause in its historical context. The broad honorable engagement clause has three sentences, but most of the cases that actually examine the clause deal only with the second sentence (freeing the arbitrators from judicial formality and the need to follow the law) or, the third (permitting the arbitrators to enforce the "general purpose" of the contract, which may differ from the literal terms the parties wrote down). These two sentences are important,⁴⁶ but they are not the whole clause.

The first sentence of the clause is worth restating here, because it is that which gives the clause its name. The first sentence says:

The arbitrators will interpret this agreement as an honorable engagement and not merely as a legal obligation.⁴⁷

That sentence has inherent content. It could stand by itself as, indeed, for many years it did. The second and third sentences of the clause *add* to the concept of honorable engagement, but they do not *define* it. The clause in the 1905 Aetna-Munich Re treaty, after all, had *only* the honorable engagement language; it did not contain either of the two additional provisions.⁴⁸

The first sentence of the honorable engagement clause is fundamentally different from the other two "equity" clauses, *ex aequo et bono* and *amiable compositeur*.⁴⁹ The latter two clauses speak only of the powers of the arbitrators — to effect a friendly composition, or to rule according to equity and justice. Telling the arbitrators to interpret the underlying contract "as an honorable engagement and not merely as a legal agreement," however, goes beyond that. It speaks not to the arbitrators' powers but rather to the underlying contract itself. It is the *underlying contract* that is the "honorable engagement," and the parties to that honorable engagement are expected to behave like gentlemen, to do the right thing. If they do *not* do the right thing, the arbitrators can do it for them. The first edition of Thompson's *Reinsurance*, published in 1942, put it this way:

It is the general provision that the reinsurance treaty shall be interpreted as an *honorable agreement* rather than a legal contract. The whole underlying purpose of the arbitration clause is to provide a means to solve difficulties in the way gentlemen with good faith work out their troubles without litigation.⁵⁰

Accordingly, in resolving disputes under an honorable engagement clause, the arbitrators are not merely dealing with a contract but are enforcing standards of behavior. A court that does not give them the flexibility to do so is not enforcing the arbitration clause the parties agreed to.

The Limits of Discretion and the Role of Judicial Review

So is the discretion of a panel of reinsurance arbitrators operating under an honorable engagement clause truly limitless? The short answer is "no," because Section 10 of the FAA remains on the books. With the choice of the umpire in reinsurance arbitrations frequently the result of a coin-toss, there is much to be said for keeping *some* substantive judicial role, however minimal it might be. Fundamental fairness in process is still a prerequisite to an enforceable award.

Process is one thing. What about substantive oversight? If it is truly unacceptable that there be no review whatsoever of the content of the award (once, of course, it is determined that the process was fair and the award is within the scope of the submission),⁵¹ one should treat seriously the verbal formulas that have grown up to describe the scope of that oversight. It may be that there is no better formulation than the "completely irrational" standard that Judge Diamond purported to apply in *Platinum Re*, but rationality must be judged in terms of what the parties committed to in their arbitration clause; "completely irrational" should not be used simply as an epithet.

In entering into a reinsurance contract with a broad honorable engagement clause, the parties are binding themselves to a standard of behavior that goes beyond the express provisions of the contract. They are also agreeing to have their behavior judged by persons with expertise in their industry, and they are acknowledging that disputes may be resolved in accordance with what the experts think is reasonable, which may *not* be the result if the contract is simply enforced in accordance with its literal terms. The rationality of a reinsurance arbitration award, then, must be judged by a business standard, not a legal one. And under any business standard of rationality, the award in *Platinum Re* passes muster. It is well within the range of

how, to use Thompson's words, "gentlemen with good faith" would have "work[ed] out their troubles without litigation."⁵² Using any more restrictive test than that does not give effect to the words the parties used when they described their arrangement as an "honorable engagement."

But courts cannot apply even deferential standards of review without something to review. Arbitrators who apply business standards of behavior should say so. The ongoing discussion about "reasoned awards" in the industry⁵³ must in this circumstance give way to the need to ensure that at least some level of judicial review — or, at least, judicial protection of parties against purely arbitrary behavior on the part of arbitrators — is available. The concept of a statement of reasons for discretionary decisionmaking is a familiar one from the Administrative Procedure Act;⁵⁴ it is also embodied in various international arbitration codes.⁵⁵ It is *not* traditional in arbitration in the United States, nor need it be in the usual case, but if an arbitrator is going to go beyond the parties' underlying contract, he owes it to the parties to say what he has done and why. This is, in a sense, enforcing the same standard of forthrightness on the arbitrator that the arbitrator is enforcing on the parties.

Both the usefulness of a statement of reasons and the potential need for some level of detail in the statement may be illustrated in the 2005 case *United States Life Insurance Co. v. Insurance Commissioner of the State of California*⁵⁶ which, though unreported, has received a fair amount of attention because of the amount of money involved.⁵⁷ A life reinsurer that had assumed a very large book of workers' compensation carve-out business claimed that the cedents had not made full disclosure of actuarial information in their files at the time of placement. The arbitration panel determined that the cedents "should have acted in a more open and forthright manner," but it did not then go on to rescind the treaty. Rather, it simply reduced the reinsurer's participation by 10 percent and directed that the ongoing relationship should continue.⁵⁸

The panel's one-line statement of reasons indicates that this was a classic use of the honorable engagement clause. Ceding companies insert honorable engagement language in treaty arbitration clauses in large part to mitigate the strict rule of law that a reinsurance contract can be rescinded for even innocent non-disclosure.⁵⁹ Arbitrators in the United States are widely believed to take a jaundiced view of rescission claims and to be reluctant to give reinsurers windfalls when ceded business turns out to be unprofitable. In this view, the arbitration panel behaved exactly as the parties could have expected at the time they entered into the treaty.

There is another way to look at this, however. *U.S. Life* came after a period in which life reinsurers, flush with cash, had jumped with both feet into the market for workers' compensation carve-out reinsurance. The life companies had had little experience with casualty business. Many in the industry regarded them as paradigmatic "innocent capacity." When carve-out losses turned out to be enormous, the life companies decided to cut and run — or so many in the industry thought. In choosing not to order rescission, did the *U.S. Life* panel simply conclude that the reinsurer should have done a better job of its own at the time of placement? Or did it perhaps implement a prejudice that life reinsurers had an unending appetite for premium but no stomach for losses? There is a fine line between judging the behavior of a specific reinsurer in a specific instance and applying a prejudice against

a class of reinsurers as a whole. The Ninth Circuit was able to divine a basis for the 10 percent reduction by taking the ratio of the low end of the reserve understatement to the overall size of the book of business,⁶⁰ but a court uncomfortable with the result might well have wanted a more fulsome statement of reasons from the arbitrators so that it could ensure that they were fairly exercising the discretion the parties had given them.⁶¹

All of which brings us back once again to *Platinum Re*. It may be obvious to me and to other reinsurance practitioners why the panel did what it did, but it was not obvious to Judge Diamond, who expressed frustration that the arbitrators had not explained their reasoning.⁶² Who knows whether, as was commonly speculated in hallway conversations at the ARIAS 2010 Spring meeting in San Diego, the award in *Platinum Re* would have been upheld had the panel explained itself, but it is clear at a minimum that the award could not then have been described as "completely irrational." Far from being irrational, the *Platinum Re* award is comfortably within the range of how parties to an honorable engagement can be made to compose their disputes.

Conclusion

The second and third sentences of the broad honorable engagement clause are, as a technical matter, sufficient to authorize the arbitrators to modify the terms of the underlying contract if that is necessary to effect a fair resolution of the dispute in which the parties find themselves. The first sentence provides the context in which those powers are to be exercised. Parties who place an honorable engagement clause in their reinsurance contract are not only talking to the arbitrators; they are talking to themselves. They are affirmatively invoking — and agreeing to adhere to — a standard of behavior that, historically, has been characterized by doing the right thing, by avoiding overreaching, and (to use a modern description of an ancient concept) by looking for win-win. Litigation is bad; settlement is good. Leave something on the table; you'll need it the next time. So long as an award under an honorable engagement clause can be described as a fair business resolution of the dispute before the arbitrators, it is entitled to be enforced.

Edward P. Krugman is a partner in the litigation and insurance practice of Cahill Gordon & Reindel LLP, litigating and arbitrating insurance-related matters throughout the country and internationally. He has litigated RICO cases since before Sedima, and for 25 years he has represented ceding companies and reinsurers in contested reinsurance matters, often involving massive financial exposure. Currently, he litigates and provides strategic advice on virtually every aspect of the business of insurance and the business of insurers. The author acknowledges with gratitude the research assistance of Kevin M.W. Jacobs.

¹ 659 F. Supp. 2d 631 (E.D. Pa. 2009), *appeal docketed*, No. 09-3963 (3d Cir. Oct. 19, 2009).

² The arbitration panel consisted of Paul Dassenko (umpire), David Thirkill, and Peter Gentile. *Memorandum in Support of Motion to Confirm* in *Id.*, at 2. According to their biographies on the ARIAS-US website, www.arias-us.org, they have between them sat as arbitrators or umpires in approximately 350 reinsurance arbitrations.

³ *PMA*, 659 F. Supp. 2d at 638.

⁴ *Id.* at 639.

⁵ *Id.* at 636.

⁶ There are various forms of "honorable engagement" clause in use. Some merely relieve the arbitrators from judicial formality and the need to follow strict rules of law; others, such as the one in *Platinum Re*, go further and permit the arbitrators to "effect[] the general purpose of the Agreement," freeing them from adherence to "the literal interpretation of the language" of the contract. *Compare, e.g.,* BRMA Clause 6C with, *e.g.,* BRMA Clause 6E (both available at <http://www.brma.org/frommembers/contractword/Arbitration%20BRMA%206A-T.doc>); *see also* Insurance and Reinsurance Arbitration Task Force, *Procedures for Resolution of U.S. Insurance and Reinsurance Disputes* § 14.3 (2009 ed.; available at <http://www.arbitrationtaskforce.org/procedures.html> (freedom from rules of law and evidence only). Because this article explores what I believe to be an inappropriate judicial limitation on the parties' freedom of contract, it takes as its text the broad form of the clause.

⁷ This is not to say, of course, that the award would be immune to attack on other grounds. The essentially procedural bases for vacating an award under Section 10 of the Federal Arbitration Act, 9 U.S.C. § 10, meant to assure that the *process* leading to the award was fundamentally fair, would still remain.

⁸ *See, e.g., Moon v. Durden*, 2 Ex. 22, 154 E.R. 389 (1848).

⁹ The leading case is the 18th century case of *Lord Walpole v. Lord Orford*, 3 Ves. 402 (1797), in which (as described in a New York case a century later):

The circumstances in Lord Walpole's Case were so strong as to provoke the comment by the Lord Chancellor, that the fact of some agreement was to be implied and that it was to be considered as an honorable engagement on Lord Orford's part. But he said that he could "not direct the execution of an honorable engagement."

Edson v. Parsons, 155 N.Y. 555, 569 (1898)

¹⁰ "Not always" is the operative phrase. It is one of the joys of historical legal research that one comes across lines of cases but dimly remembered from law school — here, the development of the doctrine in equity that solemn agreements to make a will *can* be enforced if sufficiently definite. *See, e.g., Edson v. Parsons, supra; In re Goodchild*, [1997] 3 All E.R. 63 (C.A.). Discussion of that doctrine, however, is for another article.

¹¹ *Parry v. Great Ship Co.*, (1864) 4 Best & Smith 556, 563-64 (K.B.). *See also Maspons y Hermano v. Mildred, Goyeneche & Co.*, (1882) 9 Q.B.D. 530, 537 (C.A.) (argument of counsel) ("The underwriters' slip is not a mere honourable engagement of the underwriters, but it can be stamped and produced in evidence as a contract."), *aff'd*, (1883) 8 App. Cas. 874 (H.L.).

¹² *Read v. Anderson*, (1882) 10 Q.B.D. 100, 109.

¹³ *MacDonald v. Aetna Indemnity Co.*, 92 A. 154, 155-56 (Conn. 1914). The treaty was said to have been a renewal of one in existence for several years prior to 1905, but the terms of the earlier iterations were not given.

¹⁴ Act of Feb. 12, 1925, c.213, 43 Stat. 883 (codified as amended as Title 9, United States Code).

¹⁵ *See, e.g., MacDonald v. Aetna*, 92 A. at 160 (Wheeler, J., dissenting). The core purpose of Federal Arbitration Act was to reverse this common law rule.

¹⁶ 14 F. Cas. 732 (C.C.D. Mass. 1814) (No. 7,869); *accord, e.g., Chicago M. & St. P. Ry. v. Stewart*, 19 F. 5, 10 (C.C.D. Minn. 1883) (Nelson, J. concurring).

¹⁷ *Kleine*, 14 F. Cas. at 735.

¹⁸ Black's Law Dictionary 641 (9th ed. 2009).

¹⁹ Leon Trakman, *Ex Aequo et Bono: De-mystifying an Ancient Concept*, 8 Chi. J. Int'l Law 621, 629 (2008).

²⁰ *Id.* at 630.

²¹ Treaty of Reinsurance between Riunione Adriatica di Sicurtà and La Compagnie d'Assurances Contre l'Incendie La France (1850), reproduced in C.E. Golding, *A History of Reinsurance with Sidelights on Insurance*, App. I (private, 1927). Translated, the text reads:

The three arbitrators shall dispense with all judicial formalities and may abstain from following strict rules of law. Their decision shall be final and not subject to appeal [literally: they shall judge in a last-resort capacity and without appeal] and they shall act as "amiables compositeurs."

²² Article on Cahors, in the French *Wikipedia*, <http://fr.m.wikipedia.org/wiki/Cahors> (visited 7/15/2010).

²³ E. Nys, *Le Droit de la Guerre et Les Précurseurs de Grotius* 34 (Thürner & Co., London, 1882).

²⁴ Nearly 600 years after Philippe de Valois prevented a war in Germany, King George V acted as *amiable compositeur* of an expropriation claim by the United States, on behalf of its nationals, against Chile. See *In re McCall's Estate*, 28 Pa. D. 433 (Pa. Orph. 1919). The award appears at 5 Am. J. Int'l Law 1079 (1911).

²⁵ 2 M. Goubeau de la Bilennerie, *Traité Général de L'Arbitrage en Matière Civile et Commerciale* 336-47 (Rénard, Paris, 1827).

²⁶ *Id.* at 348-55.

²⁷ *Id.* at 335 (translation mine).

²⁸ This is obvious both from the history of the phrase in connection with disputes between sovereigns and from the use of the word "*compositeur*" — one who effects a composition. Although in current usage "composition" mostly relates to an agreement with creditors in a non-bankruptcy workout, see Black's Law Dictionary (8th ed. 2004), the original meaning goes back to the old Anglo-Saxon practice of paying an injured party to prevent him from seeking physical vengeance against the wrongdoer, see R. Pound, *The Ideal Element in Law*, *Glossary* (Liberty Fund ed. 2002). When parties settle litigation, they are said to "compose their differences." *E.g.*, *Harmon v. Dreher*, 17 S.C. Eq. 87, at *1 (1843); *Morgan v. New Orleans, M. & T.R.R.*, 17 F. Cas. 754, 755 (C.C.D. La. 1876) (No. 9,804); *Keedy v. Nally*, 63 Md. 311, 313 (1885). The official translation of "*amiable compositeur*" from Québécois French into English is "mediator," see *Coderre v. Michaud*, [2008] R.J.Q. 888 (Can.), ¶¶ 49, 62, which is to be understood as a person with the power to impose a settlement, not merely facilitate one.

²⁹ *Coderre v. Michaud*, [2008] R.J.Q. 888 (Can.).

³⁰ Award in *Coderre*, *supra* note 29, ¶¶ 56, 60-61, 65, quoted in *Coderre* at ¶¶ 17, 18.

³¹ *Id.* at ¶ 65.

³² United Nations Comm'n on Int'l Trade Law, *UCITRAL Model Law on International Commercial Arbitration* (1985 & 2006) ("Model Law"), available at http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf. Article 28(3), (4) of the Model Law provides:

(3) The arbitral tribunal shall decide *ex aequo et bono* or as *amiable compositeur* only if the parties have expressly authorized it to do so.

(4) In all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of the trade applicable to the transaction.

A number of United States jurisdictions have adopted some or all of the Model Law, including Art. 28(3), (4). *E.g.*, Cal. Code Civ. Proc. § 1297.284; Fla. Stat. Ann. § 684.0039; 710 ILCS 30/25-5.

³³ Québec Code of Civil Procedure, art. 944.10, quoted in *Coderre*, *supra* note 29, at ¶ 48.

³⁴ *Coderre*, *supra* note 29, at ¶¶ 23, 53, 54.

³⁵ *Id.* at ¶¶ 53, 54, 87.

³⁶ *Id.* at ¶ 53.

³⁷ *Id.* at ¶ 87.

³⁸ See 2 G. Born, *International Commercial Arbitration* 2242 (Wolters Kluwer 2009) (emphasis added):

[I]t would be peculiar to concluded that an arbitrator sitting *ex aequo et bono* or in an *amiable composition* had no greater authority, for example, to reduce a penalty, or excuse non-performance, than an arbitrator applying national law. The better view, adopted by a majority of commentators and other authorities, is that *arbitrators may depart from the terms of the parties' contract in fashioning a fair and equitable result, provided that they do not rewrite the structure of the agreement.*

Of course, what constitutes "rewrit[ing] the structure of the agreement" could itself be the subject of endless debate.

³⁹ *E.g.*, *SCM Corp. v. Fisher Park Lane Co.*, 40 N.Y.2d 788, 792-94 (1976). *But see First Merit Realty Services, Inc. v. Amberly Square Apartments, L.P.*, 373 Ill. App. 3d 457 (2007); *Oklahoma Oncology & Hematology, P.C. v. US Oncology, Inc.*, 160 P.3d 936, 947 & n.22 (Okla. 2007).

⁴⁰ *American Home Assurance Co. v. American Fidelity & Casualty Co.*, 356 F.2d 690, 692 (2d Cir. 1966); *United States Life Insurance Co. v. Insurance Commissioner of the State of California*, 160 F. App'x. 559 (9th Cir. 2005); *Ohio Reinsurance Corp. v. British Nat'l Insurance Co.*, 587 F. Supp. 710 (S.D.N.Y. May 7, 1984).

⁴¹ In 1976 the Court said that it need not, that the arbitrator's discretion could encompass reformation-like remedies even if the only reason was that the arbitrator thought justice required such a result. *Fisher Park Lane*, 40 N.Y.2d at 793-94. *Contra*, *Oklahoma Oncology*, *supra* note 39. Four years later, however, the Court largely reversed course, suggesting that allowing an arbitrator to "rewrite" the agreement merely because it was now thought to be onerous, was impermissible without some indication that the agreement as written did not reflect the parties' true intent. *Bowmer v. Bowmer*, 50 N.Y.2d 288, 295-96 (1980). Judge Fuchsberg, who wrote for the Court in *Bowmer*, had dissented in *Fisher Park Lane*.

⁴² *Advanced Micro Devices, Inc. v. Intel Corp.*, 9 Cal. 4th 362, 382-83 (1994).

⁴³ *Bowmer*, 50 N.Y.2d at 295; *see, e.g., Egol v. Egol*, 118 A.D.2d 76, 81 (N.Y. App. Div. 1986), *aff'd*, 68 N.Y.2d 893 (1986).

⁴⁴ *E.g., IBEW, Local Union 545 v. Hope Electrical Corp.*, 380 F.3d 1084 (8th Cir. 2004); *Sheet Metal Workers Int'l Ass'n, Local 162 v. Jason Mfg., Inc.*, 900 F.2d 1392 (9th Cir. 1990).

⁴⁵ Or, to use Mr. Born's phrase, it does not "rewrite the structure of the agreement." *See supra* note 38. Most finite reinsurance contracts with experience accounts apply an interest rate to the profit or deficit in the account, and a review of the (redacted) appellate briefs in *Platinum Re* suggests that the contract there was no exception. Accordingly, payment of today's deficit today is more or less equivalent to payment of the deficit plus 12 years of interest 12 years from now. One of the arbitrators in *Platinum Re* had spent a number of years running a finite reinsurance business; the panel is unlikely to have gotten this point wrong.

⁴⁶ Among other things, it has been persuasively argued that freeing the arbitrators from following the law means that reinsurance arbitration awards cannot be reviewed for "manifest disregard" of the law. Lisman, *Honoring the Honorable Engagement Clause in Judicial Review of Arbitral Awards*, 14 ARIAS-US Quarterly, No. 2, at 11-16 (2007). It remains to be seen how these arguments play out in light of *Hall Street Assocs. v. Mattel, Inc.*, 552 U.S. 576 (2008), which held that parties cannot contract around the standards of review under section 10 of the FAA, and the Supreme Court's subsequent choice in *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758, 1768 n.3 (2010), to leave open whether "manifest disregard" survives *Hall Street* as, *inter alia*, "a judicial gloss on the enumerated grounds for vacatur set forth at 9 U.S.C. § 10" (so that, presumably, the standard is effectively statutory and cannot be contracted around).

For an example of a holding that parties cannot contract around statutory rights in the reinsurance arbitration context, *see Garamendi v. California Compensation Insurance Co.*, 2005 WL 3485747 (Cal.App. Jan. 20, 2006), which held that the provision of Cal.Ins.Code § 481(a)(1) for full return premium on rescission applies to reinsurance contracts and cannot be overridden by arbitrators, even arbitrators under an honorable engagement clause that frees them from following the strict rules of law.

⁴⁷ 659 F. Supp. 2d at 636; *see* Brief for Appellant at 6 (quoting full clause).

⁴⁸ *MacDonald*, 92 A. at 155-56. Neither (so far as one can tell from the decisions) did the clauses at issue in *North River Ins. Co. v. Walker*, 65 F.2d 116 (8th Cir. 1933), or *Pink v. Fidelity & Deposit Co.*, 15 F. Supp. 715 (S.D.N.Y. 1936). The clause in *Pacific Indemnity Co. v. Insurance Co. of North America*, 25 F.2d 930 (9th Cir. 1928), did relieve the parties of judicial formality and the need to follow the strict rules of law.

⁴⁹ The UNCITRAL Model Law formally addresses only the latter two clauses, but as the drafters of the 1996 English Arbitration Act recognized, the three clauses are very much of a piece. *Compare* Departmental Advisory Comm., 1996 Report on the Arbitration Bill ¶ 223 (*ex aequo* and *amiable compositeur* are "equity" clauses), *reprinted in* 13 *Arb'n Int'l* 275, 310 (1997) *with* Departmental Advisory Comm., 1997 Supplementary Report on the Arbitration Act 1996 ¶ 30 (honorable engagement clause reads as though it is an equity clause, although it has been given a restrictive interpretation in England), *reprinted in* 13 *Arb'n Int'l* 317, 323 (1997).

⁵⁰ K.R. Thompson, *Reinsurance* 94 (1st ed. 1942).

⁵¹ *See* 9 U.S.C. § 10(a)(4).

⁵² It also (and not coincidentally) fits within the type of amelioration of contractual strictures that courts and commentators have said that *amiables compositeurs* can do. Thus, payment of the deficit in cash was not contractually prohibited, as the court *Platinum Re* at times seemed to suggest; it just was not supposed to happen until 2021.

⁵³ The topic of "reasoned awards" has come up at virtually every ARIAS meeting for more than a decade. There is a suspicion among the lawyer members of ARIAS that some arbitrators (not the top arbitrators, who say — and are believed — that they will do whatever the parties want in this respect) do not like reasoned awards because they fear they will be less employable if their mental processes are exposed to review and analysis. More charitably, such arbitrators may simply be following Justice Story's comment, nearly 200 years ago, in a case in which the arbitrators *had* explained their reasoning:

Arbitrators may act with perfect equity between the parties, and yet may not always give good reasons for their decisions; and a disclosure of their reasons may often enable a party to take advantage of a slight mistake of law, which may have very little bearing on the merits. *Kleine v. Catara*, *supra* note 16, at 735.

⁵⁴ *E.g.*, *Dunlop v. Bachowski*, 421 U.S. 560, 571-73 (1975).

⁵⁵ *E.g.*, Model Law art. 31(2) ("The award shall state the reasons upon which it is based, unless the parties have agreed that no reasons are to be given . . ."); ICC Rules of Arbitration art. 25(2) ("The Award shall state the reasons upon which it is based.").

⁵⁶ *United States Life Insurance Co. v. Insurance Commissioner of the State of California*, 160 F. App'x 559 (9th Cir. 2005).

⁵⁷ My firm was involved in this case, but I was not — I was on the other side of an ethical screen. My discussion of the case here is derived solely from public sources, because that is all the information I have.

⁵⁸ 160 F. App'x. at **2.

⁵⁹ *E.g.*, *Gulf Insurance Co. v. Transatlantic Reinsurance Co.*, 69 A.D.3d 71, 95 (N.Y. App. Div. 2009); *Houston Casualty Co. v. Certain Underwriters*, 51 F. Supp. 2d 789, 802-03 (S.D.Tex. 1999).

⁶⁰ 160 F. App'x. at **3.

⁶¹ An amusing twist on the reasoned award debate in the honorable engagement/*amiable compositeur* context is the holding of France's highest court that (a) an *amiable compositeur* must consider equity and *may not* rule solely on the law and the contract, so that (b) the award is subject to being vacated unless the *amiable compositeur* makes it clear that he did in fact take equitable considerations into account. See Bouckaert & Dupeyré, *Insurance Arbitration and Amiable Composition* (Feb. 3, 2010), available at http://executiveview.com/knowledge_centre.php?id=11074. One can disagree with the conclusion that arbitrators cannot simply enforce the contract as written while still accepting the logic that an explanation of the award, however brief, can play a central role in assuring the parties, and a reviewing court, of the award's legitimacy.

⁶² 659 F. Supp. 2d at 639.