

Kluwer Arbitration Blog

Federal Court Upholds P&I Club's Coverage Determination as Valid, Binding ADR Decision

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The U.S. District Court for the Southern District of New York has enforced a P&I Club's internal claims appeal process as a legally binding alternative dispute resolution ("ADR") method, rejecting allegations brought by one of the Club's Members that the procedure was "fundamentally unfair." *TransAtlantic Lines LLC v. Am. Steamship Owners Mut. Prot. & Indemn. Ass'n, Inc.*, 2017 WL 2334995 (S.D.N.Y. May 30, 2017). The court's holding is a reminder that a coverage decision, rendered in connection with an ADR procedure voluntarily entered into by the parties, is not lightly set aside.

American Steamship Owners Mutual Protection and Indemnity Association ("American Steamship") is a non-profit, mutual protection and indemnity insurance association that provides marine insurance to its Members. American Steamship's claims handling and coverage determinations are carried out by its manager, Shipowners Claims Bureau, Inc. ("SCB"). Members can appeal a denial of coverage to American Steamship's Board of Directors, which is composed of the association's Members' officers and representatives. The appeal process does not permit oral argument. The Board is required to issue written decisions within six months, which are "intended to be final and binding." Further review of the Board's decision may take place in federal court under an "arbitrary and capricious standard."

One of American Steamship's Members, TransAtlantic Lines LLC ("TransAtlantic"), sought reimbursement from American Steamship for costs expended in litigation involving lost and damaged cargo. SCB allowed the claim in part, but denied it as to attorneys' fees TransAtlantic paid to a third party. TransAtlantic filed an appeal with American Steamship's Board. The appeal was fully briefed, and the Board issued a 22-page decision upholding the coverage determination.

TransAtlantic then sued American Steamship in the Southern District of New York. The threshold issue was the applicable standard of review. TransAtlantic sought de novo review of the Board's decision, and brought various tort and contract claims against American Steamship, rather than a single challenge to the Board's coverage determination. According to TransAtlantic, the ADR process was "fundamentally unfair" because: (i) the Board had a financial interest in the decision, rendering it impermissibly biased; (ii) the procedure permitting Board members (who are officers or representatives of other American Steamship Members) to act as an ADR panel violated American Steamship by-laws prohibiting directors from acting upon any claim in which they have an interest; (iii) it was "unlikely" that the Board provided meaningful consideration of the appeal because the claim was adjudicated at a regular Board meeting without oral argument; and (iv) the

Board members may not have taken an oath of impartiality and failed to disclose their financial or personal interests. TransAtlantic also argued that de novo review was appropriate because the Board's decision violated public policy.

The court rejected each of TransAtlantic's arguments. The court declined to apply a de novo standard of review, first noting that at least two Southern District of New York decisions have treated American Steamship's Board hearings as ADR proceedings that are subject to a deferential standard of review. See *Progress Bulk Carriers v. Am. S.S. Owners Mut. Prot. & Indem. Ass'n, Inc.*, 939 F. Supp. 2d 422 (S.D.N.Y. 2013) (Magistrate's Decision and Order), *aff'd*, 2 F. Supp. 3d 499 (S.D.N.Y. 2014). The court agreed with these prior rulings, reasoning that "American Steamship's hearings bear all the hallmarks of a voluntary ADR proceeding." The court explained that the agreed-to rules at issue: (i) refer to the Board's hearings as "adjudications;" (ii) provide that the Board's decisions are "intended to be final and binding;" and (iii) allow for review in federal court only under an "arbitrary and capricious" standard of review.

On the issue of whether the hearing itself was fundamentally unfair, the court rejected this argument, reasoning that: (i) any supposed bias was inherent in the ADR process agreed to by TransAtlantic when it joined American Steamship; (ii) the by-laws only disqualified Members from presiding over claims involving their own companies, which was not the situation here; (iii) there was no factual support for the allegation that the Board did not meaningfully consider the appeal, and the fact that the Board issued a 22-page decision one month after hearing the appeal "strongly suggest[ed] that the Board's consideration was, if anything, conscientious and thorough;" and (iv) there was no requirement in the agreement (which TransAtlantic voluntarily entered into) for the Board to take an oath of impartiality or disclose financial or personal interests. The court also found that TransAtlantic was aware of the "unfair" aspects of the hearing process, but failed to raise any objections before the Board. This failure to object, according to the court, was another reason why the "fundamental fairness" argument failed.

As to TransAtlantic's argument that the ADR decision should be reviewed de novo because it violated public policy, the court, again, disagreed. The court found that TransAtlantic had not satisfied either element of the two-prong test under New York law to determine whether the ADR decision violated public policy. Specifically, TransAtlantic had pointed to no statute prohibiting the use of ADR for disputes of this nature, and no evidence that the award violated a "well-defined constitutional, statutory, or common law" of New York state.

TransAtlantic also requested to defer ruling on the summary judgment motion to permit discovery into the alleged unfairness of the Board's consideration of the appeal. This request was denied. Citing the discretionary standard to be applied, the court noted that, in post-ADR proceedings, discovery is available only in limited circumstances and that, in order to take discovery of the ADR panel itself, a litigant must present "clear evidence of impropriety," such as bias or corruption. Here, discovery was not allowed because, as the court previously determined, there was no colorable argument of impermissible bias. The court stated: "Having agreed to the challenged features ahead of time, TransAtlantic cannot now take discovery into whether they were unfair."

Finally, having concluded that the correct standard of review was the more deferential "arbitrary and capricious" standard set forth in American Steamship's rules, the court reviewed the bases for the coverage determination and concluded that none of the Board's reasons for denying coverage were arbitrary or capricious.

The TransAtlantic decision is a reminder that courts are loath to set aside the results of voluntary

ADR proceedings. That is particularly so where, as was the case here, the participants do not raise any objections to the process until after the award has been issued.


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