

# Dollar Limit of Liability in Facultative Reinsurance Certificates Encompassed Both Loss Reimbursement and Expense Reimbursement

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Court Rejects Reinsured's Contention That the Reinsurer's Liability for Expenses Was Not Subject to the Contractual Limit

*Continental Casualty Co. v. MidStates Reinsurance Corp.*, N.E.3d \_\_\_\_, 2014 WL 7166484 (Ill.App. Dec. 16, 2014) (corrected opinion) **Case at a Glance** Continental Casualty Company sought a declaration interpreting facultative reinsurance certificates for amounts it had paid for environmental claims arising from injuries linked to asbestos and hazardous waste at insured facilities, contending that its claims handling expenses were not subject to the contractual loss limit of the certificates. The trial court granted the reinsurer judgment on the pleadings, finding that the certificates' dollar amount cap on the liability of the reinsurer encompassed both losses and expenses. The Court of Appeals affirmed, finding that the language of the certificates was unambiguous with respect to this issue.

**Summary of Decision** Continental Casualty Company (Continental), as ceding insurer/reinsured, filed an action seeking declaratory and other relief arising out of multiple facultative reinsurance contracts issued to it by MidStates Reinsurance Corp. (MidStates), as reinsurer. The reinsurance certificates covered policies issued by Continental under which Continental paid claims resulting from environmental liabilities arising out of exposure to asbestos and hazardous wastes that were present at insured facilities. Each of the reinsurance certificates "followed the form" of the underlying insurance policies, contained a "follow the fortunes" claim payment provision and had a dollar cap, or limit, on the liability of MidStates. MidStates paid what it considered to be its limit under the certificates, which included payment for the reimbursement of both paid losses and claims handling expenses. Continental contended that MidStates owed additional payments for its

expenses in handling the insurance claims. The disputed issue was whether MidState's obligation to reimburse Continental for its expenses in processing and paying claims was included within the limit of each certificate, or was in addition to the limit. Continental contended that the contractual liability limit applied only to the reimbursement of the actual losses it had paid to its insureds. The trial court found the reinsurance certificates to be unambiguous with respect to this issue, and that the limit of liability limited the total obligation of MidStates, including its obligation to pay claim expenses. The trial court granted MidState's motion for judgment on the pleadings. Continental appealed and the Illinois Court of Appeals affirmed, quoting extensively from the trial court's opinion and agreeing with its analysis. The courts held that the certificates were unambiguous, making it unnecessary and inappropriate to consider extrinsic evidence in interpreting the certificates. Interpreting the certificates, the courts stated that the reinsurance certificates did not remove expenses from the amount of reinsurance assumed, but also did not specifically indicate that expenses were not subject to the contractual limits of liability. The courts followed the "Bellefonte principle," which originated with *Bellefonte Reinsurance Co. v. Aetna Casualty & Surety Co.*, 903 F.2d 910 (2d Cir. 1990), which provides that contractual liability limits in facultative reinsurance certificates cap the reinsurer's liability for the payment of both indemnity and expense amounts. The courts were not impressed by Continental's argument that since some, but not all, of the reinsurance certificates explicitly stated that the liability limit was inclusive of expenses, the certificates were ambiguous or otherwise not susceptible to summary interpretation, or that the certificates which did not contain that language should be interpreted differently than the certificates which did contain that language. The courts viewed this language as being merely clarifying, and not necessary to make expenses relating to the loss payments subject to the certificates' contractual liability cap. **Comment** This dispute might have been avoided, and both parties benefitted, if the contractual liability limit provision in each reinsurance certificate had explicitly stated that the payment of reimbursement for both losses and expenses were subject to the liability cap. Protecting the integrity of any contractual liability limit should be a primary concern of reinsurers in the drafting of reinsurance agreements, and clarity with respect to this issue would provide ceding insurers with a firmer basis for making financial plans and forecasts. More attention to this detail might have helped to avoid this dispute, and its attendant expenses and administrative disruptions, for both parties. *Reprinted with permission of Thomson Reuters, Inc. All rights reserved.*

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