

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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TPG GROUP, WILLIAM HUTCHISON, :
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 : Plaintiffs, :
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 : -against- :
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 : ALTERNATIVE RE HOLDINGS LIMITED, :
 ALTERNATIVE RE LIMITED, ARCH :
 INSURANCE COMPANY, :
 : Defendants. :
----- X

No. 08 Civ. 11244 (SHS)

MEMORANDUM OF LAW IN SUPPORT OF ARCH INSURANCE COMPANY'S
MOTION TO STAY LITIGATION PENDING ARBITRATION

Dated: New York, New York
February 13, 2009

DEWEY & LEBOEUF LLP
Lawrence W. Pollack
Lisa A. Keenan
1301 Avenue of the Americas
New York, New York 10019
Telephone: (212) 259-8000
Facsimile: (212) 259-8333

*Attorneys for Defendant
Arch Insurance Company*

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Defendant Arch Insurance Company (“Arch”) respectfully submits this memorandum of law in support of its motion to stay this litigation pending arbitration between Plaintiffs TPG Group (“TPG”) and William Hutchison (“Hutchison”) (together, “Plaintiffs”) and Defendant Alternative Re Holdings Limited (“Alt Re Holdings”).

I. PRELIMINARY STATEMENT

This lawsuit arises out of a failed business venture between Plaintiffs and parties other than Arch. In at least three separate written agreements between Plaintiffs and Arch’s co-defendant in this action, Alt Re Holdings, Plaintiffs agreed broadly and without reservation to arbitrate the very subject matter of this litigation, in Bermuda. Given the federal policy strongly favoring arbitration, there can be no doubt that Plaintiffs’ claims against Alt Re Holdings should be arbitrated, as Plaintiffs agreed. Under the Federal Arbitration Act, Plaintiffs’ claims against Alt Re Holdings must be stayed pending the outcome of the Bermuda arbitration.

Plaintiffs filed this lawsuit in an attempt to avoid that arbitration. Plaintiffs must know that this action violated the Federal Arbitration Act. To attempt to justify this violation, Plaintiffs named Arch as a defendant because Arch is not a signatory to the relevant arbitration agreements. The law in this Circuit, including a case decided by this Court, frowns on this type of behavior. A federal district court has the inherent power to control its docket. Honoring the agreement of parties to utilize alternative forms of dispute resolution is one way this is done. Arch was merely an incidental player in what was at its core a business arrangement between Plaintiffs and Alt Re Holdings. Arch was involved only to the extent that the insurance risks underlying the business arrangement between Plaintiffs and Alt Re Holdings were issued on Arch’s paper. This Court should

not allow Plaintiffs to circumvent their obligation to arbitrate their disputes with Alt Re Holdings by litigating those same disputes against such an incidental party.

Judicial economy favors a stay because the facts alleged and causes of action asserted in this litigation against Arch are the subject matter of the already initiated arbitration between Plaintiffs and Alt Re Holdings. The arbitration, therefore, will determine, or at the very least inform, the outcome of this litigation. Allowing these same facts and issues to be determined simultaneously in these parallel proceedings, moreover, would cause the parties to suffer undue burden and expense, and duplication of efforts, and would run the risk of inconsistent outcomes. There is also no indication that a stay would cause undue delay or prejudice to Plaintiffs, as Alt Re Holdings has demonstrated diligence in pursuing the Bermuda arbitration proceedings. Indeed, it is Plaintiffs that have sought to delay the Bermuda arbitration by filing this lawsuit.

The equities demand that this Court exercise its inherent power to stay litigation of Plaintiffs' claims against Arch, pending Plaintiffs' arbitration against Alt Re Holdings. This motion to that effect should be granted in all respects.

II. STATEMENT OF FACTS

A. The NBG Program

The business venture between Plaintiffs and Alt Re Holdings was known as the "NBG Program." Affidavit of Lawrence W. Pollack, dated February 11, 2009 ("Pollack Affid."), Ex. 1, at ¶ 11. Plaintiffs allege that under the NBG Program, National Benefits Group wrote and placed workers compensation insurance coverage on behalf of Arch, pursuant to the Managing General Agency Agreement entered into between Arch and NBG. *See id.*, at Ex. F. The involvement of Arch was limited to the fact that the insurance policies arranged by NBG were written on Arch paper. *See, e.g., id.*, ¶¶ 11-12.

The Complaint asserts that, once placed, Arch would cede the risks and premiums associated with its workers compensation business, in part, to its captive reinsurer Alternative Re Limited (“Alt Re Ltd.”), a wholly-owned subsidiary of Alt Re Holdings (together with Alt Re Ltd., the “Alt Re Defendants”). *Id.*, at ¶ 12. Under the NBG Program, Plaintiffs purchased preferred shares in Alt Re Holdings. *Id.*, at Exs., B, D, E, and J. Under the terms of the shareholders agreements the Plaintiffs thus became obligated to collateralize the cessions assumed by Alt Re Ltd. *Id.*, at ¶ 12; *see also id.*, at Exs. B, D, E, and J.

The Alternative Re Holdings Limited Shareholder Agreement, effective as of April 15, 2001 (the “2001 Shareholder Agreements”), initially governed Plaintiffs’ rights and obligations concerning the NBG Program. Pollack Affid., Ex. 1, at Ex. B. Thereafter, the Shareholder Amendment Agreement, dated as of December 30, 2005 (the “2005 Shareholder Amendment Agreement”), which incorporated the 2001 Shareholder Agreements, and ultimately the Alternative Re Holdings Limited Shareholder Agreement, effective as of December 30, 2005, but entered into by the parties in 2007 (the “2007 Shareholders Agreement”) (collectively with the 2001 Shareholder Agreements, the “Shareholders Agreements”), governed Plaintiffs’ rights and obligations. *Id.*, at Exs. D, E, and J.

Under the Shareholders Agreements, Plaintiffs were entitled to share in the premium and investment income associated with the workers compensation risks assumed by Alt Re. *See* Pollack Affid., Ex. 1, at Ex. D, ¶ 2, and Ex. E, ¶ 2. Plaintiffs likewise were obligated to bear the risks attendant to Alt Re’s assumption of the workers compensation business. *See id.* Pursuant to those obligations, Plaintiffs were required to

post collateral to be used to indemnify Alt Re Holdings for any associated losses. *Id.*, at Ex. D, ¶ 6, and Ex. E, ¶ 6.

Each of the Shareholders Agreements was executed on Plaintiffs' behalf by attorneys at the Bermuda law firm Conyers Dill & Pearman, which held a power-of-attorney from each of the Plaintiffs. *See* Pollack Decl., Ex. 1, at Exs. B, D, E, and J. Each of the Shareholders Agreements contained a broad arbitration clause. *Id.*, at Ex. B, ¶ 12 (“All disputes between [Alt Re Holdings] and the Shareholder . . . will be submitted to arbitration in Bermuda by a panel of three arbitrators. * * *”), Ex. D, ¶ 12 (same), Ex. E, ¶ 12 (same), and Ex. J, ¶ 19 (“The parties hereto agree to consolidated arbitration proceedings in the event of any dispute under the terms of the Shareholder Agreements, as amended.”).

The NBG Program operated from April 15, 2001 through October 2, 2003. Pollack Decl., Ex. 1, at ¶ 11. The NBG Program was cancelled effective October 2, 2003. *See id.* at Ex. C. On February 11, 2005, Alt Re Holdings informed its shareholders that there was a shortfall in collateral funding and that, pursuant to the Shareholders Agreements, the shareholders would be obligated to indemnify Alt Re Holdings for their respective shares of the shortfall. *Id.*

B. The 2005 Settlement

In December 2005, NBG, Alt Re Holdings, and its various shareholders, including Plaintiffs, entered into a Confidential Settlement Agreement, effective as of December 30, 2005 (the “Settlement Agreement”). Pollack Affid., Ex. 1, at Ex. A. Under the Settlement Agreement, Plaintiffs, among other things, ratified the Shareholders Agreements then in effect. *Id.*, at Ex. A, ¶ 6(a). Those Shareholders Agreements, including their broad arbitration clauses, were incorporated by reference into the

Settlement Agreement. *Id.*, at Ex. A, ¶ 2(b). In entering the Settlement Agreement, the Plaintiffs acknowledged that they did so voluntarily, “with full knowledge of its contents and significance, and after receiving the advice of counsel of their choosing concerning it.” *Id.*, at Ex. A, ¶ 22.

As a companion to the Settlement Agreement, Plaintiffs and Alt Re Holdings entered into the 2005 Shareholder Amendment Agreement. *See* Pollack Affid., Ex. 1, at Ex. J. The 2005 Shareholder Amendment Agreement incorporated by reference the 2001 Shareholder Agreements, and redistributed those preferred shares that had been relinquished by NBG and others as a result of the Settlement Agreement. *Id.* at Ex. J, ¶¶ 2(b), 6(a). Each of the parties represented that they entered into the 2005 Shareholder Amendment Agreement voluntarily and “with full knowledge of its contents and significance, and after receiving the advice of counsel of their choosing concerning it.” *Id.*, at Ex. J, ¶ 22.

C. The Dispute before this Court and Its Referral to Arbitration under the Shareholders Agreements

A dispute arose concerning Plaintiffs’ obligation to pay to Alt Re Holdings certain amounts due under the 2007 Shareholders Agreement. *See* Pollack Affid., Exs. 2 and 3. On October 22, 2007, Alt Re Holdings demanded that Plaintiffs submit that dispute to arbitration in Bermuda, as required by the Shareholders Agreements. *Id.* Plaintiffs and Alt Re Holdings each subsequently selected their respective arbitrators. On November 21, 2008, Alt Re Holdings petitioned the ICC International Court of Arbitration for the appointment of an umpire. *Id.*, at Ex. 4.

D. This Action

On December 24, 2008, two months after Alt Re Holdings initiated the Bermuda Arbitration, Plaintiffs filed this lawsuit in the United States District Court for the Southern District of New York (the “Federal Lawsuit”). *See TPG Group, et al. v. Alternative Re Holdings Limited, et al.*, 08 CIV 11244 (S.D.N.Y.) (Stein, J.), Dkt. No. 1. Plaintiffs’ Federal Lawsuit alleges that Alt Re Holdings, Alt Re Ltd., and Arch made material misrepresentations that induced Plaintiffs to enter into the Shareholders Agreements and the Settlement Agreement with Alt Re Holdings. *See generally*, Pollack Affid., Ex. 1. Plaintiffs’ Federal Lawsuit asserts causes of action for securities fraud, common law fraud, intentional and negligent misrepresentation, breach of contract, breach of fiduciary duties, fraudulent inducement, and civil conspiracy. *Id.*, at ¶¶ 57-101. In addition to seeking compensatory damages and rescission of the various agreements, Plaintiffs ask this Court to enjoin Alt Re Holdings from proceeding with the arbitration in Bermuda. *Id.*, at p. 22.

Alt Re Holdings offered to stay the arbitration in Bermuda temporarily, pending motions the defendants would be bringing to compel arbitration and stay the Federal Lawsuit, subsequent to the appointment of an umpire. Pollack Affid., Ex. 5. Alt Re Holdings explained to Plaintiffs their desire to have an umpire in place so that the Bermuda arbitration could proceed once a decision was made by this Court on their motions to compel arbitration. *Id.* Plaintiffs refused the offer, insisting that discovery commence in the Federal Lawsuit, notwithstanding the anticipated motions to compel. *Id.* The ICC International Court of Arbitration informed Plaintiffs and Alt Re Holdings on January 29, 2009, that it intended to proceed with appointment of an umpire. *Id.*

III. THE COURT SHOULD STAY THE LITIGATION OF PLAINTIFFS' CLAIMS AGAINST ARCH, PENDING ARBITRATION OF PLAINTIFFS' IDENTICAL CLAIMS AGAINST ALT RE HOLDINGS

A. This Court Must Stay Plaintiffs' Federal Lawsuit Against Alt Re Holdings Because Plaintiffs' Claims Against Alt Re Holdings Must Be Submitted to the Bermuda Arbitration

The Federal Arbitration Act provides that where parties have agreed in writing to arbitrate their disputes, a court must stay litigation pending arbitration of those disputes. Federal Arbitration Act, 9 U.S.C. §§ 2, 3. There is a “strong federal policy in favor of arbitration, [and] the existence of a broad agreement to arbitrate creates a presumption of arbitrability” *Worldcrisa Corp. v. Armstrong*, 129 F.3d 71, 74 (2d Cir. 1997). Arch understands that Alt Re and Alt Re Holdings are filing a joint motion to compel arbitration and stay this litigation. Arch incorporates herein and relies upon the arguments made in that joint motion.

B. This Court Should Exercise Its Inherent Powers to Stay Plaintiffs' Federal Lawsuit as Against Arch, Pending Plaintiffs' Arbitration of Identical Claims against Alt Re Holdings

As this Court has ruled, “[a] stay of proceedings as to one defendant pending arbitration between that defendant and the plaintiffs may be extended to remaining defendants pursuant to a district court’s inherent power to control its docket.” *Hughes, Hooker & Co. v. Am. Steamship Owners Mut. Protection & Indem. Assoc.*, 04 Civ. 1859 (Stein, J.), 2005 U.S. Dist. LEXIS 11381, at *17-18 (S.D.N.Y. June 9, 2005); *WorldCrisa Corp.*, 129 F.3d at 76. The proponent of the stay bears the burden of demonstrating that, having considered any prejudice that might be suffered, the balance of hardships and interests of judicial economy weigh in favor of a stay. *Hughes, Hooker & Co.*, 2005 U.S. Dist. LEXIS 11381, at *18 (citing *Nederlandse Ertstankers-Maatschappij, N.V. v. Isbrandtsen Co., Inc.*, 339 F.2d 440, 441 (2d Cir. 1964)). Arch can easily sustain that

burden here. The inefficiencies of time and expense, the duplication of effort, and the risk of inconsistent results weigh strongly in favor of staying Plaintiffs' litigation of claims against Arch. Any such claims mirror those that will be the subject of the arbitration already underway in Bermuda.

“When considering whether to stay a case in favor of arbitration the court considers the expense and inconvenience of parallel litigation as well as the possibility of inconsistent determinations.” *The Provident Bank v. Kabas*, 141 F. Supp. 2d 310, 318-19 (E.D.N.Y. 2001). Courts typically extend a stay where the claims to be litigated arise out of the same facts as those which are the subject of arbitration, or where failing to do so would result in duplication of efforts, or inconsistency of result. *See Id.* at 319 (“[W]here arbitrable and non-arbitrable claims arise out of the same set of facts, the arbitration may decide the same facts at issue in the litigation making a stay appropriate.”); *Aekyung Co., Ltd. v. Intra & Co., Inc.*, 99 Civ. 11773 (LMM), 2000 U.S. Dist. LEXIS 14911, *5 (S.D.N.Y. Oct. 13, 2000) (“It is appropriate, as an exercise of the district court’s inherent powers, to grant a stay where the pending arbitration is an arbitration in which issues involved in the case may be determined.”) (*quoting Sierra Rutile Ltd. v. Katz*, 937 F.2d 743, 750 (2d Cir. 1991)).

Courts also consider whether a stay will result in undue delay or other prejudice to the parties. *The Orange Chicken, LLC v. Nambe Mills, Inc.*, 00 Civ. 4730 (AGS), 2000 U.S. Dist. LEXIS 18214, at *28 (S.D.N.Y. Dec. 19, 2000). “[T]he moving party has the burden of showing that it will not hinder the arbitration, that the arbitration will be resolved within a reasonable time, and that such delay that may occur will not cause undue hardship to the non-moving party.” *Id.* Where, as here, the arbitration proceeding

already has been initiated, courts typically find that this requirement has been satisfied. *See id.* at 34; *see also O'Dean v. Tropicana Cruises Int'l, Inc.*, 98 Civ. 4543 (JSR), 1999 U.S. Dist. LEXIS 7751, *10 (S.D.N.Y. May 25, 1999) (finding requirements met upon defendants' representation that they would begin arbitration at plaintiff's earliest convenience).

Finally, courts consider the plaintiff's motive for naming as a defendant a party not subject to the arbitration agreement. "A party ought not be able to avoid arbitration by suing a related party 'with which it has no arbitration agreement in the hope that the claim will be adjudicated first and have preclusive effect on the arbitration.'" *The Provident Bank*, 141 F. Supp. 2d at 319; *see also WorldCrisa*, 129 F.3d at 76 (quoting *IDS Life Ins. Co. v. SunAmerica, Inc.*, 103 F.3d 524, 530 (7th Cir. 1996) (Posner, J.)).

All of the authorities cited above as well as the balance of the equities weigh strongly in favor of staying Plaintiffs' Federal Lawsuit against Arch, pending the outcome of the Bermuda arbitration. Plaintiffs allege against Arch the same facts and claims as those that they allege against Alt Re Holdings. Those facts will be discovered and claims will be determined in the Bermuda arbitration. Indeed, it would appear that many, if not all, of Plaintiffs' claims against Arch may be subject to dismissal depending upon the conclusions reached in the Bermuda arbitration. Litigation of identical claims based upon identical facts here in New York, therefore, would require duplicative discovery and expense and would pose a risk of inconsistent determinations. Under these circumstances, a stay is appropriate. *See The Provident Bank*, 141 F. Supp. 2d at 319 (finding stay appropriate where claims in litigation and arbitration arose out of same facts).

For example, determination of Plaintiffs' derivative claims against Arch cannot be made without analysis in the first instance of the Shareholders Agreements. Those agreements defined Plaintiffs' rights and obligations under the NBG Program, and will be at the heart of the Bermuda arbitration. Because Plaintiffs and Alt Re Holdings were parties to the Shareholders' Agreements, and Arch was not, the decision by the Bermuda arbitration panel as to the parties' respective rights and obligations under the Shareholders Agreements will govern the interpretation of those agreements in Plaintiffs' Federal Lawsuit. Thus, courts have concluded that where, as here, the determination of the claims against the remaining defendant in the litigation "center around and depend upon [the] interpretation of the contractual agreement[s] that [are] subject to arbitration . . .," a stay is appropriate. *Hughes, Hooker & Co.*, 2005 U.S. Dist. LEXIS 11381, at *19-20; *see also The Orange Chicken*, 2000 U.S. Dist. LEXIS 18214, at *29-30 (finding stay appropriate where arbitration involved interpretation of licensing agreement implicated in litigation over competing licensing agreement).

By contrast, Plaintiffs will suffer no prejudice if their Federal Lawsuit against Arch is stayed. The Alt Re Defendants have already initiated the Bermuda Arbitration, and completion of the composition of the arbitration panel is imminent. The Alt Re Defendants have provided every indication that they intend to proceed with the Bermuda arbitration in a forthright manner. *See* Pollack Decl., Ex. 4. Indeed, it is Plaintiffs that, thus far, have attempted to delay the arbitration. Thus, there is no reason to suspect that the Bermuda arbitration will not conclude within a reasonable time.

The circumstances presented here also suggest that Plaintiffs named Arch as a defendant in this lawsuit because they knew ultimately they would be compelled to


arbitrate their claims against Alt Re Holdings. At its core, this lawsuit is a dispute between Plaintiffs and Alt Re Holdings over their respective contractual obligations. Arch was not a party to those contracts, and was involved only to the extent the underlying workers compensation risks ceded to Alt Re Ltd. were written on its paper. Plaintiffs should not be permitted to use Arch as a surrogate to litigate its disputes against Alt Re Holdings. Plaintiffs' Federal Lawsuit against Arch, therefore, should be stayed pending the outcome of the Bermuda arbitration.

CONCLUSION

Based on the foregoing, Arch respectfully requests that this Court enter an order staying the litigation of Plaintiffs' claims against Arch, pending Plaintiffs' arbitration with Alt Re Holdings.

Dated: New York, New York
February 13, 2009

Respectfully submitted,
DEWEY & LEBOEUF LLP

By: 

Lawrence W. Pollack (LP 3273)
Lisa A. Keenan (LK 1081)
1301 Avenue of the Americas
New York, NY 10019
Telephone: (212) 259-8000
Facsimile: (212) 259-6333

Attorneys for Defendant Arch Insurance Co.