Contract Law

Jurisdiction clauses and their effects on foreign (US) affiliates

Parent companies usually conclude comprehensive insurance contracts for themselves and their national and international affiliates. The only parties involved in the conclusion of the contract are the parent company (policy holder) and the insurer.

Insurance contracts often contain a separate jurisdiction clause in addition to the choice of law clause. If a coverage dispute arises after the occurrence of damage to a foreign affiliate, it is questionable whether an affiliate (as insured) is also bound to the agreement on jurisdiction.

The European Court of Justice decided in 2005 that a beneficiary/affiliate located in another member state of the EU than the insurer and the policy holder (parent company), is not bound to a jurisdiction clause it did not explicitly agree to ("SFIP" decision\(^1\), below 1.). This decision was followed by a decision of the United States District Court of Illinois of 7 November 2012 regarding co-insured companies in the USA (below 2.).

1. **SFIP-DEcision of European Court of Justice**

According to the SFIP decision of the European Court of Justice (ECJ), foreign co-insured companies are only bound to the choice of jurisdiction if they agreed to it.

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The decision of the ECJ was based on the Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters (“Brussels Convention”, Art. 12 no. 3) applicable at that time. The ECJ regarded the insured company as worthy of protection although the jurisdiction clause had explicitly been agreed by the policy holder and the insurer and the affiliate was beneficiary of the insurance contract.

The court held that a protection of the insured was justified since he is usually confronted with a pre-formulated insurance contract. Art. 12 no. 3 of the Brussels Convention contained a final list of requirements which allow the contract parties to depart from the provisions of the Brussels Convention. According to Art. 12 no. 3 of the Brussels Convention, a deviating agreement on jurisdiction is (only) admissible if policy holder and insurer are domiciled in the same state and the agreement has the effect of conferring jurisdiction on the courts of that state even if the harmful event were to occur abroad. If the insured (the affiliate) was bound to the agreement on jurisdiction, he could neither bring action at the place where the damage occurred nor before the courts of his domicile. The insured would rather have to file claims against the insurer before courts in the state where the insurer is domiciled. This would not be reasonable for the insured without his explicit approval.

With this decision, the ECJ created the possibility for the parent company (policy holder) and the foreign affiliate (insured) to carry on a cover dispute against the insurer deviating from agreements – after considering the advantages and disadvantages.

2. DECISION OF THE US DISTRICT COURT ILLINOIS

Based on the SFIP-decision of the ECJ, the United States District Court, N.D. Illinois, decided on 7 November 2012 that an agreement on jurisdiction in a German insurance contract in favor of jurisdiction in Germany (Cologne) was not enforceable vis-à-vis a co-insured company in the USA.  

The District Court based its decision on the following facts:

2.1 Facts

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2 United States District Court, N.D. Illinois, decision of 7 November 2012, File No. 11 C 9131, 2012 WL 5429618 (N.D. Ill.).
The plaintiff (Baxter International Inc., “Baxter”) claimed for coverage against the insurer (AXA Versicherung AG, “AXA”) in the USA.

Baxter is a company located in Illinois. In 1996, Baxter acquired the Immuno-AG (“Immuno”), located in Austria. At that time, Immuno was insured with the legal predecessor of AXA. Baxter AG located in Vienna was included into the insurance contract of Immuno as additional policy holder.

According to the appendix of the insurance contract, Baxter became an additional insured company under Immuno’s insurance contract.

The insurance contract contained a choice of law clause in favor of German law. According to the clause, the place of jurisdiction was Cologne.

2.2 Decision

The District Court decided that the agreement on jurisdiction in the insurance contract was effective and had an exclusionary effect. The agreement on jurisdiction was though not enforceable vis-à-vis Baxter as insured beneficiary. Baxter was no original party of the insurance contract and had not agreed on the choice of jurisdiction at any time.

The District Court based its decision on the European Regulation on Jurisdiction and Enforcement (Regulation (EC) no. 44/2001, “Brussels I Regulation”). It argued that the SFIP-decision of the ECJ was also applicable on the basis of the Brussels I Regulation. An insured that is not a contract party should be protected from a place of jurisdiction which he did not explicitly agree to and which was chosen by the insurer.

During the proceedings, AXA argued that the idea of protection of the SFIP-decision was not applicable here. Opposite to the Brussels Convention, the Brussels I Regulation now provided the additional possibility to generally depart from the provisions in case the insurance contract covered a “major risk” (Art. 13 para. 5, 14 para. 5 Brussels I Regulation). Both the Immuno insurance contract and Baxter met the requirements of such major risk. Neither the policy holder (Baxter AG) nor the co-insured company (Baxter) were therefore economically weak parties that had to be protected from a jurisdiction at the insurer’s domicile. However, the District Court held that a deviation from provisions of the Brussels I Regulation nevertheless required an agreement with the insured. Such agreement did not exist.
Further, the District Court pointed out that AXA provided no other reasons to prove that the USA as place of jurisdiction were unacceptable for the insurer (forum non conveniencia).

3. CONSEQUENCES

Given the District Court’s decision, agreements on jurisdiction in policies of European corporations are probably not enforceable vis-à-vis insured affiliates in the USA (below 3.1). Whether co-insured affiliates should bring action before courts in the USA depends on financial and other advantages or disadvantages in the individual case (below 3.2, 3.3).

3.1 Possibility of actions for coverage in the USA

Insured US affiliates might claim for coverage against their European insurer in the USA contrary to an agreement on jurisdiction in the company’s policy.

Usually, affiliates do not explicitly approve agreements on jurisdiction in insurance contracts. That is why a US affiliate may in case of dispute at any time invoke (by referring to the District Court’s decision) that it did not explicitly approve the agreement on jurisdiction in the policy and was thus not bound to it.

The District Court’s decision is however not binding for other US courts. Other US courts may therefore hold that co-insured affiliates do not need protection from agreements on jurisdiction if a major risk is covered. The District Court’s decision has though an indicative effect for future legal disputes.

There is no possibility to bring action if the parent company officially represented the co-insured company (e.g. on the basis of an authorization) when the company’s policy was concluded. In this case, the co-insured affiliate explicitly approved the agreement on jurisdiction through representation by the parent.

3.2 Costs of action for coverage in the USA

An action for coverage could cause higher costs in the USA than in the EU, both for the insurer and the insured company. Court fees for legal disputes may be lower in the USA than in Germany, but lawyers’ fees are usually higher in the USA. Lawyers’ fees are not calculated on the basis of the amount in dispute but based on hourly rates.
Whether the costs for an action for coverage in the USA are in any case higher than those of an action before German (or other European) courts or not, is questionable. At least in case of business disputes, German and European attorneys usually work on the basis of hourly rates equivalent to the rates of American colleagues. Thus, higher costs will just arise due to the fact that American attorneys perform more extensive work in the course of the proceedings (e.g. preparation of trial proceedings by gathering of evidence in the pre-trial discovery, extensive hearings of witnesses and experts).

3.3 Advantages / disadvantage of actions for coverage in the USA

For US affiliates, actions for coverage in the USA might be advantageous due to the closer proximity of the court to the facts of the case and due to possible corresponding liability questions (publicity of the damage event). An advantage not to be underestimated is the fact that courts psychologically tend to favor the local party. A US court might therefore tend to grant the claim against a foreign insurer.

On the other hand, the US court would have to apply foreign law to the action. The law chosen in the policy will probably be the law of the chosen jurisdiction. The US court might e.g. (when German law is chosen) have to judge on the interpretation and systematics of general terms and conditions of insurance in connection with the German Insurance Contract Act. This might be an advantage or disadvantage both for the insurer and the policy holder depending on the court’s expertise.

If the US court judges on the basis of the law chosen, the insurer will probably not be confronted with higher claims for damage (besides the claim for coverage). Punitive damages may only be adjudged if the applicable law provides for this possibility. This is not the case for German law.

4. EVALUATION ON THE BASIS OF GERMAN LAW

Whether or not a (foreign) affiliate may in the future bring action at a place deviating from the agreement on jurisdiction (at his own domicile or at the place of damage) even if an insurance contract covering major risks is given, depends on – at least from the German legal point of view) a) whether the SFIP-decision of the ECJ applies also for insurance contracts covering major risks on the basis of the Brussels I Regulation and b) whether the insured company has a right of action under the insurance contract.
4.1 Applicability of SFIP for major risks

It is not clarified yet whether the ECJ will apply the SFIP-decision also to insurance contracts which cover major risks.

The District Court’s argumentation that an agreement on jurisdiction is enforceable vis-à-vis the insured only in case of his explicit agreement – independent of the existence of a major risk –, is justified. Also in case of major risks, any departure from the provisions of the Brussels I Regulation pursuant to Art. 13 para. 5, 14 para. 5 Brussels I Regulation requires agreement. The agreement on jurisdiction is a separate (procedural) agreement that can only bind involved parties. Thus, also in case of major risks, the agreement of the insured company (not only of the policy holder) might be a precondition for a binding effect of the agreement on jurisdiction.

On the other hand, insurers might argue that insurance contracts which cover major risks might principally deviate from the provisions of Brussels I Regulation which protect the insured. Therefore, a beneficiary of such major risks insurance contract should have to accept the limits set by contract. The contract parties intended to grant insurance coverage to the insured from the start only under the agreed terms (including place of jurisdiction). In insurance contracts covering major risks, the policy holder is an economically strong company which does not need protection by the Brussels I Regulation. This applies especially if the insured company itself meets the requirements of major risks.

However, independent of a future ECJ decision, US affiliates will probably already now refer to the District Court’s decision.

4.2 The affiliate’s right of action

If an affiliate wants to claim for coverage against the insurer, the affiliate as insured has to be entitled to bring action under the insurance contract.

If there is no clause in the insurance contract entitling the insured affiliate to bring action, the right of action is determined by the legal provisions of the Insurance Contract Act for those contracts which are subject to German law.

Parent companies conclude their insurance contracts for their own accounts and for their affiliates’ accounts. As far as an insurance contract affects an affiliate, the regula-
tions for insurance on account of third parties apply in the relationship between insurer and insured company.

According to sec. 44 para. 2 Insurance Contract Act, an insured may only lay claim to his rights from the insurance contract without the policy holder’s agreement and assert these rights in court if he possesses the insurance policy. Reversely, this means that the policy holder (parent company) may entitle the insured (affiliate) to bring action independent of the possession of the insurance policy. For a coverage dispute in the USA it might thus be sufficient if the parent company agrees to the action of the insured affiliate in the USA.

5. OUTLOOK

The District Court’s decision has consequences for insurers. US affiliates affected by insured events might in the future override agreements on jurisdiction of European company policies and claim for coverage against their insurer before US courts.

Parent companies as policy holders should consider the option of an action by the insured company in the USA in the insured event (thoroughly taking advantages and disadvantages into account).