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Defence Costs Coverage

This article analyses a recent decision in the Supreme Court of Texas which has important implications for defence cost cover in relation to policy terminology that often forms the basis of Liability insurance coverage in the oil & gas industry.

The recent decision delivered on the 25th January 2019 in the Supreme Court of Texas in the case of Anadarko Petroleum Corporation and Anadarko E&P Company, L.P. v Houston Casualty Company, et al. (No. 16-1013) highlights an important issue regarding defence cost cover in relation to policy terminology that often forms the basis of Liability insurance coverage for the oil & gas industry.

The case relates to a legal dispute arising from the Deepwater Horizon offshore drilling unit incident. Specifically, a dispute between Anadarko Petroleum Corporation and Anadarko E&P Company, L.P. (collectively Anadarko) and certain underwriters participating in the Excess Liability section of Anadarko's Energy Package insurance policy.

The coverage in question was based upon the JL.007 (2003) London Claims Made Policy. The Court of Appeals had previously held that the terminology of the policy Joint Venture clause applied a limit to all coverage under the policy, including cover for defence costs. Such limit being based upon Anadarko's joint venture percentage interest in the Macondo well.

The Supreme Court concluded that the policy terminology did not mean that Anadarko's percentage interest in the well should be applied to their defence cost expenditure, so as to reduce the amount of policy coverage available for such defence costs.

Having rendered judgment on the policy limit in respect of defence costs the Supreme Court remanded the case to the trial court for further proceedings. The Supreme Court leaving the trial court to address the matter of quantum.

The Excess Liability section of Anadarko's Energy Package policy provided coverage limited to US$ 150,000,000 (100%) any one occurrence. In accordance with a joint venture agreement with BP entities and MOEX Offshore 2007 LLC, Anadarko held a 25% ownership interest in the Macondo well.

In accordance with the Court of Appeals interpretation of the policy wording, applying 25% to the policy limit of US$ 150,000,000 would

result in underwriters per occurrence exposure for all coverage being limited to US$ 37,500,000. Allowing for settlements already made under the policy, in respect of Anadarko's liability to third parties, underwriters position was that the policy limit had already been reached and as such no coverage was available in respect of Anadarko's defence costs.

The Joint Venture clause in the policy wording, being the clause which entitled underwriters to reduce the policy limit to reflect the Insured's percentage interest in the well, expressly restricted this reduction in limit to any *"liability"* of the Insured covered under the policy.

Whilst Anadarko's policy amended the standard terminology of the JL.007 Joint Venture clause, the salient provisions remained unchanged. Specifically, the provision that the Joint Venture clause only enabled underwriters to scale down the policy limit with regards to any *"liability"* of Anadarko.

Significantly, in addition to providing cover for *"liability"* for damages imposed upon the Insured for third party bodily injury, property damage and the like, the policy wording, via the Ultimate Net Loss definition, also provided coverage in respect of defined *"Defence Expenses"*.

Underwriters had contended that the reference within the Joint Venture clause to *"liability"* included defence costs, thus enabling them to apply the reduced policy limit to such costs.

However, the Joint Venture clause terminology, introducing the formula to reduce the policy limit, only referred to the *"liability"* of the Insured and made no reference whatsoever to the broader coverage provided by the Ultimate Net Loss definition, specifically the *"Defence Expenses"* cover. Based upon this point the Supreme Court found in favour of Anadarko, thus providing a basis for their defence costs to be considered under the policy.

Prior to the involvement of the Supreme Court, the Court of Appeals had supported underwriters contention that, so far as policy coverage was concerned, the term *"liability"* included defence costs. It is interesting to note that whilst this case was heard in Texas, the deliberations on policy coverage involved the London Claims Made Policy. At English Law, longstanding case law exists to support the contention that under a marine liability insurance contract legal expenses, in defending a claim, do not constitute a liability. (Xenos v Fox (1869) L.R. 4 C.P. 665).

Based simply upon the principle of insurable interest, it is entirely reasonable that the Joint Venture clause should scale the limit of underwriters exposure to reflect the Insured's interest in the asset upon which the coverage is based. In accordance with their percentage interest in a joint venture agreement, such insurable interest being the Insured's potential liability to third parties.

However, it would not be unreasonable to suggest that such scaling of the policy limit should not apply to an individual joint venture partner's defence cost coverage on the basis that an individual joint venture partner may be responsible for 100% of their own defence costs.

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