UK Legal News Analysis

Court considers liability insurance policy

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Abstract

Dispute Resolution analysis: Chris Finney, a partner with Edwards Wildman Palmer UK LLP, explains the complexities of the judgment in Astrazeneca Insurance Company Ltd v XL Insurance (Bermuda) Ltd, and advises lawyers that if you decide to change the applicable law in a contract, make sure you understand all of the consequences of doing so.

Analysis

Original news

Astrazenca Insurance Co Ltd v XL Insurance (Bermuda) Ltd [2013] EWHC 349 (Comm), [2013] All ER (D) 08 (Mar)

The claimant was the captive insurer of a major worldwide pharmaceutical group, which had settled class actions brought in respect of the prescription drug, Seroquel, which it manufactured. The claimant brought a claim contending that it was entitled to be indemnified by the defendant reinsurers in respect of all sums it had paid in respect of settlements and defence costs. The defendants denied any such entitlement to an indemnity.

The Commercial Court, in answering two preliminaries issues, held that: (i) the insured was only entitled to an indemnity under the policy where it demonstrated that it was under an actual legal liability; and (ii) the insured was only entitled to an indemnity for defence costs where it established that it was or would have been liable for the claim in question.

What key issues did this case raise?

Key facts

The claimant (AstraZeneca Insurance Company Limited) (AIC) is a captive insurance company in the AstraZeneca pharmaceuticals group (AG). It provided product liability insurance for AG for a layer of £133 million in excess of £365 million for the period 2001-2003 (the Policy).

The Policy wording

o was based on the standard Bermuda Form XL004, save that the parties agreed it would be subject to English, instead of New York, law

o required AIC to 'indemnify [AG] for [the] Ultimate Net Loss [AG] pays by reason of liability...imposed by law...for Damages on account of...Personal Injury'

o defined the term 'Damages' so it included compensation and defence costs

Each of XL Insurance (Bermuda) Limited (XL) and ACE Bermuda Insurance Limited (ACE) agreed to reinsure AIC against 50% of its liability under the Policy.

From 1997, AG manufactured, marketed and sold an FDA approved antipsychotic drug, Seroquel. In 2003, a US class action was filed against AG alleging:

o Seroquel caused personal injury

o it was defective

o the warnings about the drug were inadequate

A large number of additional claimants joined the class action, or filed claims of their own. By 31 October 2012, AIC had indemnified AG against claims under the Policy worth £83.5 million in excess of the £365 million.

The overwhelming majority of AG's Policy claims were for the reimbursement of defence costs. However, it had also agreed and paid a small number of commercial settlements. AIC asked XL and ACE to indemnify it against the £83.5 million of AG claims it had already settled, but they refused. XL and ACE argued AG was only entitled to an indemnity under the Policy in respect of claims where, on the balance of probabilities, it had an actual liability to a claimant. There was no evidence that AG was liable to any of the claimants. It was not therefore entitled to anything under the terms of the Policy. As a result, there was nothing for XL and ACE to indemnify AIC against.

The issues

(1) Bermuda Form policies are conventionally governed by New York law and 'the traditions and practices of the US [insurance] market'. Should the court therefore have regard to New York law when it construes the Policy?

(2) Does AG's right to an indemnity against the costs of settling a claim depend on it being able to show that, on the balance of probabilities, it was liable for the claim it settled?

(3) Does AG's right to an indemnity against the costs of successfully defending a claim also depend on whether, on the balance of probabilities, it was liable for the claim?

To what extent did the Commercial Court clarify the law in this area?

Most of the law in this area is well established. Mr Justice Flaux reviewed it, and sought to apply it as it stands. By doing so, he found that:

(1) 'To the extent that...[AIC] sought to contend that part of the "matrix" or "background" which this court should consider in construing the [Policy] was that the Bermuda Form is conventionally governed by New York law, and that, somehow, the court should be influenced in construing the [Policy] by how the New York courts or New York law would approach the issues of construction, that contention is misconceived and heretical...the parties have deliberately chosen...English law...so that what New York law might decide in terms of construction is irrelevant...the parties...are to be taken objectively to have intended that their contact should be governed by English law...In those circumstances, it seems to me it would be quite wrong to construe the contract in any respect by reference to New York law.' [see paras [5], [18] and [19] of Flaux Js' judgment]

(2) '...there is a consistent and well-established line of authority that, in the absence of clear contrary wording in the contract of liability insurance, under English law (i) the insured has to establish that it was under an actual legal liability, not just an alleged liability, to the third party before it is entitled to an indemnity under the contract; and (ii) the ascertainment of loss by a judgment or settlement does not automatically establish such actual legal liability (although a judgment against the insured may be strong evidence of such liability). It is still open to the insurer to challenge that there was an actual legal liability, in which case it is for the insured

to prove that there was.' [see para [96] of Flaux J's judgment]

The question was therefore whether the Policy included 'clear contrary wording'. It did not. Rather, in the phrase 'indemnify [AG] for [the] Ultimate Net Loss [AG] pays by reason of liability...imposed by law...for Damages on account of...Personal Injury', 'the words "by reason of" indicate that there has to be a clear causal link between what is paid and the liability and the words "imposed by law" make it clear...that there has to be an actual legal liability'. [see para [98] of Flaux J's judgment]

(3) 'In considering the recoverability of Defense Costs, an important starting point is that, as a matter of English law, in non-marine liability insurance, there is no concept of "sue and labour", so that, if the insured acts to defend a claim and thereby avoids the insurer being under any liability, there is no entitlement to an indemnity against the costs and expenses incurred in defending successfully the liability which would otherwise have arisen under the insurance, in the absence of some express provision to that effect...' [see para [137] of Flaux J's judgment]

The question was therefore whether there was a free-standing indemnity for defence costs under the terms of the Policy, but there was not. '...by tacking the words "and shall include Defense Costs" on to the definition of Damages, the parties have expressed the intention that defence costs should only be recoverable in circumstances where what might be described as "traditional" damages are recoverable, not that there should be free-standing coverage for such defence costs. In relation to the first preliminary issue, I have decided that traditional damages are only recoverable where there is an actual legal liability. In those circumstances, it is difficult to see how Defence Costs, which are expressly made recoverable as part of Damages ("and shall include Defense Costs") can be recoverable even where no actual legal liability is established. That conclusion involves a subversion of language...It is true that, because the draughtsmanship of the contract is somewhat lacking in clarity, even the defendants' construction involves treating Defence Costs as a "liability...imposed by law" for the purposes of the insuring clause, but, unlike the claimant's construction, that does little violence to the language of the provisions of the contract. In any event, whatever the conundrum over how precisely Defense Costs become recoverable under this contract wording, in my judgment, the claimant cannot begin to demonstrate a free-standing provision for Defense Costs, let alone one which entitles the insured to recover defence costs even where no actual legal liability has been demonstrated.' [see paras [144] and [145] of Flaux J's judgment]

Are there any grey areas or unresolved issues remaining?

Most of the law in this area is settled and clear. This decision is novel--Bermuda Form disputes are usually subject to New York law and settled by London arbitration. This is therefore the first time the court has been asked to settle a Bermuda Form dispute, or to construe a Bermuda Form policy. It may also be surprising: the court found that AG/AIC were not entitled to an indemnity against the costs of successfully defending a claim--unless, on the balance of probabilities, they could show AG was liable for the claim it successfully defeated. Some commentators would argue that such outcome is flawed as a matter of policy as well as law. But there isn't much that's entirely new here.

All that said, there is still one grey area: absent clear words in a policy, a liability insurer is entitled to question whether an insured was liable to meet a claim before indemnifying him against the costs of settling it--and if the insured cannot show, on the balance of probabilities, that he was liable he will not be entitled to an indemnity. An English court judgment against the insured is good evidence he was liable, but that doesn't mean a challenge cannot be mounted and, if it is, the insured must still prove that he was liable as a matter of law. However, it has been suggested (by Potter LJ in *Commercial Union Assurance Co plc v NRG Victory Reinsurance Ltd, Skandia International Insurance Corpn v NRG Victory Reinsurance Ltd* [1998] 2 All ER 434), that the judgment of a foreign court is final and binding on the question of the insured's liability. Like Lord Mance in *Wasa International Insurance Co Ltd v Lexington Insurance Co; AGF Insurance Ltd v Lexington Insurance Co* [2009] UKHL 40, [2010] 2 All ER (Comm) 324, Flaux J expresses doubts about this assertion. But whether he's right to do so remains to be seen.

What are the implications of the ruling for insurance companies?

There aren't any immediate or direct consequences for other insurers and reinsurers. That's partly because this decision seems to rest on its own facts--there aren't likely to be many Bermuda Form contracts that are subject to English law. Even if there were, this was a High Court decision. It binds the parties. And it might be followed if the same issues were brought before another court in the future, but other High Court judges would not be bound to follow it.

What should lawyers take from this case?

There are probably two key lessons to take away from this decision. If you decide to change the applicable law in a contract, make sure you understand all of the consequences of doing so. There is no reason to suppose that AIC, AG, XL and/or ACE did not fully appreciate the consequences of the changes to this Policy; but if New York law had applied, the outcome of this dispute could have been quite different.

The parties to an insurance or reinsurance contract can displace or vary many principles of English (re)insurance law. When they negotiate an insurance or reinsurance contract, they should consider whether or not to do so and, if they decide to make a change, they should make that change using clear words. In particular, it would be worth considering (for example) whether to include a 'follow the settlements' clause and/or whether to impose a duty to defend on the insurer.

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Interviewed by Kate Beaumont.

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