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Client Alert

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Texas Supreme Court Finds Anadarko is Entitled to Over $100 Million in Deepwater Horizon Defense Costs Based on Undefined Term in Insurance Policy

Insurance coverage litigation arising out of the 2010 Deepwater Horizon explosion continues to result in important precedents that will impact energy companies and policyholders with operations in Texas. On January 25, the Texas Supreme Court issued an opinion that opens the door for Anadarko, one of the entities that has been ensnared in costly Deepwater Horizon litigation for nearly a decade, to recover more than $100 million for defense costs. Anadarko's insurers had refused to pay those defense costs based on their argument that a cap on recoverable damages in an endorsement to Anadarko's policy applied to defense costs, and thus Anadarko was only entitled to recover $37.5 million.[1] After carefully reviewing the insurance policy as a whole, in keeping with Texas rules of insurance policy construction, the Court rejected the insurers' argument, finding that if the insurers had wanted to cap Anadarko's right to recover defense costs, they should have said so in their policy. While this particular decision turned on the interpretation of words in a specific policy endorsement in Anadarko's policy, the holding in this case is instructive for all policyholders who purchase liability policies that provide coverage for defense costs and indemnity.

BACKGROUND

Anadarko owned a 25% interest in the Macondo Well in the Gulf of Mexico through a joint venture agreement.[2] Anadarko and its partners garnered international attention when the Macondo Well blew out in April 2010 during drilling operations from the Deepwater Horizon drilling rig causing an explosion on the rig.[3] Numerous third-parties sued Anadarko, seeking damages for bodily injury, wrongful death, and property damage.

Following years of costly litigation and an adverse ruling, Anadarko entered a settlement agreement with co-defendant BP, and agreed to transfer its 25% ownership interest in the Macondo Well to BP and to pay BP $4 billion.[4] In addition, Anadarko had spent more than $100 million on defense expenses.[5]

Anadarko had tendered the claims arising from the Deepwater Horizon catastrophe to its liability insurers (collectively, the "Underwriters") who had issued an "energy package" insurance policy (the "Policy"). The Policy provided up to $150 million in coverage per occurrence, and required the Underwriters to indemnify Anadarko for its "Ultimate Net Loss," which included "the amount [Anadarko] is obligated to pay, by judgement or settlement, as damages resulting from an 'Occurrence' covered by this Policy . . . and all 'Defence Expenses' in respect of such 'Occurrence.'"[6] However, the Policy contained a "Joint Venture Provision" that limited coverage of "any liability of [Anadarko] . . . to the product of (a) the percentage interest of [Anadarko] in said Joint Venture and (b) the total limit afforded [Anadarko]"[7]—in this instance, 25%. Despite the use of the word "liability" in the "Joint Venture Provision," the Underwriters argued that the Policy capped their coverage obligations for defense costs at 25% of the total Policy limit ($37.5 million), inclusive of both settlement payments and defense expenses.[8] In response, Anadarko argued that the Joint Venture Provision did not apply to defense costs, and capped coverage only for its liabilities to third parties (*e.g.*, settlements and judgments). Thus, Anadarko argued that the Underwriters must pay the full amount of Anadarko's defense expenses up to the Policy's $150 million per occurrence limit.[9]

Because the Underwriters refused to repay more than $37.5 million, Anadarko sued the Underwriters seeking payment of its defense expenses up to $112.5 million.[10] The trial court ruled in Anadarko's favor,[11] but the Texas Court of Appeals reversed and held that the Joint Venture Provision limited coverage to $37.5 million.[12] Anadarko then appealed to the Texas Supreme Court.

THE TEXAS SUPREME COURT OPINION

The Texas Supreme Court granted Anadarko's petition for review and held that the Joint Venture Provision did not limit coverage for Anadarko's defense expenses.[13] In reaching this conclusion, the Court found that the provision only expressly limited Anadarko's "liability . . . insured"[14] and did not specify that "liability . . . insured" included defense expenses. The Court, therefore, found that coverage turned on whether Anadarko's defense expenses constituted an insured liability arising out of the joint venture.[15] Because the Policy did not define the word "liability," the Court considered the word's common, ordinary meaning by looking at dictionary definitions and considering the word's usage in other authorities.[16] Although the dictionary definitions of "liability" referred broadly to any debt or obligation, the Court also looked at the context in which the Policy used the word, in keeping with the principle that policies should be interpreted as a whole.[17] Because other sections of the Policy "consistently distinguishe[d] between Anadarko's 'liabilities' and 'expenses,'" the Court held that the term "liability" in the Joint Venture Provision did not include defense expenses.[18] Specifically, the Court "found no policy provision that implies, indicates, or suggests that a reference to a 'liability . . . insured' includes expenses Anadarko itself incurs responding to or defending a 'Claim.' To the contrary, the policy repeatedly refers separately to 'liability' and 'expenses.'"[19] Therefore, the Court held that the Joint Venture Provision applied only to liabilities and did not reduce the Policy's limits for defense expenses.[20]

THE BROADER IMPLICATIONS OF THE *ANADARKO* DECISION

While the *Anadarko* decision dealt with the interpretation of a specific Joint Venture Provision, its holding may have much broader implications for the interpretation on liability policies, particularly those that do not provide a duty to defend. Like the Policy at issue in *Anadarko*, most directors and officers ("D&O") and errors and omissions ("E&O") policies, as well some general liability and cyber insurance policies, do not provide a duty to defend, but do require the insurer to reimburse the policyholder for defense costs, as well as damages or settlements. While the terms of such policies vary significantly, "defense costs" are typically defined separately from "damages" or other covered "loss."

Consequently, the holding in *Anadarko*, which relied heavily on the fact that the policy "consistently distinguishes"[21] between "liability" and defense "expenses," might be incorrectly used to support an argument that certain exclusions and limitations only apply to defense costs depending on how such exclusions are worded.

Most liability policies structure exclusions to bar "Loss," a defined term that explicitly includes both liability for third party claims and defense costs. However, exclusions added to form policies through manuscript endorsements and policy provisions, like the "Joint Venture Provision" at issue in *Anadarko*, may use undefined or inconsistent terms that would allow for the types of arguments that the policyholder successfully made in *Anadarko* to avoid the exclusion. If, for example, a provision purports to limit the recovery for only "damages" or "liability" for a certain excluded risk, then the *Anadarko* holding suggests that this exclusion would not limit the recovery of defense costs as long as defense costs are not included with the Policy's definition of "damages" or "liability." Similarly, if a condition in a policy purports to preclude a policyholder from assuming any "liability" without the insurer's prior consent, such a provision might not apply to defense costs or other "expenses," depending on how those terms are defined. Conversely, however, this interpretive principle may be incorrectly used by insurers in the future to argue that coverage extensions for certain "liabilities" or "damages" would not cover associated defense expenses, so policyholders should pay careful attention to these definitions when purchasing liability policies.

The recent *Anadarko* decision provides a reminder that in many insurance coverage disputes the "devil is in the details" and the specific words used in an insurance policy matter. Since insurance policies are generally interpreted as a whole to give effect to all provisions, even seemingly insignificant provisions can have a profound impact on how a policy is interpreted. Moreover, a related takeaway from *Anadarko* is that context and consistency are also important in certain situations when construing terms in an insurance policy. Accordingly, it is prudent for companies to periodically review the terms and conditions in its insurance program to determine if there may be latent coverage issues, or potential additional enhancements that could be added. Likewise, *Anadarko* shows that policyholders should not assume that an insurer's stated interpretation of exclusionary language in a coverage letter is correct, particularly when the provisions relied on by the insurers include what may be argued to be undefined terms or otherwise ambiguous language.

We work closely with our clients and their risk managers to collect from their insurers for losses arising from property damage, business interruption, and supply chain disruption caused by catastrophic events, and have obtained billions of dollars in insurance recoveries for our policyholder clients.

[1] *Anadarko Petroleum Corp., et al. v. Houston Casualty Co., et al.*, No. 16-1013 (Tex. Jan. 25, 2019).
[2] *Id.* at 3.
[3] *Id.*
[4] *Id.*
[5] *Id.* at 3-4.
[6] *Id.* at 4-5.
[7] *Id.* at 5.
[8] *Id.* at 2.
[9] *Id.* at 6-7.
[10] *Id.* at 7.
[11] *Id.*
[12] *Id.*
[13] *Id.* at 7-8.
[14] *Id.* at 8.
[15] *Id.* at 9.
[16] *Id.*
[17] *Id.* at 10-11.
[18] *Id.* at 11-12.
[19] *Id.* at 16.
[20] *Id.* at 17.
[21] *Id.* at 12.