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When the drugs don't work…who pays the price?

The recent case of AstraZeneca Insurance Co Ltd v XL Insurance (Bermuda) Ltd and another *[2013] EWCA Civ 1660* exposes the risks that policyholders face when seeking coverage for costs incurred in the course of settling and defending claims brought against them.

Where an insured has purchased insurance to protect it from claims made against it by third parties, as well as to cover the costs of defending such claims, the question will arise of whether such insurance will respond if the insured settles the claim before the matter reaches trial and before liability is decided by way of a court judgment. The *AstraZeneca* case addresses this specific question, as further described below.

The case involved a reinsurance claim by AstraZeneca's captive insurer for the cost of settling and defending large numbers of personal injury claims commenced by plaintiffs in the US and Canada in respect of a drug called 'Seroquel'. The reinsurance in question was governed by a Bermuda Form wording, which is usually governed by New York law, but this particular policy was made expressly subject to English law. AstraZeneca had settled large numbers of the personal injury claims, with only one such claim reaching trial (and being defended successfully). The captive had made sure to obtain the consent of the reinsurers before these settlement were approved. However, the reinsurer's consent was given expressly on the basis that reinsurers were not, by providing such consent, confirming that any of the settlements or defence costs incurred in defending the claims fell within the terms of the reinsurance coverage.

As to the settlement amounts, Reinsurers argued that these were not covered under the terms of the reinsurance because the Bermuda Form only covered amounts paid by reason of liabilities. As under English law (which governed the Bermuda Form) the entering into of a settlement does not necessarily establish the existence of a liability, this was something which instead depended on separate proof that, on the balance of probabilities, the insured had actual liabilities to the plaintiffs in respect of Seroquel.

The English Court of Appeal confirmed the reinsurer's interpretation of the reinsurance. In the absence of wording in the contract to the contrary, the law in England is that coverage under a liability insurance or reinsurance policy depends on proof by the insured of an actual liability, not merely that settlements had been entered into with the plaintiffs, even if those settlements were bona fide settlements entered into for genuine commercial reasons.

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The Court of Appeal also decided against the captive on the question of coverage for the defence costs. This was because there was no free-standing cover for the defence costs in the reinsurance – the defence costs cover having been added as a bolt-on to the definition of the "damages" insured by the policy. This had the effect that there was also no cover for the defence costs unless the captive had first established it had a liability for damages insured by the policy (i.e.

the same issue that arose with respect to the cover for the settlements).

Despite the reasoning of this decision, the Court of Appeal did note in its judgment that the defence costs provisions of the Bermuda Form it was interpreting were "badly drafted" and that the result it came to (i.e. that the defence cost were not covered unless the defence failed and an actual liability was found to exist) was "surprising" and "unusual" – although admittedly "not unheard of".

The finding that settlements themselves do not establish liabilities for coverage purposes under a policy covering liabilities is unsurprising. The requirement that liability be separately proved on the balance of probabilities has long been understood as what English law requires in these circumstances (unless of course the policy provides otherwise or the insurer agrees to cover the costs of the settlement)

The separate finding that the appellant also was not entitled to indemnification in respect of the defence costs is likely to attract more attention. In particular, insurers may in the future seek to ride on the coat-tails of the Court of Appeal's judgment, to argue that they are not required to indemnify insureds for the costs of defending claims which are successfully defended, with the consequence that the insured has incurred no liability for damages to which the policy in question responds. Notwithstanding that the judgement may be seized upon by insurers for that reason, in reality the outcome of the *Astrazeneca* case depended on the wording used in the Bermuda Form (and in particular the bolting-on of the cover for defence costs to the cover provided for "damages"). The case does however present at least two possible lessons for insureds and those responsible for negotiating liability insurance cover on their behalf.

First, care should be taken to ensure that policy wordings provide for separate stand-alone coverage for defence costs, rather than cover which is parasitical on the cover provided for the liabilities insured by the policy. Second, policyholders should be extremely wary of the unforeseen consequences that can follow from making a policy form that was designed with one law in mind instead expressly subject to the laws of another jurisdiction.