

WSGR ALERT

JUNE 2008

CALIFORNIA SUPREME COURT DENIES REVIEW IN D&O LIABILITY INSURANCE CASE

On June 11, 2008, the California Supreme Court denied a petition for review of the Court of Appeal's recent decision in *Qualcomm, Inc. v. Certain Underwriters at Lloyd's, London*, 161 Cal. App. 4th 184 (2008). In *Qualcomm*, the Court of Appeal relied on the language in an excess directors and officers' liability insurance policy to hold that when a company settled an insurance dispute with its primary insurer and the primary insurer paid less than the full limits of its policy, the company effectively forfeited all coverage from the excess carrier. The *Qualcomm* decision underscores the need for companies to carefully review not only their primary policies, but also their excess policies when buying insurance.

Qualcomm was a lawsuit brought by Qualcomm against its excess insurer, Lloyd's of London (Lloyd's). After Qualcomm apparently had incurred approximately \$30 million in defense and settlement expenses related to a series of stock-option lawsuits, the company reached a settlement of its coverage disputes with its primary insurer. The settlement provided that the primary insurer would pay \$16 million of the \$20 million primary insurance policy in exchange for a full release of any further claims under that policy.

Qualcomm then turned to its excess carrier, Lloyd's, for coverage. Qualcomm argued, among other things, that even though it had settled for \$4 million less than the full amount of the primary policy, the company itself had paid an additional \$4 million of loss that otherwise would be covered under the policies. Therefore, Lloyd's was not being required to pay under its policy any earlier than it had bargained for; in other words, \$20 million had been paid out by a combination of

the primary insurer and Qualcomm before Lloyd's was asked to contribute anything towards settlement or defense costs.

Lloyd's, however, refused coverage. Lloyd's argued that coverage had not been triggered because the underlying primary policy had not been exhausted. According to Lloyd's, exhaustion required that the primary insurer, and no one else, had to have actually paid the entire \$20 million policy limit in order for its obligation to be triggered.

The appellate court sustained Lloyd's demurrer to the complaint on the grounds that coverage had not been triggered. The court stressed that judicial interpretation of an insurance contract is controlled by the "clear and explicit meaning" of the written provisions of the contract, which are to be "interpreted in their ordinary and popular sense." The court then looked to the language of the policy:

Underwriters shall be liable only after the insurers under each of the Underlying policies have paid or have been held liable to pay the full amount of the Underlying Limit of Liability.

The court found that this language unambiguously required that the primary insurer actually had to have paid the entire \$20 million in order for excess coverage to be triggered. As such, the court held that Lloyd's was not obligated to reimburse Qualcomm for loss incurred unless and until the primary insurer paid the full amount on the primary policy. Because Qualcomm had released its primary insurer without requiring full payment, it effectively had forfeited any coverage from Lloyd's.

In so holding, the court rejected Qualcomm's arguments that it had a reasonable expectation of coverage in light of prior case law, which had held that excess coverage was triggered by settlement with a primary insurer. The court held that the unambiguous language of the excess policy meant what it said—the entire primary policy had to have been paid by the primary insurer before the excess policy was triggered. In this vein, the court noted that "an expectation of coverage cannot create an ambiguity; it is merely an interpretive tool used to resolve an ambiguity once it is found to exist." The court also rejected Qualcomm's argument that the court's interpretation of the policy language was against public policy.

The court's holding demonstrates that companies must carefully review not only the language in their primary insurance policies, but also in their excess insurance policies. If an excess policy contains the above cited language, a company will not be able to settle a coverage dispute with its primary insurer without risking the loss of coverage under the excess policy. Yet, excess insurers sometimes are willing to negotiate endorsements to their policies that avoid the *Qualcomm* issue; such endorsements can require the excess policy to pay out on a claim, even if the insured settles with its primary insurer for below the policy limits, provided that the insured meets specified conditions such as paying the difference between the original and the reduced primary policy limit.

Should you have any questions about this case or any of these issues, please feel free to contact Steven Guggenheim or Katherine Henderson in Wilson Sonsini Goodrich & Rosati's litigation department.

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