

## 'Additional Insured' At Stake In Texas High Court BP Case

*Law360, New York (March 12, 2014, 5:35 PM ET)* -- The Supreme Court of Texas is poised to clarify the extent of “additional insured” insurance coverage under Texas law. The court has before it two certified questions from the Fifth Circuit seeking guidance regarding the availability of additional insured coverage in the matter of *In re Deepwater Horizon*. This case deals with liabilities arising from the catastrophic oil pollution in the Gulf of Mexico in 2010 that followed the accident on the Deepwater Horizon oil drilling rig.

In the litigation, BP PLC, the oil company that owned the subsurface well that was being drilled, seeks coverage for its liabilities arising from the pollution as an “additional insured” under insurance policies issued to the owner of the drilling rig, Transocean Ltd., by Ranger Insurance Co. and Lloyd’s of London.

The Texas high court’s resolution of the Fifth Circuit’s questions will determine whether BP or Transocean is entitled to nearly \$750 million in coverage for the Deepwater Horizon oil spill. More broadly, the Texas Supreme Court’s decision in this matter will likely have major implications for both the drilling and insurance industries and impact how insurers and their policyholders deal with additional insured coverage in the future.

### The Deepwater Horizon Blowout

The events of the Deepwater Horizon oil spill are well known. In April 2010, while drilling at the Macondo Prospect, the Deepwater Horizon drilling rig experienced a major well blowout that triggered an onboard explosion and, ultimately, led to the sinking of the rig.

The oil spill caused by the blowout is considered to be the largest accidental marine oil spill in U.S. history. At the time of the explosion, Transocean Holdings Inc., owner of the offshore drilling unit, was engaged in drilling activities on behalf of BP American Production Co. and its affiliates under a drilling contract between BP and Transocean’s predecessors. BP’s total costs associated with the Deepwater Horizon oil spill are estimated to exceed \$42 billion.

The drilling contract defined BP’s and Transocean’s respective obligations, including the pollution liabilities each assumed. As is standard industry practice under the drilling contract, BP assumed liability for pollution originating below the surface of the water (i.e., pollution originating from the well) and Transocean assumed liability for pollution on or above the surface of the water (i.e., pollution originating from the drilling rig).

The drilling contract required Transocean to maintain insurance covering the operations to be performed under the contract and to name BP as an “additional insured.” Specifically, the contract

provided that “[BP] shall be named as [an] additional insured in each of [Transocean’s] policies, except [w]orkers’ [c]ompensation for liabilities assumed by [Transocean] under the terms of this [c]ontract.”

### **The Ensuing Insurance Litigation**

Following the blowout, BP sought coverage for its losses under Transocean’s primary and excess policies as an “additional insured.” Both Transocean’s primary and excess insurers denied any obligation to provide coverage for BP as an additional insured because the polluting incident — the blowout of the well — originated below the surface of the water and Transocean had not agreed to assume liability for such pollution.

Transocean’s insurers filed suit in the U.S. District Court For The Eastern District Of Louisiana seeking a declaratory judgment that BP’s additional insured coverage was limited to the liabilities Transocean assumed under the drilling contract and, therefore, the insurers were not obligated to indemnify BP for the Deepwater Horizon incident. Transocean, the owner of the rig, intervened in the case, aligning itself with its insurers on the additional insured issue.

BP sought judgment on the pleadings, relying in part on the Texas Supreme Court’s decision in *Evanston Insurance Co. v. ATOFINA Petrochemicals Inc.*, and arguing that, under that case, the insurance policies alone governed the scope of BP’s coverage as an “additional insured” under the policies and the drilling contract and its indemnity provisions were irrelevant to that issue.

The district court disagreed with BP. The court found the ATOFINA case to be distinguishable, and focused on the language in the drilling contract that required BP to be named as an “additional insured[] in each of [Transocean’s] policies ... for liabilities assumed by [Transocean] under the terms of the contract.”

Because Transocean had not assumed liability under the contract for subsurface pollution, the court concluded that BP’s additional insured coverage under the policies did not extend to such pollution. The district court granted summary judgment in favor of Transocean and its insurers.

### **The Initial Fifth Circuit Decision**

BP appealed to the Fifth Circuit. That court reversed the district court and held that BP was an additional insured under the Transocean policies for liabilities arising from the subsurface pollution.

The Fifth Circuit found the “insurance policy itself — not the indemnity provisions of Transocean’s and BP’s contract — controls the extent to which BP is covered for its operations under the drilling contract.” Because the policy “imposes no relevant limitations” on the extent of BP’s additional insured coverage, the court concluded that BP had coverage for its liability for the subsurface pollution.

The court, relying on ATOFINA, said that, when determining the scope of additional insured coverage under Texas law, the court should “look to the terms of the ... insurance policy itself, instead of looking to the indemnity agreement in the underlying service contract.”

Again citing ATOFINA, the court said that this analysis applied “so long as the indemnity agreement and the insurance coverage provisions [in the service contract] are separate and independent.” Having determined that the Transocean policies imposed no relevant limitation on additional insured coverage for BP, the court turned to the drilling contract and determined that the indemnity agreement and the

insurance coverage provisions in that document were, in fact, separate and independent.

### **The Fifth Circuit's Two Questions for the Texas Supreme Court**

Six months after its initial decision, the Fifth Circuit, upon rehearing, withdrew that decision and instead certified two questions to the Texas Supreme Court. The court did so “[b]ecause this case involves important and determinative questions of Texas law as to which there is no controlling Texas Supreme Court precedent.”

The questions are:

1. Whether [Atofina] compels a finding that BP is covered for the damages at issue, because the language of the umbrella policies alone determines the extent of BP’s coverage as an additional insured if, and so long as, the additional insured and indemnity provisions of the drilling contract are “separate and independent?”
2. Whether the doctrine of contra proferentem applies to the interpretation of the insurance coverage provision of the drilling contract under [Atofina], given the facts of this case?

The court said that the certification was triggered by uncertainty about the outcome under Atofina and noted that the second question was relevant if the issue of how to interpret the drilling contract arose.

### **Parties’ Positions on the Certified Questions**

#### ***Does Atofina Compel a Finding in Favor of BP?***

Regarding the first certified question, BP asserts that the Atofina case compels a finding that BP is covered for its pollution liabilities because, under Atofina, the language of the policies alone should determine the scope of BP’s additional insurance coverage and, here, the Transocean policies contain no relevant limitation on the scope of that coverage.

BP argues that, under Atofina, the court should not look at the underlying drilling contract for purposes of determining the scope of coverage. BP argues that “no principled distinction” exists between the present case and Atofina, and several similar cases. BP points out that two leading treatises which deal with additional insured coverage indicate that, once additional insurance coverage is granted, that coverage applies to the full extent of the policy, and the additional insured enjoys the full benefits of the policy. BP states that no language in the Transocean policies has ever been identified that limits the scope of BP’s additional insured coverage to the scope of the contractual indemnities in the drilling contract.

Transocean and its insurers vehemently disagree with BP’s position. They assert that Transocean’s policies, unlike the policy in Atofina, contain language that refers to and incorporates the underlying drilling contract for purposes of determining the scope of additional insured coverage. They posit that the policies and the underlying contract specify the scope of BP’s coverage as an additional insured and limit the coverage to liabilities assumed by Transocean under the drilling contract.

Transocean and its insurers argue that the Atofina case’s “policy only” rule of coverage interpretation, which BP advocates, would inject uncertainty into the interpretation of thousands of existing policies

covering drilling operations. Taken to its logical extreme, they assert that BP's interpretation would remove the only limit on additional insured coverage, thereby making Transocean — and its insurers — potentially liable to provide coverage for BP's activities worldwide.

Transocean and its insurers note the Fifth Circuit has previously recognized in a number of non-Texas "additional insured" cases that the provisions of the underlying service contract must be considered in determining the scope of an additional insured's coverage under the insurance policy in question. They cite *Becker v. Tidewater Inc.* (5th Cir. 2009) and similar cases, which they argue the Texas Supreme Court should find persuasive.

Ranger points the Texas Supreme Court to *Urrutia v. Decker* (Tex. 1999), and similar cases in which that court has held that an insurance policy may incorporate a separate contract by reference and, when that occurs, a court should apply all the provisions of the incorporated contract. Hence, Ranger contends that the drilling contract was incorporated into the Transocean policies, and that the limitations in the contract on Transocean's indemnity obligations must be read to limit the scope of additional insured coverage for BP.

Transocean argues this case differs from the cases BP relies on because the dispute here is between the named insured and an additional insured, not between the named insured and the insurer. Transocean posits that BP is a major company that chose to self-insure, whereas Transocean chose to insure its liability, and the question is whether Transocean's insurance will go to cover BP's liabilities. Transocean asserts that the additional insured coverage is limited to that which is required by the "[i]nsured [c]ontract" for indemnification obligations of the named insured, because the insurers can assess and underwrite such risks based upon the operations of the named insured.

### ***Does Contra Proferentem Apply to the Drilling Contract?***

BP argues that ATOFINA correctly applies the well-established rule that uncertainties in an insurance policy's language should be construed in favor of coverage for the insured, and so BP should be given the benefit of any doubt about whether additional insurance coverage should exist under the Transocean policies for BP's liabilities for subsurface pollution arising from the Deepwater Horizon blowout.

In opposition, Transocean and the insurers argue that: (1) all parties supposedly agree that no ambiguity exists in the documents, so the contra proferentem principle does not apply here, (2) the insurers had no role in the drafting of the drilling contract, so the principle should not be applied to construe that document against them and (3) in any event, the court should find a "sophisticated insured" exception to the principle in this case because BP was a major company that would have stood on equal footing with the insurers in any negotiation.

### **Awaiting the Wisdom of the Texas Supreme Court**

If the Texas Supreme Court believes the additional insured issue should be resolved in favor of BP, the court could accept the company's focus on the ATOFINA case and rule that the "policy only" approach in that case precludes reference to the drilling contract to limit the scope of the additional insured coverage for BP.

On the other hand, if the court concludes the issue should be resolved in favor of Transocean and its insurers, the court could do so in a number of ways. It could distinguish ATOFINA from the present case

because the policy language in the Transocean's policies differs from that in ATOFINA's policies and directs the parties to the drilling contract to determine the scope of BP's additional insured coverage. The court could rely on its earlier rulings Urrutia and similar cases to conclude that the drilling contract was incorporated by reference into the Transocean policy and, thus, limit the scope of BP's additional insured coverage to the indemnity obligation assumed by Transocean in the drilling contract.

Whatever the court's resolution is it will have a significant impact on the drilling and insurance industries. If BP wins, drilling contractors and their insurers will have to go back to the drawing board with their insurance policies and drilling contracts if they want to effectively limit the owner/operator to additional insured coverage for the drilling contractor's indemnity obligations.

If Transocean and its insurers win, owners and operators who want expanded additional insured coverage will need to negotiate new provisions to that effect in the existing industry standard drilling contract. The stakes are high.

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