

June 17, 2020

California – Ninth Circuit Holds D&O Policy Only Requires Advancement of Defense Expenses for Actually Covered Claims, Not Those That Are Only Potentially Covered

BY:

On June 17, 2020, in an unpublished decision, the Ninth Circuit affirmed a ruling by the Central District of California in *U.S. TelePacific Corp., AKA TPx Communications v. U.S. Specialty Ins. Co.*, which found that, under the D&O liability insurance policy in the case before it, the insurer had no duty to advance any of the defense costs incurred by the insured. U.S. TelePacific Corp, doing business as TPx Communications, was faced with two wage-and-hour class action lawsuits which were eventually consolidated into one action. TPx tendered the lawsuits to its D&O policy insurer, U.S. Specialty Insurance Company. After Specialty denied coverage and refused to advance the defense costs, TPx brought suit against Specialty for breach of contract and of the implied covenant of good faith and fair dealing. The district court found in favor of Specialty on its motion for judgment on the pleadings, and TPx appealed.

The D&O policy stated that the insurance company had no duty to defend but it did provide for advancement of defense expenses under certain situations. TPx's proposed interpretation of the policy language would require Specialty to advance defense costs for any *potentially* covered claim, similar to the traditional duty to defend language. The Ninth Circuit quoted specific Policy language that requires Specialty to "advance defense costs for claims 'for which [the] Policy provides coverage,'" "pay only those amounts properly allocated as 'covered matters,'" and, where there is a dispute over whether a claim is covered, "Specialty will advance defense costs only for the portion 'which the parties agree is not in dispute.'" The Ninth Circuit concluded that TPx's interpretation was unreasonable based on the clear and unambiguous language in the policy. The court found that Specialty's duty to advance TPx's defense costs under the language of the policy only extended to claims that were *actually* covered by the policy.

In looking to see if there were covered claims in the underlying wage and hour actions as to which the advancement of defense costs might be necessary, the Ninth Circuit found that the district court did not err in holding that the claim for failure to pay wages upon termination in a timely manner was precluded by the policy's definition of "Loss." "Loss" as defined in the Policy excludes "penalties" from coverage, and under the California Labor Code, the relief available for failure to pay wages in a timely manner upon termination is "a penalty." The Ninth Circuit further found that Exclusion (L), which barred claims for losses relating to the Fair Labor Standards Act or similar provisions in federal, state or local law, applied to the causes of action in the underlying lawsuit involving claimed violations of the California Labor Code. Finally, the court found that Exclusion (F), barring coverage for claims made by employees against TPx, "except where a claim is for an actual or alleged "Employment Practices Wrongful Act," excluded coverage for all the claims in the underlying suits because those claims did not fall within the definition for that term.