Summer 2010

Perspectives
on Insurance Recovery

pillsbury

Welcome to Perspectives on Insurance Recovery, *a newsletter from Pillsbury's Insurance practice. From long experience, we know just how time-consuming it can be to keep up on the latest developments and trends in commercial insurance coverage. Our goal is to relieve some of that burden for our clients by sharing our latest information and insights with you.*

Whether you need an advocate in an unexpected dispute or some advice on the adequacy of your coverage, Pillsbury attorneys are at the leading edge in securing insurance coverage for corporate clients.

Article Highlights

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Preparing Your Business for the 2010 Atlantic Hurricane Season

by Vince Morgan

The Atlantic hurricane season officially runs from June 1 to November 30, though peak activity usually occurs in August and September. With the beginning of tropical storm activity just around the corner, now is the time to prepare your company and review your insurance coverage for what may lie ahead in the coming months.

Predictions for 2010

The upcoming Atlantic hurricane season will be busier than average, according to some atmospheric researchers, thanks to tropical sea surface temperatures that are warming combined with a weakening El Niño effect. No one can predict how many storms will make landfall, but even one may be enough to cause massive losses.

Steps to Prepare Your Company

Though it is impossible to predict precisely if, and where, this year's storms may make landfall, it is prudent for companies with significant exposure to the Eastern and Gulf coast regions to prepare as if a storm is headed their way. With that approach in mind, here are some steps that

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Taking a Gamble on Litigation

Pillsbury recently concluded a contentious federal lawsuit over the acquisition of a startup Internet company via a novel strategy: poker.

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Preparing Your Business for the 2010 Atlantic Hurricane Season

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can be taken now to prepare ahead of time, which should be part of the company's disaster and business continuity plan.

Review Your Policies, and Adjust Them if Necessary

The time to review your company's policies is now, not after a storm has passed. Scenario planning is an excellent way to identify potential gaps in coverage as well as challenges the company might face in the aftermath of a storm. For example, preparing a hypothetical claim for a Category 3 storm at a key facility should present a fairly realistic picture of potential losses and how the policies will likely respond. To the extent that this process identifies any deficiencies in coverage, or perhaps asset schedules and related policy information that needs to be updated, now is the time to take care of these details to avoid disputes in the future.

Understand Key Coverages

Protecting the Company's Property

A company's commercial property policy is usually the starting point for protecting its tangible property. Ensuring that the policy carries adequate limits, based on a current fixed-asset verification, is critically important. Additionally, the policy should be carefully examined for exclusions, deductibles and internal sublimits that may reduce available proceeds. Further, some policies place conditions on where insured property can be located to be covered, such as within a certain distance from a covered location.

Protecting the Company's Income

Covering tangible property itself is usually not enough to make most businesses whole in the aftermath of a natural disaster. It may take weeks, months, even years to fully restore the company's revenue produced by these assets. Thus, there are a number of "time element" coverages that serve to protect against such losses. These include:

- *Business Interruption Coverage*: Business interruption coverage protects a company against the revenue lost as a result of covered damage to the company's own property. For example, if a hurricane causes damage to a company's facility, which then results in downtime while the property is being repaired or rebuilt, business interruption coverage provides protection against this lost revenue.
- *Contingent Business Interruption Coverage*: Hurricanes typically cause widespread damage to affected areas. As a result, a company's key suppliers or customers might also suffer outages that affect the company's ability to conduct its normal business operations. Contingent business interruption coverage protects against losses due to these disruptions.
- *Civil and Military Authority Coverage*: In the aftermath of a disaster, and occasionally beforehand with approaching storms, government authorities may issue evacuation orders and other constraints on access to certain areas. After the September 11 terrorist attacks, parts of Manhattan were off-limits for several days. Likewise with Hurricanes Katrina and Rita. Most commercial property policies provide coverage for losses arising out of prohibitions against access due to orders from a "civil or military authority."
- *Service Interruption Coverage*: Service interruption coverage is designed to protect against losses that result from the interruption of utilities such as water, power, communications or similar services.

Prepare for Initial Post-Storm Activities

Steps taken in the immediate aftermath of a storm are critical to preserving and maximizing a company's insurance recovery, as well as ensuring that the company's business levels return to normal as quickly as possible. From the standpoint of insurance, these steps include: (i) notifying all carriers in accordance with the policies; (ii) forming a claims team, utilizing both internal personnel from the risk management, operations, legal and accounting functions as well as external claim consultants and coverage counsel; (iii) setting up separate accounts to track post-claim losses and expenses incurred in the recovery efforts; and (iv) establishing and observing effective claim management procedures to avoid disputes and streamline the process, such as preservation of the carrier's salvage rights, protecting covered property against further loss and seeking advances against the ultimate loss payment.

Hurricanes Can Wreak Havoc on Your Business

Hurricanes that make landfall often cause enormous damage. Having a properly managed insurance recovery process, however, can mitigate a storm's impact on your business.

IN THE NEWS
Recent Pillsbury Representations

Pillsbury's Insurance Recovery & Advisory practice has been quite busy so far in 2010, handling a number of insurance matters for incidents that have made front pages of newspapers across the globe. Some of our most recent representations include:

- An international airline on its business interruption claims related to Iceland volcanic ash
- A property owner, retail operator and musical instrument manufacturer on claims related to recent flooding in Nashville
- A major party involved in the Deep Horizon well blowout in the Gulf of Mexico
- Former directors and officers in connection with claims arising out of one of the largest credit union failures in U.S. history

To learn more about our practice, please contact Peter M. Gillon at 202.663.9249 or email peter.gillon@pillsburylaw.com.

D&O Plus: Pillsbury's D&O Policy Advocacy Program

D&O insurance is one of the most important safeguards a company and its directors and officers have against allegations of wrongdoing by activist investors, aggressive plaintiffs' firms and the SEC. Public and private companies purchase D&O coverage to protect management and outside directors against the ever-changing risks of litigation in a world where their decisions are frequently second-guessed, and it is critical to a company's ability to attract and retain strong directors and officers.

Yet, despite the importance of D&O coverage as a bulwark against personal and corporate exposure, most people are surprised to learn that the scope of coverage, as reflected in the terms and conditions of the D&O policy, is highly negotiable. No sooner does an insurer issue a revised policy form to exclude more claims than brokers and policyholder counsel have prepared extensive "endorsements"—customized amendments that materially enhance the scope of coverage. Likewise, coverage terms may be tailored to a company's unique circumstances, such as a merger or sale, an IPO or a liquidation.

The manuscripting of D&O policies is driven by a number of factors. Over the past decade, insurers have sought to minimize their exposure to certain types of claims through denials of coverage and litigation over the meaning of key terms. On issues where policyholders have succeeded in overcoming insurers' defenses, insurers have sought to narrow the scope of coverage afforded in their policies by revising their forms with more restrictive terms and conditions. Not surprisingly, larger companies—especially the ones buying more insurance—have withstood these contractions in coverage terms with greater success.

Paradoxically, in 2010, notwithstanding the financial meltdown of 2008–2009, the D&O insurance market has remained remarkably "soft." That is, most policyholders have largely retained the ability to purchase D&O coverage at record low rates and with advantageous terms. The keys to success in this arena are market knowledge, up-to-date understanding of the rapidly evolving case law on D&O insurance and capable advocacy—unique skills that can be found only in the top brokers and coverage counsel.

D&O Policy Advocacy

Pillsbury's D&O Policy Advocacy program provides our clients with those critical skills, deployed to secure significant enhancements to our clients' D&O policies. We work closely with our clients' insurance brokers to place and negotiate improvements to coverage: drafting and negotiating manuscripted policy wordings; advising on coverage towers and Side A structures; modifying policies to address recent case law developments; and, more generally, advocating for state-of-the-art coverage. And, of course, when a claim or potential claim arises, the Pillsbury team is available to advise and, if necessary, litigate to enforce our clients' coverage rights.

Frequently Asked Questions

Why D&O coverage and not property or E&O coverage, for instance?

In fact, we provide the same service on all forms of coverage, but the zone of potential improvement and the value of the exercise are usually greatest for D&O policies.

How often should this be done?

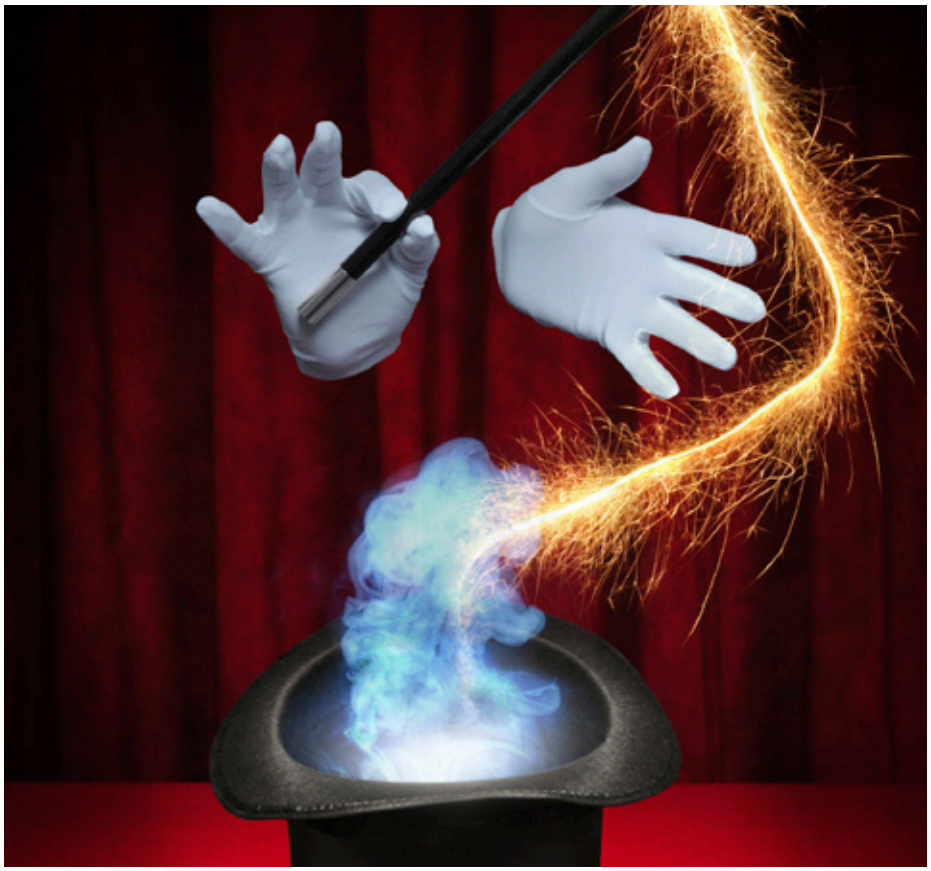
For some of our clients, this is an annual process, and policy wording enhancements may evolve slowly, yet inexorably, in our clients' favor. Other clients consult us only when they have a particular transaction or exposure they are concerned about.

What does a D&O policy review cost?

The D&O Plus program may be performed on a reasonable, flat-fee basis, with the cost dependent on the complexity of the coverage. Our clients, particularly boards and management, have been unanimous in their opinion that the program provides tremendous value.

Will this offend my broker?

Not the good brokers. The top D&O brokers regularly recommend a "second look" by counsel and frequently refer their valued clients to Pillsbury. We complement, but do not replace, your broker. A good insurance broker is uniquely qualified to take your insurance application to market, work with the underwriters and advise on market issues such as the amount of limits being purchased by peer companies. But good brokers will admit that drafting and revising policy language is not their bailiwick. Our strong relations with the top brokers and insurers are key to our success.



Misdirection: The (Rising?) Use of Unstated Exclusions to Deny Coverage

by Peter M. Gillon and James P. Bobotek

In magic it is called misdirection. "Look at the floating bikini-clad lass seeming to defy gravity," the magician suggests, "and look at the hoop passed around her to prove there are no wires; but ignore the fact that the hoop has gaps in it to pass over the wires."

Misdirection is practiced by insurance companies with what I perceive to be increasing frequency when denying claims. It may take several forms, but one of the most common is the fabrication of an implied policy exclusion or forfeiture clause notwithstanding the fact that a claim otherwise falls within the basic insuring agreement. Policyholders should be careful to identify such misdirection when it occurs. Once the fallacy is revealed, the courts generally find the misdirection unacceptable and hold in favor of the insureds.

This situation arises most commonly when an insurance company or its counsel makes the argument that a claim is not covered, due to an unstated exclusion the insurer reads into the policy based upon an interpretation of policy language, the policy "taken as a whole" or even public policy—despite the fact that an express grant of coverage in the policy addresses the precise issue. That grant of coverage may appear in an insuring agreement, a specific endorsement or a carve-out from an exclusion. Such insurer arguments may violate several general rules of insurance contract interpretation: the rule that a court must give meaning to all contract terms and not render a provision (such as a coverage grant) surplusage; the rule that exclusions, exceptions or limitations to coverage "are strictly construed against the insurer ... [and therefore a] risk that comes naturally within the terms of a policy is not deemed to be excluded unless the intent of the parties to exclude it appears clearly, so that it cannot be misconstrued;" or the rule that insurance policies "must not be so construed as to work a forfeiture, unless by clear and unambiguous language, readily understandable ... by businessmen of average intelligence ... ." On the other hand, in some circumstances, an exception to a policy exclusion cannot, by itself, create coverage where the coverage is not otherwise provided by the policy.

Court Case Examples

Insurers attempt to argue the existence of unstated, implied, or, to call a spade a spade, fabricated exclusions across all lines of coverage, from CGL to D&O. Here are a few notable examples from the case law.

In *Hotel des Artistes, Inc. v. General Acc. Ins. Co. of America*, 9 A.D.3d 181, 775 N.Y.S.2d 262 (N.Y. A.D. 2004), a hotel restaurant that was damaged in a fire sued the hotel operator for loss of income due to the hotel's failure to meet its lease obligations to complete repairs in a timely fashion. The hotel tendered the claim to its CGL insurer under a standard policy covering amounts the insured is "legally obligated to pay as damages because of bodily injury and property damage to which the insurance applies." The policy also contained a standard contractual liability exclusion that excepted from its scope any "insured contract," including any lease. The insurer denied the claim on the ground that the CGL policy generally does not provide coverage for losses caused by the insured's failure to perform its contractual obligations. The appellate court made short shrift of this argument. The underlying claim by the restaurant for breach of the lease following a fire fell

squarely within the insuring agreement, the court held, and the insurer conceded that the contract exclusion did not apply. The court rejected the theory that the policy contains an implicit exclusion for "contractual obligations" as contrary to the general rule that "the insurer must establish that the exclusion is stated in clear and unmistakable language, is subject to no other reasonable interpretation, and applies in the particular case. [citations omitted] Further, 'policy exclusions are not to be extended by interpretation or implication, but are to be accorded a strict and narrow construction.' "

In simpler terms, the express contractual liability exclusion set forth the bargain struck by the insured and the insurer as to which contractual claims were covered and which were not. Any other policy terms should be construed to give meaning to the expressly delineated provision and not to render it meaningless.

Anti-Policyholder Decisions

An appellate court violated these principles in *CNL Hotels & Resorts, Inc. v. Twin City Fire Insur. Co.*, 291 Fed. Appx. 220, 2008 WL 3823898 (11th Cir. 2008). There, the court accepted an insurer's argument under a directors and officers' liability policy that public policy concerns trump these principles of construction. CNL had been sued by its shareholders under Section 11 of the Securities Act of 1933 for damages as a result of a stock offering that allegedly overvalued the stock price by $8 per share. The class action was settled for $35 million, and CNL sought coverage under the D&O policies. The insurers denied the claim, arguing that the settlement amount constituted disgorgement of "ill-gotten" gains that did not constitute a "loss" within the meaning of the policy, citing *Level 3 Communications, Inc. v. Fed. Ins. Co.*, 272 F.3d 908, 910 (7th Cir. 2001) (another anti-policyholder decision by Judge Richard Posner). The court agreed, concluding that the return of money obtained by the insured through violation of law, even if the insured was innocent in committing the violation, is not a "loss." Yet the panel (and the district court below) rejected CNL's argument that the insuring agreement explicitly covered claims under the Securities Act of 1933, of which Section 11 is a part. Thus ignoring the express grant of coverage for the exact claim at issue, the court chose to fabricate an exclusion based upon a public policy-driven interpretation of "loss." Again, by misdirection, the insurer was able to keep the court's eyes deflected from the parties' understanding, as reflected in the stated wording of the coverage grant.

Finally, in a recent case, *Dyncorp. v. Certain Underwriters at Lloyd's, London*, C.A. No. 08C-09-218 (D. Del. Nov. 9, 2009), the court addressed a claim for coverage under aviation liability policies for lawsuits brought by landowners allegedly damaged by Dyncorp's aerial spraying to eradicate drug crops in Columbia. The insurer denied coverage, in relevant part, under the policy's pollution exclusion. However, the insured pointed out that the policy included a separate exclusion for aerial spraying that excepted from its scope spraying that was declared to the insurers, which the insured had done. In granting summary judgment for the insured on the duty to defend, the court relied on the more specific provision, which afforded coverage for the "spraying" claims, concluding that "if the spraying operations of Plaintiffs were intended to fall under the Pollution Exclusion, there would not be a need to have a separate exclusion for undeclared 'crop dusting' and 'spraying.'"

Is There a Trend?

These cases illustrate the variety of contexts in which an insurer may deny coverage by misdirecting attention away from an express grant of coverage to an unstated exclusion or from an exclusion's express carve-out to a less specific exclusion. And they show the divergence in the approaches the courts will take in response. I have seen no reliable data to support the hypothesis that the reliance on such unstated exclusions is on the rise, but, from a sampling of the claims that our practice group has been asked to handle, that appears to be the case. I would be grateful to receive other examples or data on this point.

Rene Siemens Joins Firm

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Rene Siemens has joined Pillsbury's Litigation and Insurance Recovery & Advisory practices as a partner in the firm's Los Angeles office.

Rene's insurance coverage practice ranges from large environmental and product claims to complex property and business interruption losses; disputes under director and officer, errors and omissions, and fiduciary liability policies; and issues under most other kinds of coverage (including advertising, aviation, bond, clinical trial, credit, earthquake, employment liability, insolvency risk, Internet, life, media, mold, nuclear, intellectual property and workers' compensation). He has served as lead or co-lead counsel in coverage cases in state and federal trial and appellate courts around the country, including the U.S. Supreme Court, often in matters involving issues of first impression.

A graduate of Harvard Law School, Rene holds DPhil and BPhil degrees from Oxford University and a BA from the University of Winnipeg.

"In addition to his insurance recovery experience, Rene is also widely experienced in other complex litigation matters including product liability, mass tort, environmental and consumer class actions. Rene will be a terrific addition, bolstering our commitment to grow and expand in Los Angeles and throughout Southern California."

—Pillsbury Firm Chair James M. Rishwain, Jr.

Agoglia Shows the Importance of Reading the Fine Print in Excess D&O Policies

by Peter M. Gillon

A March 2010 ruling by the U.S. Court of Appeals for the Second Circuit, affirming the decision of District Court Judge Gerard Lynch in *XL Specialty Ins. Co. v. Agoglia*, 2009 WL 1227485 (S.D.N.Y. Apr. 30, 2009), provides an object lesson in the importance of reviewing excess D&O policies for conformance to the primary policy. *Murphy v. Allied World Assurance Company (US), Inc*., No.s 09-1362-bk(L), 09-1365-cv (Con) (2d Cir. Mar. 23, 2010).

Agoglia is a D&O coverage dispute arising from the collapse of Refco, brought on by the revelation at the time of Refco's IPO that the company had a $435 million receivable from an entity controlled by its CEO, Philip Bennett. There was little question that Bennett's knowledge of this receivable, established in Bennett's stipulated judgment, precluded coverage for him under the company's D&O policies by operation of the "prior knowledge" exclusion, which bars coverage where any insured had knowledge of facts which are likely to give rise to a claim at the inception of the policy. The key issue was whether coverage was preserved for the innocent directors and officers.

Severability of Coverage

The Refco primary policy included a severability of knowledge provision, also known as a "non-imputation" clause, the effect of which in this circumstance is that prior knowledge of claims by one director would not cause forfeiture of coverage for innocent directors. The dispute centered on whether the severability provision applied to the supposedly "follow form" excess policies. At the time of binding, the broker furnished the insured a "binder" (in effect a policy summary without the actual policy wording) for what were labeled "follow form" excess policies. The binder for the third- and fourth-layer excess policies referenced an "Inverted Warranty Endorsement as of Inception," which, when the policy was issued, turned out to be a broad, joint and several exclusion for all claims "arising out of" any "facts and circumstances of which any insured had knowledge as of inception" of the policy and which a "reasonable person would suppose might afford valid grounds for a [covered] claim."

Does Excess Follow Form?

The "innocent" directors and officers first argued that the severability endorsement in the primary policy should be construed to apply to the follow-form excess policies despite the more restrictive exclusion in the excess. That is, the excess policies followed form to the primary, except where the excess contained contradictory provisions. Here, the insureds argued, the policies could be construed consistently by permitting the more restrictive prior knowledge exclusion to apply only to the individual with the prior knowledge. Judge Lynch disagreed, concluding that the more restrictive exclusion in the excess referenced the knowledge of "any insured" and was thus irreconcilable with the severability clause in the primary. The Second Circuit concurred.

Perhaps the stronger argument made by the "innocent" directors and officers in the district court and on appeal was that the excess insurers were precluded from relying on the inconsistent "prior knowledge" exclusion in the excess policy because they failed to put the insureds on notice of the conflicting exclusionary wording in the excess policy at the time the policy was issued. However, Judge Lynch concluded that Refco had ample warning, quoting the binder reference to an "Inverted Warranty Endorsement" combined with correspondence between the broker and the excess insurers stating: "Refco prefers not to sign any warranties. Should you need one to bind, please include an inverted warranty endorsement on your revised quote." Again, the Second Circuit agreed.

Although the actual facts are unknown to this author, this may have been a situation in which Refco was cognizant of the implications of the insurers' request for a warranty of no knowledge of pending claims and chose to avoid such a clear (and potentially false) warranty—opting instead for a less onerous prior knowledge exclusion. Nevertheless, innocent directors and officers should never be exposed to this type of coverage gap—a strong argument for purchase of non-rescindable Side A DIC coverage or segregated Side A limits for independent directors.

Lessons Learned

Looking at this case from 30,000 feet instead of the ground level, the lessons here are fairly stark. One, a policyholder should never agree to bind excess coverage without reviewing and understanding all of the terms and conditions that may vary from the primary. Two, there is almost never a reason for the terms of an excess policy to vary materially from the primary—particularly on the wording of a critical exclusion such as for prior knowledge or pending claims. And three, to add some lessons born of recent experience in other cases, the excess policies should contain compatible dispute resolution clauses to avoid having to litigate with the primary in New York and to arbitrate with one excess in London and another in Bermuda.

Taking a Gamble on Litigation

by Robert L. Wallan and Mariah Brandt

We recently concluded a contentious federal lawsuit over the acquisition of a startup Internet company via a novel strategy: poker. The $50 million acquisition closed on the eve of the recession, and within a year the entrepreneurial parties were trading allegations ranging from misrepresentations to accounting improprieties to large payment breaches. Multiple mediation sessions narrowed the case considerably, but both sides had claims they refused to drop. As trial approached and the costs of litigation increased, the parties engaged in a final lengthy mediation. The result: the parties agreed to avoid gambling with a jury and instead resolve their disputes via a high-stakes game of no-limit Texas Hold'em.

Rather than long days of trial, the case was settled at a card table in Las Vegas. The principals and their respective entourages convened in a casino's private card room, ordered cocktails and settled in for what was anticipated to be a several-hour match. But only 15 minutes and 12 hands into the day, the principals went "all in." While Texas Hold'em is a game of skill, it is good to be lucky—an extremely rare straight flush dealt to our client could not be beat.

An unconventional settlement? Definitely. Something that would work for a public company's board of directors? Definitely not. But in the end, this was a creative (and far more entertaining) strategy for two private companies to reach a cost-effective case resolution.

Stanford Financial Scandal Begets New Judicial Guidance on D&O Coverage

by Rene L. Siemens

The Fifth Circuit's March 15, 2010, opinion in the Stanford Financial D&O insurance coverage case contains important lessons for every policyholder. In particular, the opinion shows how important it is for directors and officers to review—and demand improvements to—their insurance policy language before they are faced with potentially ruinous claims. It also confirms that even if directors and officers find themselves stuck with less than optimal policy language, their insurers cannot simply cut off their defense funding unilaterally but must first obtain a court ruling that the claim is excluded.

The Fifth Circuit's opinion arises out of the district court's entry of a preliminary injunction against two insurers, requiring them to pay for the defense of Allen Stanford and several other executives facing civil and criminal proceedings that allege they ran a massive Ponzi scheme. After one of the defendants pled guilty, the insurers unilaterally denied coverage for the others under the policies' "money laundering" exclusion, which required the insurers to pay the insureds' defense costs only "until such time that it is determined that the alleged act or alleged acts did in fact occur."

Under the personal conduct exclusions found in many D&O policies, an insurer is expressly allowed to deny coverage only if there is a "final adjudication" that the insured engaged in the excluded conduct. Courts have universally interpreted this wording as requiring the insurer to pay defense costs unless and until there is a final adjudication of wrongdoing in the third-party proceeding against the insured. Under exclusions that require a "final adjudication," therefore, the insurer cannot deny coverage—let alone deny coverage unilaterally—if the insured settles the claim before suffering an adverse judgment.

Insurers Sought an Out

In the Stanford Financial case, the insurers unilaterally denied coverage on the basis that their exclusion only required a

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Stanford Financial Scandal Begets New Judicial Guidance on D&O Coverage

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"determination" (not a "final adjudication") that the excluded conduct had "in fact" occurred. The insurers argued that since the exclusion did not specify that a court needed to make the "determination," they were entitled to determine whether the exclusion "in fact" applied and then cut off their insureds.

The Fifth Circuit, applying the rule that ambiguous exclusions must be interpreted narrowly and in favor of the insured, rejected the insurers' argument and held as a matter of law that "determination ... in fact" requires a judicial decision that the excluded conduct actually took place. Under such policy wording, an insurer must continue paying the costs of defending its insured unless and until the insurer obtains a judicial determination that the insureds have "in fact" engaged in the excluded conduct.

Noting, however, that a "determination" is not necessarily the same as a "final adjudication," the Fifth Circuit held that the insurers were entitled to seek a decision regarding the exclusion's applicability in a separate, parallel coverage action, without waiting to see how the factual issues were adjudicated in the underlying proceedings. Because the exclusion required the insureds to repay any costs that turned out to be uncovered, the insurers could potentially recoup the costs they had paid if they managed to prove that the insureds had "in fact" engaged in excluded conduct. *Pendergest-Holt v. Certain Underwriters at Lloyd's of London, et al.*, 2010 WL 909090, No. 10-20069 (5th Cir. Mar. 15, 2010).

The Decision's Impact

The Stanford Financial opinion contains four important lessons for policyholders. First, it adds to the growing body of cases holding that insurers cannot simply abandon their insureds by unilaterally determining that they have engaged in wrongful conduct. To the contrary, as the Fifth Circuit explained, insurers are "contractually bound to reimburse reasonable defense costs until [a] merits decision is reached."

Second, although the district court issued a preliminary injunction against the insurers, it is unnecessary for the insured to jump the often expensive hurdle of obtaining an injunction against a recalcitrant insurer. Given that the insurer is "contractually bound" to pay defense costs until it can prove that an exclusion applies, the policy language alone precludes the insurer from refusing to pay. As the Fifth Circuit put it, "[t]he practical effect of this legal conclusion" regarding the meaning of the policy language "is equivalent to the effect of [a] preliminary injunction."

Third, policyholders must carefully negotiate policy terms at renewal time in order to avoid a costly "two-front war" with their insurers when faced with a claim later on. If the insurance policy does not expressly provide that its personal conduct exclusions apply only after there has been a "final adjudication," the policyholder could end up having to defend itself not only against class action plaintiffs and government prosecutors but also against its own insurers, who may try to escape their coverage obligations by initiating parallel litigation designed to prove that the insureds are "guilty as charged"—effectively ganging up with the third-party claimants against their own insured.

Finally, it is conceivable that the insured can escape this result simply by avoiding inconsistent policy language. In deciding what the Stanford Financial policy exclusion meant, the Fifth Circuit noted that "in fact" could not possibly be synonymous with "final adjudication" because another exclusion within the same policy referred to a "final adjudication" and different terms within the same insurance policy must have different meanings. If the insured had simply demanded that the policy consistently use one term or the other, it might have obtained a better result.

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