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ALERT

# Declaratory Judgment Action Dismissed Due to Insureds' Failure to Comply with ADR Clause

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Applying California law, the United States District Court for the Central District of California has dismissed a declaratory judgment action on the grounds that the insureds failed to comply with policy conditions requiring the insureds to pursue alternative dispute resolution prior to filing a judicial proceeding. *Previti v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA.*, 2012 WL 3257877 (C.D. Cal. Aug. 7, 2012).

Defendants in 25 separate bankruptcy actions sought coverage under three consecutive directors and officers liability policies. The insurer acknowledged potential coverage for the bankruptcy actions under the first policy, but denied coverage under the second and third policies, prompting the defendants to file a declaratory judgment action seeking a determination with respect to coverage. The insurer filed a motion to dismiss the action on the grounds that the defendants had failed to satisfy the conditions precedent to suit in the policies. Those provisions stated that, "[e]xcept as provided in Clause 17 of the policy, no action shall lie against the Insurer unless, as a condition precedent thereto, . . . the amount of the Insureds' obligation to pay shall have been finally determined . . . by judgment against the Insureds after actual trial[.]" Clause 17, in turn, provided that "[t]he Insured shall have the option, in its sole discretion, to submit all disputes or differences which may arise under or in connection with the policy" to the alternative dispute resolution ("ADR") set forth therein, and that no "judicial proceeding shall be commenced until . . . at least 120 days shall have elapsed from the date . . . of the termination of the mediation."

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The court granted the insurer's motion to dismiss. As an initial matter, the court rejected the defendants' argument that the insurer had waived its rights under the policy conditions due to the insurer's alleged breach of contract, noting that arbitration provisions that are not repudiated are meant to survive such claims. Turning to the defendants' main argument, the court agreed that "no action" clauses that operate to completely bar declaratory judgment actions are unenforceable, but held, relying on precedent within the Ninth Circuit, that the policy conditions did not completely bar suit, but rather controlled the timing of suits brought by insureds prior to a final determination of their obligations. The court also rejected the defendants' argument that ADR was not required because the policies gave insureds the "sole discretion" to pursue ADR in the first instance, holding that, while true, insureds nonetheless were required to engage in ADR if they wished to institute judicial proceedings against the insurer prior to a final determination in the underlying action.

The opinion is available here.