

# Featured Article

## Navigating the Cyber-Insurance Marketplace. Part 4 of 4 in a Series

*Contributed by:*

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Technological change is occurring at a dramatic pace. As companies increasingly rely on technology to sustain their business, the cyber-liabilities that companies face change accordingly. The drafters of cyber-policies are thus faced with a moving target. Over the years, the insurance industry has developed over two dozen cyber-policies – each with very different terms. The result is a variegated but imperfect market. Some policies are risk-averse and written narrowly so that they provide little coverage, while others are written very broadly and may result in coverage disputes.

It is instructive to compare the new cyber-policies with employment practices liability insurance (EPLI). When the insurance industry developed EPLI policies in the late-1980s, the world of employment liability was already well-defined. All of the insurance companies that chose to enter this field developed policies that provided similar basic coverage, with the differences in the nuances. These policies largely met the expectations of companies in need of protection, and little coverage litigation ensued.

Insurance companies are often accused of having a herd mentality, so that they tend to offer the same basic policies. The cyber-insurance market is different. It is a complex marketplace with radically different products available. Since cyber-insurance is still in its infancy, it remains unclear whether cyber-policies follow the path of EPLI, or will result in a new wave of coverage litigation.

### *Understanding the Options for Cyber-Coverage*

To obtain the appropriate protection, a company may need to rely on both an insurance professional and an intellectual property consultant before purchasing coverage. The term 'cyber-insurance' is a catch-all that sweeps in totally different categories of risk. On the liability side, these include:

- all IP infringement risks, including trade dress, trademark, copyright, and even patent;
- privacy liability, a vast new and quickly expanding field;
- slander, libel, defamation and related torts; and
- liability for damage to another's computers and data.

The first party exposures involve a company's own data and computers, electronic theft and cyber-extortion. Policies exist that cover only one of these exposures or multiple exposures, and insurers will customize policies to meet an individual company's needs.

The CNA *Net Protect* insurance policy is an example of a broad policy that provides coverage against multiple cyber risks. The policy includes four liability coverages and seven first-party property coverages. The liability coverages are (1) content injury liability (which includes defamation related injuries and intellectual property infringement claims, except patent and trade secret); (2) privacy liability, which includes coverage for both claims by private parties and also by the government; (3) professional services liability; and (4) network security liability, which includes coverage for denial of access claims, claims of damage to a third party's network, and claims involving data. The policy has 36 exclusions and 78 definitions, many of which have multiple subparts.

At the other end of the spectrum, Samian's *IPGuard* policy is an excellent example of an innovative, narrowly focused policy. This policy only provides coverage for the insured's defense costs against any allegation that its "Declared Product" or "Declared Intellectual Property" infringes on the intellectual property rights of a third party. 'Declared' means specifically submitted to and approved by the insurer. The policy provides coverage against infringement claims arising from the actual or prospective manufacture, sale, licensing or distribution of a "Declared Product", and the licensing of an Intellectual Property Right. The policy also provides coverage for the prosecution of counter-claims. A wide variety of such narrow policies exist.

### *Can the Insurers Defeat Ambiguity?*

In cases involving advertising injury coverage under a commercial general liability policy, the insurers frequently lost because of their failure to define terms. As a result, the new cyber-policies try to control the insurers' exposure through numerous definitions and exclusions. However, even defined terms cannot always avoid ambiguity or, from the insurers' viewpoint, overreaching by insureds. For example, In *i-Frontier Inc. v. Gulf Underwriters Insurance Company*, No. 04-5797 (E.D.Pa. 2005), an employee of MBC, downloaded MBC's manual on his last day of work, and used it at his new employer, i-Frontier. MBC sued the employee and i-Frontier. i-Frontier had an insurance policy that provided coverage for:

- D. infringement of copyright, plagiarism or misappropriation of ideas under implied contract;
- E. misuse of intellectual property right in Content, but only when alleged in conjunction with the types of Claims named in [C. and] D. above;
- I. errors, omissions, and negligent acts; committed by the Insured during the Policy Period in performing Cyberspace Activities as stated in Item 6. of the Declarations, including obtaining, processing, uttering, or disseminating Content in or for the Cyberspace Activities, regardless of when Claim is made or suit is brought.

*i-Frontier* at 2-3.

'Cyberspace Activities' was defined as "creation of internet advertising content for others." *i-Frontier* at 3. i-Frontier sought coverage, asserting that the MBC claim alleged Cyberspace Activities. The insurer replied that the employee did not create internet advertising content; rather, it wrongfully accessed MBC's manual. The court found against the insured on other grounds, but this case demonstrates that even carefully defining terms will not necessarily prevent coverage litigation. See also *Walt Disney Company v. American Casualty Company*, 65 Fed. Appx. 147, 149 (9th Cir. 2003) (finding the terms "utterance or dissemination" and "matter" ambiguous, and ordering insurer to defend insured against claim for theme park idea infringement).

### *Key Provisions to Look Out For*

#### *What is a Claim?*

The cyber-policies usually provide definitions for the key term 'claim,' which can create a trap for insureds. 'Claim' is the key trigger term; once the insured receives a 'claim', it must provide notice to its insurer. Because cyber-claims can arise in a variety of contexts, the policies often have broad definitions of 'claim.' One problem with these broad defense triggers is that they can result in late notice that forecloses coverage. Risk managers and general counsel generally are aware of the need to place insurers on notice when they receive a complaint. The less a triggering

document resembles a complaint, the greater the likelihood that no one will think to notice the insurer. Moreover, all cyber-policies are claims-made policies - policies that provide coverage in the year in which the insured receives a claim. In all jurisdictions, the insured forfeits coverage if it provides notice after the end of the policy period. Further, some policies contain provisions that require notice within a shorter period of days.

In *General Insurance Company v. Marvel Enterprises, Inc.*, 2004 NY Slip Op 50129 (N.Y. Sup. Ct. 2004), the policy defined 'claim' as "[A] demand or suit for money tendered to the insured for loss or injunctive relief." While the insured ultimately won the notice issue in this case, it is nonetheless instructive. Marvel became involved in a dispute with Fox over the licensing of the X-Men, and Fox wrote to Marvel:

Fox hereby demands that any further development, production and distribution of "MUTANT X" cease immediately, and Fox will take all appropriate action to enforce its rights, and will seek such remedies as may be necessary to protect itself against such a flagrant and willful breach of our agreement . . .

At the end of the letter, Fox additionally requested that:

In order to prepare for the contingency of litigation Marvel retain all documents, including e-mails, related to this project and notify Tribune Entertainment, Fireworks and any other entities involved with the production or distribution of "MUTANT X" to do the same.

On the advice of its broker, Marvel did not provide notice of this letter to its insurer. In the coverage litigation that ensued, the Special Master found that the letter sought injunctive relief and was a 'claim,' and that late notice foreclosed coverage. The trial judge reversed, on the highly technical ground that a letter by its very nature could not 'seek' injunctive relief; rather, only a complaint asking a court for that relief could be said to 'seek' injunctive relief. The insured narrowly escaped a bullet. The best advice for any insured is to give notice broadly and early.

Notice provisions must be a major consideration when purchasing cyber-policies. In this regard, one key provision that can usually be manuscripted controls who must provide notice. In any organization, a claim may first be received by someone who is unskilled in insurance and is not aware of the notice ramifications. This increases the risk of late notice. Thus, many companies have provisions stating that the insured does not need to provide notice until specified individuals, such as the general counsel and risk manager, receive the claim.

#### *Choice of Law/Forum*

Choice of law and choice of forum provisions are also prevalent in these new policies and must be carefully analyzed. The construction of insurance policies differs dramatically from one state to the other, with New York usually considered a 'bad' jurisdiction for policyholders. Many new policies contain New York choice of law provisions, and require the insured to submit to ADR before litigation. Further, policies written by insurance companies headquartered outside the United States can require that disputes be arbitrated in, for example, England or Bermuda, pursuant to the laws of that jurisdiction. The purchaser of insurance products must weigh the utility of a policy with such a provision against a policy that permits the insured to sue in its own jurisdiction.

#### *Control of Defense and Settlement*

In the Samian policy discussed above, the relationship between the insurer and insured in controlling the litigation and settlement has a dominant role. The collision of interests between

insurer and insured on this issue has produced frequent disputes under general liability and D&O policies. Policyholders must review the new cyber-policies to make sure that they are not ceding too much authority to the insurer on issues that can go to the heart of the way that the company does business. The insured should negotiate to make sure that it can use its attorneys of choice in claims that come under the purview of the insurance policy.

#### *Definition of Covered Loss*

Certain risks covered by cyber-policies may have unique remedies. For example, privacy violations can result in a duty to notify affected individuals and to provide credit monitoring. The policyholder must make certain that the 'Loss' covered by the policy is co-extensive with the types of relief that the insured may need to provide. Policyholders benefit here from broadly and carefully defined terms. While undefined terms are construed in a manner favorable to the insured in most jurisdictions, lack of definition can also produce litigation.

#### *Conclusion*

All told, companies are well advised to treat the purchase of a "cyber-policy" with the sort of caution that is warranted for such a nuanced insurance product. Given that insurers are seeing a definite up-tick in claims activity, more aggressive claims handling will naturally follow. In other words, doing more work on the front-end negotiation process will ensure that the coverage intended is actually set forth in the policy.

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