

Availability of Insurance to Cover the Cost of Privacy and Data Breach Litigation

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The authors examine the types of insurance available to cover claims related to privacy and data breach litigation. Fortunately, many companies already have insurance that could cover these costs.

Gone are the days of protecting consumers' and employees' personal information in the back of a securely locked safe. Today, much of that information is maintained electronically, and companies strive to keep it secure from hackers and others seeking to misuse it. The repercussions of failing to do so can be significant.

With the proliferation of regulatory requirements, as well as an increased focus on data security issues in the public generally, companies have seen a spike in privacy-related litigation in recent years. Because these suits plunge companies into often unfamiliar waters, companies frequently overlook insurance that could cover the costs of the investigation of the claims, the ensuing litigation, and, ultimately, any settlement or judgment. Fortunately, many companies already have insurance that could cover these costs.

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PRIVACY COVERAGE UNDER COMMERCIAL GENERAL LIABILITY POLICIES

When faced with privacy suits, many corporate defendants overlook their commercial general liability (“CGL”) policies under the assumption that a more privacy-specific or “cyber” policy is the only policy that could provide coverage. However, a CGL policy is the first place a company should look to find coverage for privacy or data-security related costs. Courts consistently have held that coverage may be available, notwithstanding that insurers routinely deny these claims to avoid their obligations under these types of policies.

Most CGL policies include a “Personal and Advertising Injury” (“PI”) clause. The standard-form PI clause developed by the Insurance Services Office (“ISO”) requires the insurer to defend and indemnify the policyholder for injuries arising out of an “oral or written publication, in any manner, of material that violates a person’s right of privacy.” In most cases alleging privacy violations, coverage is triggered if the claim satisfies a two-prong test: (1) an alleged violation of a person’s privacy and (2) some form of publication. Applying this standard, courts have found coverage for claims involving the use, collection, or distribution of personal information.¹

For instance, courts have held that claims under the Federal Credit Reporting Act (“FCRA”)², which regulates the use of consumers’ personal information, are covered by the PI clause in CGL policies. In *Zurich American Insurance Co. v. Fieldstone Mortgage Co.*, the court held that the insurer had a duty to defend Fieldstone under the PI clause in Fieldstone’s CGL policies.³ The underlying claim alleged that Fieldstone had violated FCRA by improperly accessing the plaintiffs’ credit information to solicit their business for sub-prime mortgages. Finding coverage under Fieldstone’s CGL policy, the court held, applying the two-prong test, that “there is no question that the information that was accessed was secret,” and furthermore, “one of the purposes of [FCRA] is to ensure that consumer credit reports are kept private.”⁴ Additionally, the court held, the mere use of this information in a written solicitation constituted a “publication,” and thus fell within the scope of the PI clause of

Fieldstone's CGL policies.⁵

Similarly, in *Netscape Communications Corp. v. Federal Insurance Co.*, the court held that a company's collection and distribution of its consumers' personal data, which triggered suit for breach of contract, breach of the covenant of good faith and fair dealing, and violations of California Business and Professions Code Section 17200, fell under the PI provision in the company's CGL policy.⁶ Although the *Netscape* court ultimately held that the insurer did not have a duty to defend the company, the analysis applied by the court is instructive as to how courts would interpret similar PI provisions. The court assumed that Netscape's Smart Download program, which gathered and distributed personal information, was an invasion of privacy, thus satisfying the first part of the two-prong test. The court also found that the distribution of personal information to AOL and Netscape employees through the Smart Download program was a publication sufficient to trigger the PI provision of Netscape's CGL policy.⁷ However, the court held that the policy's Online Activity Exclusion applied, thereby precluding coverage.⁸

Unlike privacy litigation involving the collection, use, and distribution of personal information, courts are split on whether seclusion privacy cases, usually under the Telephone Consumer Protection Act, ("TCPA"),⁹ trigger the PI clause. TCPA claims arise when companies send out unsolicited blast fax advertisements, which involves the consumer's right to be left alone (or "seclusion privacy"), but it does not involve the privacy of the consumer's personal information (or "secrecy privacy"). Courts differ on whether an invasion of seclusion privacy is the type of injury that the PI clause is designed to protect.

For example, in *Resource Bankshares Corp. v. St. Paul Mercury Insurance Co.*, the court distinguished seclusion privacy from secrecy privacy.¹⁰ The court held that the "the advertising-injury offense part of the policies is exclusively concerned with those types of privacy...like secrecy," not seclusion privacy.¹¹ "Accordingly the privacy prong of the advertising injury provision cannot be construed to cover a violation of the TCPA."¹² Some courts do not agree with the privacy distinction in *Bankshares'* analysis. For instance, in *Valley Forge Insurance Co. v. Swiderski Electronics, Inc.*,¹³ the court held that "privacy is privacy. In

other words, because transmitting an unwanted facsimile constitutes an intrusion on seclusion, it violates one's right of privacy."¹⁴

As discussed, CGL policies can provide coverage for privacy related claims. For claims involving statutes like FCRA, which involve the use, collection, and distribution of personal information, the claims are commonly considered invasions of privacy, and therefore the PI clause in a CGL policy is a good fit. However, litigation involving TCPA and other similar statutes may be covered depending on the court's interpretation of and/or distinction between secrecy and seclusion privacy. In any event, these sorts of privacy claims should also be reviewed against a companies' CGL policy for potential coverage.

POTENTIAL LIMITATIONS ON PRIVACY COVERAGE

When evaluating the availability of coverage, policyholders must also consider policy exclusions. As with any claim, all typical policy exclusions apply, such as intentional acts¹⁵ or prior acts exclusions.¹⁶ But in the privacy context, in addition to the usual suspects, the upsurge in privacy litigation has led insurers to develop new exclusions.

Intentional acts exclusions are common in CGL policies, and often cited by insurers to bar coverage for privacy claims. Privacy claims brought under criminal statutes may be subject to exclusions that bar coverage for the knowing or willful violation of a criminal act. For example, in *National Fire Insurance Co. v. NWM-Oklahoma, LLC*, despite an affirmative grant of coverage for claims based on the Wiretap Act, the court found that claims based on the Wiretap Act and other similar statutes fall within the applicable exclusion and therefore barred coverage.¹⁷

On the other hand, an intended acts exclusion may not bar coverage for claims brought under FCRA and TCPA. Insurers have a duty to defend claims if any theory in the underlying complaint could potentially be covered by the policy, thus if an exclusion bars coverage for one claim, but not the other, coverage is still available. For example, some TCPA and FCRA claims require intent, others do not. Therefore, in FCRA and TCPA cases that allege both intentional and nonintentional violations, and where coverage is otherwise available, the intended acts exclusion does not bar

coverage for any claims.¹⁸

Insurers also have developed exclusions for claims based on specific statutes or types of statutory violations. For example, one exclusion, drafted by the ISO in 2004, excludes claims arising out of any action or omission that violates the TCPA, the CAN-SPAM Act of 2003, or similar statute or ordinance “that prohibits or limits the sending, transmitting, communicating or distribution of material or information.” Another exclusion, used in Hartford CGL policies, excludes coverage for personal and advertising injuries “arising out of the violation of a person’s right of privacy created by any state or federal act.” Arguably, such exclusions could deprive policyholders of coverage for TCPA or FCRA claims because TCPA and FCRA are statutes that generally prohibit some type of distribution of material or information.

Policyholders should also be on the lookout for industry-specific exclusions. For example, Netscape’s coverage would have been available but for an On-line Exclusion.¹⁹ Its CGL policy excluded any personal or advertising injury as a result of an Online Activity, including “providing e-mail services,...supplying 3rd party content and providing internet access to 3rd parties.” Internet companies are vulnerable to this exclusion because if their alleged invasions of privacy were committed in the process of providing online services, the resulting injury may be excluded from coverage.

Policyholders should negotiate with insurers over these types of exclusions and consult with coverage counsel to evaluate the scope of the exclusions’ potential impact on the company’s privacy coverage.

ALTERNATIVE PRIVACY COVERAGE

A company’s CGL coverage may provide adequate protection against potential privacy claims. However, if the company is concerned that their CGL policies may be inadequate due to the nature of their potential exposure or the likelihood that policy exclusions would apply, the company may find it necessary to purchase privacy specific coverage. Privacy coverage is offered as an endorsement or amendment to an already existing CGL or Error and Omissions policy, or as a standalone policy. But again, the poli-

cyholder must pay attention to the language of the policy or the endorsement because it too may not provide coverage for certain types of litigation.

For instance, companies may be concerned with Travelers' Web Extend Endorsement. The Web Extend Endorsement replaced the PI clause in the standard CGL policy with a revised version covering "[o]ral, written or electronic publication of material that appropriates a person's likeness, unreasonably places a person in false light or gives unreasonable publicity to a person's private life."²⁰ Although this endorsement should provide broad coverage for a range of privacy litigation, at least one court has held that the endorsement would not provide coverage for a policyholder's alleged Fair and Accurate Credit Transactions Act ("FACTA")²¹ violation.²² The court determined that the alleged FACTA violation did not violate a privacy right as it was defined in the revised PI clause.²³

On a more positive note, some privacy coverage is so broad that it would cover even regulatory claims. A Privacy Protection Insurance Policy that was drafted specifically to protect the policyholder against a wide range of privacy related offenses provides coverage for claims arising from:

- a "violation or infringement of any right to privacy, consumer data protection law, or other legal protection for personal information,"
- a "breach of duty to maintain the security of confidentiality of sensitive personal information under any federal, state or local statute, rule or regulation, or under any contract, including but not limited to your" privacy statement or policy,"
- "any civil regulatory action brought against you by a regulator based on the same allegations as a claim under [the above actions], including but not limited to for breach of any regulation promulgated by the FTC."

This policy excludes general regulatory claims, but the policy affirmatively states that it does not exclude certain regulatory privacy claims, such as the ones outlined above. Therefore, this type of policy would probably provide coverage for alleged FCRA, TCPA, and even FACTA violations.

CONCLUSION

Many companies are vulnerable to privacy or data breach claims. Companies that may be sued or investigated for alleged privacy violations should first turn to their CGL policy for coverage. The policyholder should review the policy closely for potential coverage, particularly under the PI clause. But, even if coverage is affirmatively available under the PI clause, policyholders should also be wary of new privacy and industry specific exclusions developed by insurers in response to the increase in privacy litigation. And for these companies, that are particularly vulnerable to privacy claims, CGL coverage may not offer enough protection and it may be necessary to acquire privacy specific insurance to protect against potential losses.

NOTES

¹ See *American Family Mut. Ins. Co. v. C.M.A. Mortgage, Inc., et al.*, No. 1:06-cv-1044-SEB-JMS, 2008 U.S. Dist. LEXIS 30233, at *15-16 (S.D. Ind. March 31, 2008) (“A reasonable person who reads the advertising injury provisions of these policies would conclude that coverage exists for a claim arising out of the mailing of a solicitation letter that was triggered by a violation of the privacy protection rights established in FCRA.”); *Pietras v. Sentry Ins. Co., et al.*, No. 06 C 3576, 2007 U.S. Dist. LEXIS 16015, at *11 (N.D. Ill. March 6, 2007) (“the Court holds that the FCRA allegations in the underlying complaint fall within the ‘advertising injury’ provision in the Sentry policy”).

² 15 U.S.C. § 1681.

³ No. CCB-06-2055, 2007 U.S. Dist. LEXIS 81570 (D. Md. Oct. 26, 2007).

⁴ *Fieldstone*, 2007 U.S. Dist. LEXIS 81570, at *15-16.

⁵ *Id.* at *13-15.

⁶ *Netscape Commc’ns Corp., et al. v. Fed. Ins. Co.*, No. 06-cv-00198-JW, 2007 U.S. Dist. LEXIS 78400 (N.D. Cal. Oct. 10, 2007).

⁷ *Id.* at *17.

⁸ *Id.* at *18.

⁹ 47 U.S.C. § 227 *et seq.*

¹⁰ 407 F.3d 631 (4th Cir. 2005).

¹¹ *Id.* at 641.

¹² *Id.* at 642.

¹³ 834 N.E.2d 562 (Ill. App. Ct. 2005).

¹⁴ *Id.* at 574.

¹⁵ *See, e.g., Netscape*, 2007 U.S. Dist. LEXIS 78400, at *7, 17-18.

¹⁶ *See, e.g., Fieldstone*, 2007 U.S. Dist. LEXIS 81570, at *18-20 (“an exclusion for personal and advertising injury ‘arising out of oral, written, televised, videotaped, or electronic publication of material whose first publication took place before the beginning of the policy period’”).

¹⁷ *See, e.g., Nat’l Fire Ins. Co. of Harford v. NWM-Oklahoma, LLC, Inc.*, 546 F. Supp. 2d 138, 1248 (W.D. Okla. Mar. 12, 2008). (The policy excluded coverage for a injury “arising out of the willful violation of a penal statute or ordinance committed by or with the consent of the insured.”)

¹⁸ *See, e.g., Valley Forge*, 834 N.E.2d at 575-76 (where the policy excluded coverage for an injury that is “caused by or at the direction of the insured with the knowledge that the act would” the court found that because “Insurers have a duty to defend if any theory in the underlying complaint could potentially be covered the exclusion does not bar potential coverage in this case...claims under the [TCPA] do not rest on intent to cause harm and may be made on the basis of mere negligence”).

¹⁹ *Netscape*, 2007 U.S. Dist. LEXIS 78400 at *20. (The allegations against the policyholder were sufficient to trigger the insurer’s duty to defend, but “the scope of the online activity exclusion [was] sufficiently broad to encompass Plaintiffs’ activities with regard to Netscape’s SmartDownload product as alleged in the Underlying Actions.”)

²⁰ *Whole Enchilada, Inc. v. Travelers Prop. Cas. Co. of Am.*, 581 F. Supp. 2d 677 (W.D. Penn. 2008).

²¹ 15 U.S.C. § 1681.

²² *Whole Enchilada*, 581 F. Supp. 2d 677.

²³ *Id.*