

# E-commerce

## *insurance developments in the US*



By Michael A. Rossi

*This article is a continuation of Michael Rossi's thorough discussion of issues arising from the application of insurance to the new risks posed by e-commerce activities. The first article, published in the August edition of Corporate Risk, introduced the area of insurance and e-commerce, and dealt with the area of first-party risks. In the concluding article, the author addresses third-party risks in e-commerce, and offers some direction for considering how best to deal with your company's e-commerce exposures.*

### **Third-party liability e-commerce risks**

Many of the articles written on the risks of e-commerce activities provide a litany of the different third-party liability risk exposures for e-commerce activity. Rather than address the issues in that way, the author will discuss the risk issues in the context of the potential gaps in traditional insurance programs for many corporate insureds. The discussion of liability risks set forth below



is not, therefore, intended to be comprehensive, but rather illustrative.

### Program comprehensiveness

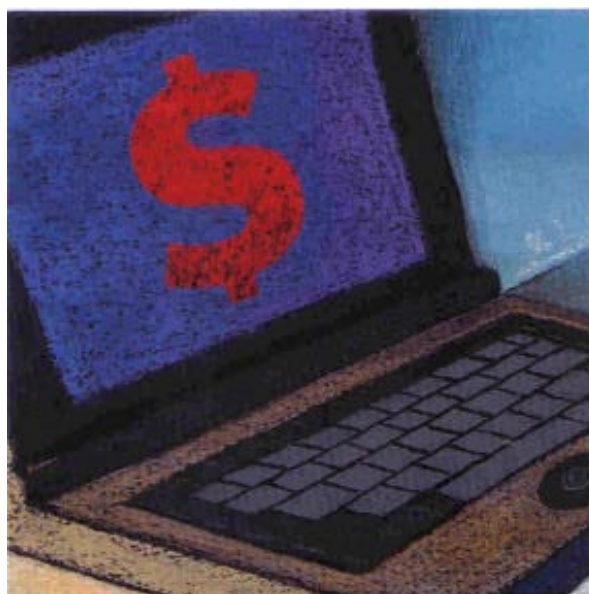
The first point that should be made (and this is the focus of much of the debate among risk managers, underwriters and brokers in this area) is that not all corporate insureds have all of the liability-coverages in their insurance program needed to respond to liability risks associated with e-commerce activities. This is markedly different from first-party risks, where most corporate insureds already have the necessary coverages in their program (even if some of them need to be enhanced a bit as discussed above). At a minimum, insureds should have commercial general liability, professional liability and media errors and omissions liability insurance, or their equivalent, in their liability insurance program to respond to e-commerce liability risks.

However, many corporate insureds have only standard commercial general liability, umbrella liability and excess liability coverage in their programs. As will be explained below, these corporate insureds will have the most issues to address if they want their liability risks for e-commerce activities more fully covered.

However, some corporate insureds do have all three of these coverages, either in stand-alone policies or rolled into one manuscripted liability policy. The risk managers of such organisations are the most vociferous in their opinion that they have no need for any of the new e-commerce insurance. They might be right, but the point for them to recognise is that their insurance program profile is in the minority among US Fortune 1000 companies, and the companies with only CGL, umbrella and excess liability insurance are the ones who are in need of additional insurance coverages built into their programs.

### Why is CGL coverage not sufficient for e-commerce risks?

Standard CGL coverage is not sufficient for e-commerce risks for a variety of reasons. True, some e-commerce risks can be covered by traditional CGL wording, just like a host of other types of liability claims, and the fact that such claims involve e-commerce activities



will not make any difference to the coverage. However, there are several risks associated only with e-commerce activities that likely will prove problematic for coverage under traditional CGL wording. The risks set forth below are illustrative of the problems -note that this discussion is not intended to be exhaustive.

### Invasion of privacy

E-commerce activities pose a risk of liability for invasion, infringement or interference with rights of privacy that could be problematic for traditional CGL insurance wording. That is because traditional wording provides coverage for invasion of rights of privacy caused by the publication or utterance of information that violates a person's right of privacy. But the risk posed by e-commerce activity is not so limited — the big privacy risk is risk of liability for gathering information about someone who visit a

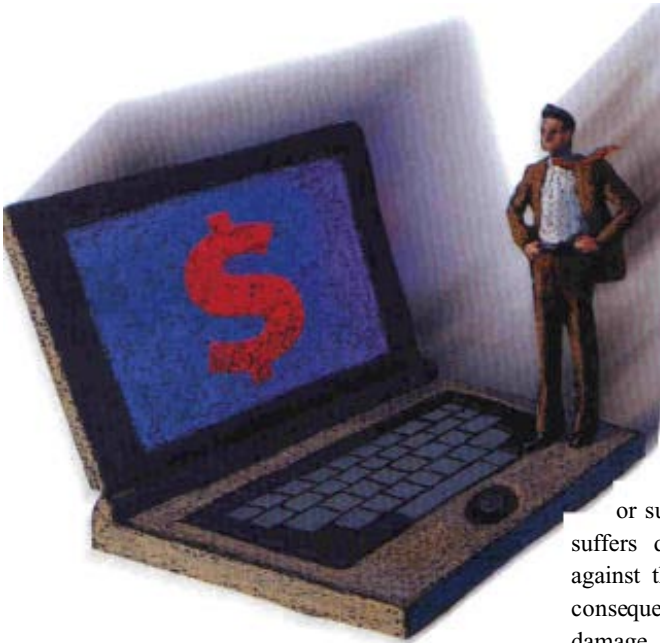
website without that person knowing. A CGL insurer faced with the insured's tender of such a claim likely will deny coverage on the basis that the insured's liability has nothing to do with disseminating information, but rather has only to do with the gathering of information. This is a potentially large gap in traditional CGL wording for risks posed by e-commerce activities.

### Infringement of intellectual property rights

E-commerce activities pose a risk of liability for infringement of intellectual property rights, such as infringement of patent, trademark, copyright, right of publicity and the like. Some of these risks can and should be covered by standard CGL wording. However, some are not, for any of the following reasons.

First, the claimed injury must be causally connected to the insured's advertising activities. That is because much of the coverage for such risks will be provided by the 'advertising injury' coverage in a CGL policy. But that coverage only responds if the injury arises out of the insured's advertising activities. One of the problems associated with e-commerce activities is that an insured could be faced with liability because a third party's advertisement on its website (eg, a banner ad) is the source of infringing material. CGL insurers are already denying coverage for such claims, on the basis that they do not arise out of the insured's advertising activities. There also is the possibility that courts might not construe the insured's internet and website activity as advertising activity. In that event, none of the intellectual property claims based on such activity can be covered as advertising injury under a CGL policy.

Second, even if the claimed injury does arise out of the insured's advertising activities, the injury still must fall within one of the specified 'offences' set forth in the standard definition of



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advertising injury in a CGL policy. Some of the intellectual property risks associated with e-commerce activities likely fall outside of such definitions. For example, the risk of infringement of the right of publicity would be unlikely to fall within the scope of the definitions.

Third, many CGL insurers are issuing their policies with very narrow advertising injury coverage. Such narrow provisions limit coverage to infringement of trademarked or copyrighted advertising materials, and specify that the infringement must be caused by the insured's paid advertisement in a newspaper, magazine, television ad or other medium. Such language severely restricts the extent of coverage for intellectual property risks posed by e-commerce activities.

### Third party damage

E-commerce activities pose a risk of liability for damage to another person's computer data, software, programs or computer network. This could occur, for example, by reason of the spread of a computer virus, when a customer or supplier of the insured connects to the insured's computer network or website, and the virus spreads from the insured's system to the customer

or supplier. If that customer or supplier suffers damage, it could present a claim against the insured for that damage, and all consequential losses suffered because of that damage (eg lost profits, repair costs, restoration costs etc). The question raised by such a scenario is whether the claimant is seeking damages because of 'property damage' as that term is defined in standard CGL policies. Standard CGL policies in the US define property damage as "physical injury to tangible property" or "loss of use of tangible property" that has not been physically injured. From 1998 to today, US insurance companies and their lawyers have taken the position that computer data, programs, software, networks etc do not constitute 'tangible property' in CGL policies. US courts have not fully resolved this coverage question (although several courts have found in non-insurance coverage cases that computer data is tangible property). In any event, until this issue is resolved, this issue poses a large potential gap in traditional CGL coverage for e-commerce risks.

### Pure financial loss

What if the insured's computer network or website crashes, or sustains a denial of service attack, or for some other reason is inaccessible by the insured's customers and suppliers? What if, as a result of such inaccessibility, the insured's customers

and/or suppliers sustain a purely financial loss (ie a financial loss not caused by physical injury to tangible property)? How are such claims going to be covered by a standard CGL policy? The answer is that they likely are not. Such claims have been the subject of much litigation in the US. The general consensus among US courts is that the only time that financial losses sustained by third persons can be covered under a CGL policy is if the losses result from or flow from 'property damage' as defined by the particular CGL policy at issue.

As noted above, this discussion is not intended to provide a comprehensive listing of e-commerce third-party liability risks. Rather, it is intended to be illustrative, to show some of the potential gaps in coverage for e-commerce risks if an insured's program uses only standard CGL, umbrella and excess liability insurance.

### New ecommerce policies

The insurance industry has responded to the potential gaps discussed above with a proliferation of new ecommerce insurance products intended to respond to liability risks. The names of these policies are quite fanciful, even if, as will be explained below, the liability insurance coverages provided by them are not really all that novel. For example, AIG is selling the netAdvantage Internet Professional Liability Policy, Chubb is selling the Safety'Net Internet Liability Policy, Zurich is selling the E-Risk Protection Policy, Royal is selling the Computer, Telecommunications and Internet Services Liability Coverage policy, Gulf (through Media/Professional Liability) is selling the CyberLiability Plus Insurance Policy, and Great American (through Tamarack) is selling the Dot.Com Errors and Omissions Liability Insurance Policy. These are just examples: there are a host of other policies available from several different Lloyd's facilities and several other US insurers.

These policies are designed to insure some or all of the risks that may fall into



one of the potential gaps in traditional CGL policies. So, for those companies whose liability insurance program consists of only standard CGL, umbrella and excess liability policies, buying one of these new e-commerce insurance policies is a viable option.

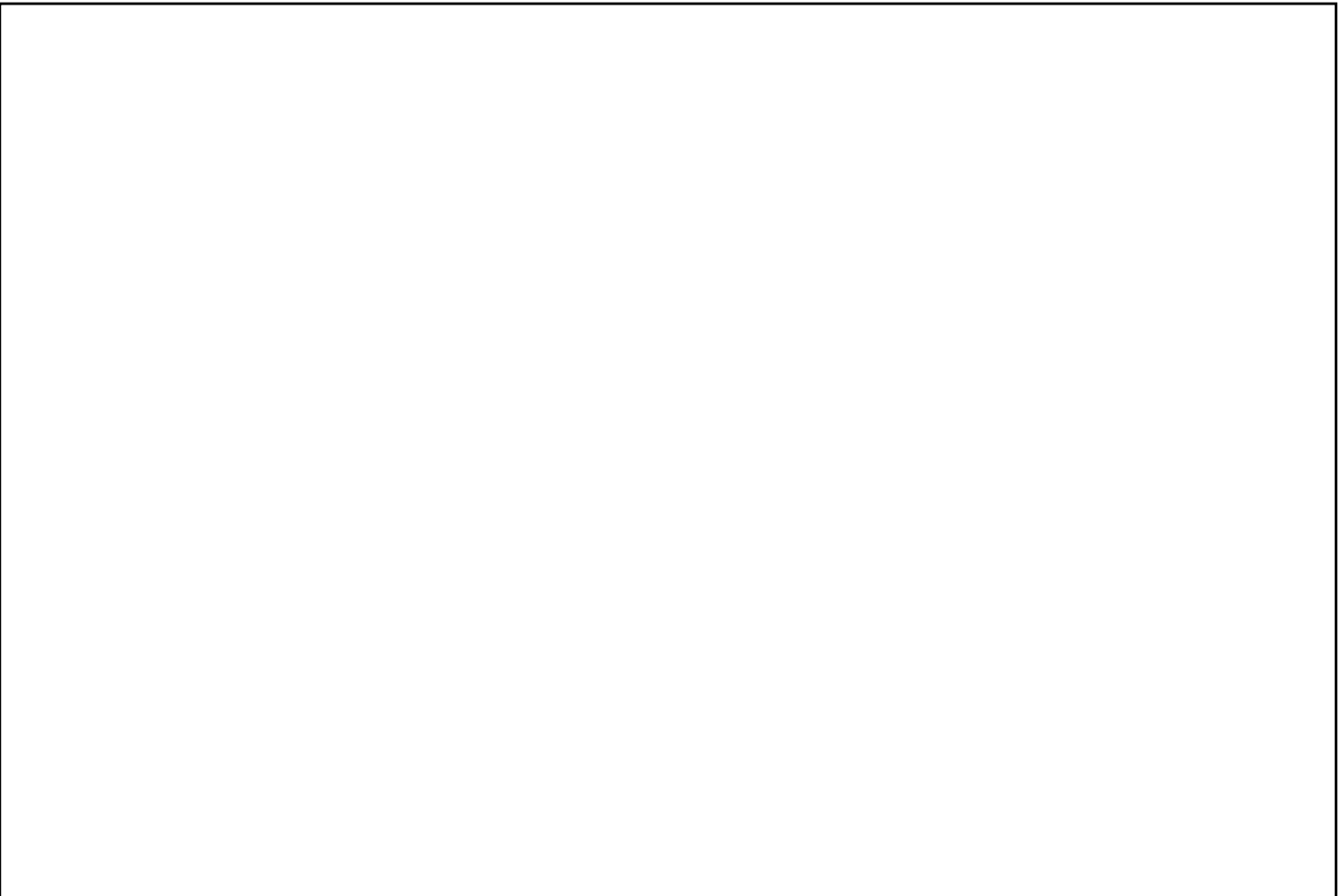
However, looking beyond the labels and buzzwords used in the policies, and focusing on the substance of the coverage being provided, one is almost immediately struck by the following observation. With respect to the liability insurance coverages provided by these policies (some of the policies also provide coverage for firstparty risks), these policies are not much more than combined professional liability and media errors and omissions liability coverages. Indeed, some of the policies are

quite blatantly so: setting forth different insuring agreements, one entitled something like 'Professional Liability Coverage' and the other entitled something like 'Media Errors and Omissions Coverage' or 'Publisher's Errors and Omissions Coverage'.

This should raise three very important considerations for companies attempting to address their e-commerce liability insurance risks when their insurance programs currently consist only of standard CGL, umbrella and excess liability insurance. First, they need to realise that their choices are not limited to foregoing coverage or buying one of these new e-commerce insurance policies. They could insure the risks by adding standard professional liability and media errors and

omissions liability coverage to their programs (as discussed below).

Second, companies need to realise that if they are going to buy one of the new e-commerce insurance policies, they must carefully review the policy forms and endorsements being quoted to them to make sure that the quoted coverage insures all the professional liability and media errors and omissions liability risks that otherwise would be insured by buying standard professional liability and media errors and omissions liability coverage. Some of the policy forms come up short on one or the other coverage, either focusing on the professional liability aspect to the detriment of the media errors and omissions aspect, or leaving one of the coverages out altogether.





Some of the carriers, even though their policy form might contain both coverages, are quoting their policies with endorsement exclusions that delete one of the coverages. These problems are due to the fact that the market for this insurance is young, and that some of the underwriters selling the insurance are not sufficiently experienced: they may only have experience in one area, and therefore are not comfortable offering coverage for both exposures.

Third, regardless of which course of action a company takes, it should try to amend its CGL and/or umbrella policies to address some of the gaps mentioned above for any risks that it actually wants to be covered under those policies. For example, most insureds seem to want the invasion of privacy risk run through the CGL program, and are therefore trying to amend the definitions of 'personal injury' and 'advertising injury' to accommodate the risk. In other words, they are trying to delete the requirement of 'publication or utterance' so that the wording reads something like: "any form of infringement of, interference with or invasion of privacy".

### **Traditional insurance policies**

As with first-party e-commerce risks, the question must be asked: does an insured have to buy one of these new e-commerce insurance policies to insure its e-commerce liability risks? Whereas the answer with respect to first-party e-commerce risks is "in theory, no" the answer with respect to liability e-commerce risks is "in practice, no". As noted above, in many ways the new e-commerce liability insurance policies are nothing more than a policy that combines two traditional coverages — professional liability and media errors and omissions liability.

Thus, those insureds who use only standard CGL, umbrella and excess liability insurance should be able to simply purchase traditional professional liability and media errors and omissions liability coverage, with perhaps some minor adjustments to confirm coverage for e-commerce exposures, at either a primary level or built into the umbrella policy. For those insureds buying the coverage on a primary level, the questions that will remain for such insureds will include the following. Should such coverages be bought separately or in a combined policy? Can the coverage be scheduled as underlying insurance on the umbrella policy, or must the insured maintain a separate tower of insurance for the coverage? Regardless of how such coverage is built into the program, an insured still should ask itself whether there are any adjustments that should be made to the CGL policy to better insure e-commerce risks through that coverage, as explained above.

Those insureds who already have professional liability and media errors and omissions coverage in their program (whether with stand-alone policies or manuscripted poli-



cies at a primary or umbrella layer) should be able to review their program to determine what, if any, gaps exist and to close all identified gaps with further amendments to the policies (eg the invasion of privacy coverage in their CGL policies should be reviewed). That is why the risk managers of such companies are so vociferous in their opinion that there is no need for the new e-commerce liability insurance policies. Again, however, such risk managers should realise that the majority of US Fortune 1000 companies do not have all three of these coverages in their programs and that, therefore, such companies could use such new e-commerce policies, or the types of coverages provided by them (ie professional liability and media errors and omissions liability).

With respect to liability insurance issues, all of the foregoing scenarios are being played out in the US market (as well as the UK market). Some insureds already have the basic coverages needed in their liability insurance programs to respond to e-commerce risks, and are merely reviewing their programs to confirm intents with their insurers and/or amending some of the policies where necessary. Some insureds have only standard CGL, umbrella and excess liability policies in their programs, and are either adding standard Professional Liability and Media Errors and Omissions Liability coverage into their programs, or are buying one of the new e-commerce insurance policies.

### Concluding thoughts

In the final analysis, Australian risk managers should not be led astray by the hype being created by certain insurers and insurance brokers with respect to the 'need' for the new e-commerce insurance policies. Nor should they ignore the issue either, by relying on those risk managers who say that there is no need to address e-commerce insurance issues with new policies or amended traditional policies. Rather, Australian risk managers should conduct their own analysis and decide for themselves what, if anything, needs to be done to their insurance programs. The process for any risk manager must start with an understanding of the issues and then a review of their company's particular insurance program to identify potential gaps in coverage for e-commerce risks. Only after such a review is completed can the risk manager know whether any changes need to be made to the insurance program to better respond to e-commerce risks. That is the process currently being used by more and more US and UK risk managers. Hopefully, this article provides some useful information to help Australian risk managers with the same process. ■

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