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*Expert Analysis*

# The State of Coverage Disputes Concerning Advertising And Privacy Claims

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False-advertising and data breach lawsuits against retailers and marketers seem to be on the rise and present real legal risks to companies that sell and advertise consumer products. Such companies should carefully evaluate their existing insurance and determine whether it sufficiently covers them for their particular advertising-related and data breach risks.

Coverage for data breach and false-advertising claims generally can be found under the "personal and advertising injury" coverage section in commercial general liability policies. Also, given the recent increase in the number of data breaches and ensuing class actions, additional coverage for such events is available under relatively new cyber insurance policies.

The coverage and language for these policies vary widely and, as such, companies should not assume that all such policies are the same. Further, given the relative infancy of these policies, there is little reported case law on them from which to glean the extent of their coverage and exclusions.

Several recent insurance coverage lawsuits highlight issues of which companies and risk managers must be aware in purchasing insurance and making coverage claims.

## MICHAELS STORES INC.

The Michaels craft store chain was sued in several putative class actions alleging that it failed to safeguard PIN pad terminals used by its customers when making purchases, thereby permitting criminals to access customers' private financial information and then make unauthorized purchases and withdrawals. Primary CGL insurer Arch Insurance Co. initially agreed to participate in Michaels' defense but then sued the retailer to disclaim coverage. Excess insurer XL Insurance America denied coverage and sued separately.[1]

The fairly typical terms of the Arch "personal and advertising injury" coverage provide for coverage in response to an "injury ... arising out of ... [o]ral or written publication, in any manner, of material that violates a person's right of privacy" that is "caused by an offense [during the policy period] arising out of [Michaels'] business."

In support of its no-coverage position, Arch argued, among other things, that the underlying alleged injuries did not stem from oral or written publication of material that violated privacy rights. Michaels responded that the underlying lawsuits alleged that its failure to safeguard PIN pad terminals permitted the "publication" by electronic means of consumers' private financial information to criminals, thereby "violat[ing] [each claimant's] right of privacy."

In other words, Michaels allegedly published private financial information that violated each consumer's right to privacy. Michaels argued that because the terms "publication" and "right of privacy" are not defined in the policy, they should be given an ordinary and inclusive meaning. Michaels also asserted that its alleged failure to protect data occurred during the purchase process, and thus the claims arose out of its business.

The parties recently reached a confidential settlement, which generally reflects a recognition of risks by both parties.

***The coverage and language for new cyber insurance policies vary widely, and companies should not assume that all such policies are the same.***

## SHAPE UP!

A class of consumers who alleged that deceptive advertising led them to purchase CSA Nutraceuticals' Shape Up! diet and nutritional products sued CSA and related entities.

In seeking coverage, CSA contended that the underlying plaintiffs alleged that they suffered bodily injuries because of the failure of the products to perform their advertised purposes. CSA's primary CGL insurer, Chubb, ultimately denied coverage, and CSA sued.[2]

The trial court ruled in Chubb's favor, finding that the underlying claimants did not allege "bodily injury" but only economic loss from having purchased a product that failed to work as advertised. CSA appealed to the 5th U.S. Circuit Court of Appeals, arguing that the duty to defend is broad and, when "liberally construed as required," the underlying allegations "at least potentially allege 'bodily injury' covered by the Chubb policy."

Chubb recently filed a brief, arguing, among other things, that the consumers' alleged loss was entirely economic and not personal or advertising injury.

## PETARMOR

Federal Insurance Co. recently filed a complaint against Velcera Inc. and FidoPharm in Pennsylvania federal court. Federal Insurance seeks a ruling under a life sciences liability policy that it owes no coverage for consolidated class-action lawsuits alleging deceptive trade practices and fraudulent marketing in connection with Velcera's PetArmor flea and tick repellant.[3]

The life sciences policy, like a standard CGL policy, provides coverage for losses arising from bodily injury or property damage. Federal Insurance initially accepted

the defense and then sued for a no-coverage ruling on the ground that the plaintiffs sought economic damages for buying an unfit product and not damages for bodily injuries.

Velcera probably will argue that it is being sued for bodily injuries it allegedly caused to the plaintiffs' pets. Because the life sciences policy at issue appears to be structured in relevant part like a standard CGL policy, developments in this case could be of interest to companies that sell a broad array of consumer products.

### 5-HOUR ENERGY

Innovation Ventures, doing business as Living Essentials, which makes the 5-Hour Energy drinks, was sued by Hansen Beverage Co. on the basis of allegations that Living Essentials' advertisements falsely disparaged Hansen's competing energy drinks. Innovation Ventures purchased two insurance policies: a CGL policy from Citizens Insurance and a "media special peril — advertiser coverage" policy from National Casualty. Citizens accepted coverage and paid more than $900,000 in fees and expenses. National Casualty declined coverage.

Citizens sued National Casualty for contri-bution, and National Casualty moved to dismiss.[4] A California federal court denied National Casualty's motion, stating it could not rule as a matter of law that the National Casualty policy is excess to the Citizens policy and that, even if the National Casualty policy excludes coverage for false-advertising claims, Hansen also alleged trade libel, which appears to be covered by the National Casualty policy.

***Even before being sued, policy-holders can and should take steps to enhance their coverage positions by being proactive in their analysis of their existing coverage.***

Coverage for one advertising sales channel has generated a significant amount of attention, with varied results. Although some companies that have been sued for allegedly violating the Telephone Consumer Protection Act by sending unsolicited fax advertisements have found favorable rulings in certain courts, others have not fared as well.

Coverage for these claims tends to arise under the personal and advertising provision of a CGL policy, based on the alleged violation of the privacy rights of the fax recipients. In some cases, courts have found coverage appropriate, since the unsolicited faxes caused damage to the recipients.

A Wisconsin appellate panel recently held that West Bend Mutual Insurance Co. had a duty to defend Atlas Heating Sheet & Metal Works for a junk-fax class action.[5] The court found that the personal and advertising liability provision covers damages for injury from oral or written publication, in any manner, of material that violates a person's right to privacy. The panel held that the transmission of the faxes by Atlas constituted "publication of material that infringes the recipients' privacy rights."

Many courts have adopted this same approach and found coverage appropriate.

Other courts, however, have denied coverage under CGL policies for similar claims, particularly in cases in which a company seeks indemnity for settlements. In these cases, courts have found that the TCPA's statutory fine of $500 per violation, the basis for some settlements, is a penalty, not damages, and thus is not covered.

For example, in a recent 2-1 decision by a Missouri appellate panel arising from the settlement of a TCPA class action against Quiznos, the majority observed that the class had sought statutory rather than actual damages (which could have included wasted ink and paper and lost productivity).[6] The majority concluded there was no coverage for such statutory damages, which it considered to be penalties.

Another Missouri court reached the opposite conclusion in a similar TCPA junk-fax case under the products-completed operations coverage purchased by HIAR Holdings LLC from Columbia Casualty Co.[7] The court rejected Columbia's affirmative defense that coverage was barred under a policy exclusion for willful violation of a penal statute, noting that the TCPA is a strict liability statute, not a penal statute (contrary to the court's findings in the Quiznos suit), and that the underlying judgment specifically found that HIAR did not intend to injure the recipients of the faxes.

## CONCLUSION

Whether a company that is sued for deceptive advertising or a data breach ultimately obtains coverage obviously depends on the facts alleged. But, even before being sued, policyholders can and should take steps to enhance their coverage positions by being proactive in their analysis of their existing coverage.

Coverage determinations depend on the precise language used, and key language often varies in subtle but significant ways in CGL policies and in not so subtle ways in specialized policies such as cyber liability policies. Insurers are not likely to provide coverage for claims to recover the purchase price of a product that simply does not work, but some companies may want to consider purchasing product recall insurance.

And, for claims involving trade disparage-ment, violation of the right to privacy, damages from data breaches, copyright infringement in advertisements and more (such as products-completed operations), coverage may very well be available under CGL policies.

Procuring coverage with appropriately broad coverage terms and appropriately narrow exclusions for each company's particular risks is not something that generally happens by coincidence, but only through careful analysis. It is critical to have the right coverage in place before an event that leads to claims occurs.

In the event of a demand for payment or a lawsuit, the insured must promptly and carefully review the allegations and prepare appropriate notices to insurers. Policies generally require that prompt notice of claims be given to the insurer. Some courts have held that the failure to give prompt notice forecloses any insurance recovery.

The insured should consider all potentially implicated insurance policies and, further, should consider giving notice to umbrella and excess insurers even if it appears that the claim will not breach primary limits.

By being proactive and careful in buying or renewing coverage and by insisting on favorable policy terms, advertisers and companies that sell consumer products will maximize their likelihood of recovery in the unfortunate event that claims arise.

## NOTES

1 *Arch Ins. Co. v. Michaels Stores Inc.,* No. 1:12-CV-00786 (N.D. Ill. 2012); *XL Ins. Am. v. Michaels Stores Inc.,* No. 651909/2012 (N.Y. App. Div. 2012).

2 *CSA Nutraceuticals LLC v. Chubb Custom Ins. Co.,* No. 12-10317 (5th Cir. 2012); *CSA Nutraceuticals LLC v. Chubb Custom Ins. Co.,* No. 3:10-cv-02155 (N.D. Tex. Jan. 30, 2012).

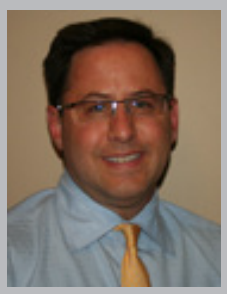
3 *Fed. Ins. Co. v. Velcera Inc. et al.,* No. 2:12-CV-03172 (E.D. Pa. 2012).

4 *Citizens Ins. Co. of Am. v. Nat'l Cas. Co.,* No. 3:12-CV-00430-IEG (WVG), 2012 WL 2127928 (S.D. Cal. June 12, 2012).

5 *Sawyer (d/b/a A-1 Security Locksmiths) v. West Bend Mut. Ins. Co. et al.,* No. 2010-CV-5852, 2012 WL 2742291 (Wis. Ct. App. July 10, 2012).

6 *Olsen v. Siddiqi et al.,* No. ED97455, 2012 WL 1699322 (Mo. Ct. App. May 9, 2012).

7 *Columbia Cas. Co. v. HIAR Holdings, LLC,* No. 07SL-CC00520 (Mo. Nov. 29, 2011).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