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PERSPECTIVE

Liability insurance often has a role in class action defense

By Peter S. Selvin

Three key cases that were decided this year highlight that liability insurance may often play an important role in providing for defense and indemnity in class actions.

In *Travelers Indem. Co. of Am. v. Portal Healthcare Solutions*, 35 F.3d 765 (E.D.Va. 2014), aff'd, 644 Fed. Appx. 245 (4th Cir. 2016), Portal Healthcare Solutions, a business specializing in the electronic safekeeping of medical records for hospitals, clinics and other medical providers, was sued in a class action by two patients of a hospital (Glen Fall) for which Portal provided electronic recordkeeping services.

The class action arose because certain confidential patient records appeared on the internet, causing those records to become publicly accessible. The class action complaint alleged that patients' confidential records were accessible and downloadable from the internet by unauthorized persons without security restrictions by a more than one-year period.

Travelers had issued Portal a policy of liability insurance which provided that Travelers was obligated to defend and indemnify Portal from injury arising from "electronic publication of material that … gives unreasonable publicity to a person's private life" (2012 policy language) or "discloses information about a person's private life" (2013 policy language).

The core issue in the coverage dispute was whether exposing material to online searching of a patient's name constituted "publication" of electronic materials within the meaning of the policy. The district court answered this question in the affirmative, rejecting Travelers' primary argument that because the data leakage was supposedly unintentional on Portal's part, there could be no "publication." The district court rejected this argument, holding that "the issue cannot be whether Portal intentionally exposed the records to public viewing since the definition of 'publication' does not hinge on the would-be publisher's intent. Rather, it hinges on whether the information was placed before the public." In April of this year, the 4th U.S. Circuit Court of Appeals affirmed this result.

Another case from this year also highlights the availability of liability insurance in class actions arising out of alleged violations of a group of individuals' privacy rights. In *National Fire Insurance Company of Hartford, et al. v. E. Mishan & Sons*, 650 Fed. Appx. 793 (2nd Cir. 2016), National Fire had issued commercial general liability policies to Emson, a company in the data storage and transfer business. The policies at issue contained "personal and advertising injury" coverage parts which would be triggered by, among other conduct, the "[o]ral or written publication … of material that violates a person's right of privacy."

Emson was sued in two class actions which alleged that it worked with two other companies to deceptively trap consumers into recurring credit card charges. In effect, the lawsuits alleged that Emson acted as a purveyor of data, facilitating "data passes" and transferring private customer information for profit.

National Fire declined to pick up Emson's defense in the underlying class actions, basing its decision on an exclusion for "personal and advertising injury" caused by "knowing violations of another's rights." The district court agreed with National Fire's position, noting that the underlying complaints alleged conduct that was intentional and knowing — i.e., that Emson "intentionally passed along the consumers' private information as part of a scheme to defraud those consumers."

The 2nd U.S. Circuit Court of Appeals reversed. In language that highlights a key distinction for coverage purposes — between what may be *alleged* in a complaint and the *actual elements* of a claim or cause of action — the court held that the "knowing violation" exclusion did not foreclose coverage because it could not be concluded with certainty "that the policy does not provide coverage, because

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the conduct triggering the violation policy exclusion is not an element of each cause of action." As illustrative, the underlying complaints alleged, among other claims, breach of contract and unjust enrichment — "neither of which require a showing of knowledge or intent."

Finally, a recent case from Delaware highlights the "damages vs. disgorgement" coverage battle that often follows an insured's settlement with a claimant. In *TIAACREF Individual & Institutional Services, et al. v. Illinois National Insurance Company*, 2016 WL 6534271 (Oct. 20, 2016), the Delaware Superior Court, applying New York law, held that amounts TIAA-CREF paid to settle several class actions did not represent "uninsurable disgorgement."

The case illustrates the distinction in insurance law between damages (which typically constitute covered "loss") and disgorgement, restitution, the return of so-called "ill-gotten gains" or regulatory fines, which are ordinarily not considered to be part of covered "loss." In this regard, Black's Law Dictionary defines disgorgement as "the act of giving up something (such as profits illegally obtained) on demand or by some legal compulsion." In addition, courts have defined disgorgement as serving the purposes of depriving a party of ill-gotten gains and deterring improper conduct. *See, e.g., Vigilant Ins. Co. v. Credit Suisse First Boston Corp.*, 2003 WL 24009803, at *4 (N. Y. Sup. Ct. 2003).

In the *TIAA-CREF* case, the class action complaints alleged that TIAA-CREF had improperly failed to credit the accounts of its customers with otherwise applicable investment gains pending its processing of transfer or withdrawal requests. While the defendant-insurers in *TIAA-CREF* sought to characterize the consideration paid in that case as akin to an "order to return funds," the court disagreed, pointing to both the absence of any SEC or other administrative dimension to the controversy and the presence in the parties' settlement agreement of language whereby the defendants expressly admitted no liability and denied any wrongdoing. While such language is often regarded as boilerplate in many settlement agreements, the court found this language to be important in distinguishing the settlement in *TIAA-CREF* from those instances in which payment arising out of a consumer class action would be regarded as uninsurable disgorgement and hence not part of "loss."

"*Credit Suisse* … involve[d] conclusive links between the insured's misconduct and the payment of monies. Not so here. TIAA-CREF settled and expressly denied any liability. The court finds no conclusive link between the settlements in the Underlying Actions and wrongdoing by TIAACREF that would render the settlement agreements uninsurable disgorgement."

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