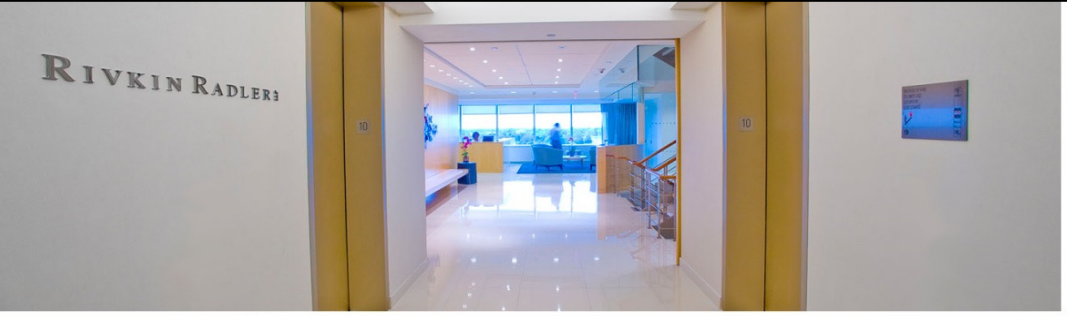

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California Supreme Court Rules That TCPA Claim Against Yahoo Might Be Covered

Yahoo was named in several putative class action lawsuits alleging that its unsolicited text messages violated the Telephone Consumer Protection Act (TCPA). It tendered the suits to its commercial general liability insurer for defense and indemnity.

The standard policy had a TCPA exclusion, but a negotiated endorsement removed the exclusion and modified the standard language in a few other ways. The endorsement covered "personal injury," defined to include "oral or written publication, in any manner, of material that violates a person's right of privacy."

The insurer declined to defend Yahoo and Yahoo filed a suit in federal court for breach of contract. The federal district court ruled for the insurer, finding that the policy covered liability for right of secrecy violations (to prevent disclosure of personal information to others) but not right of seclusion violations (to be free, in a particular location, from disturbance by others). The district court found that the policy language required the privacy violation to relate to the content of the published material. Because the TCPA claims focused on the transmission of unsolicited text messages rather than the content of those messages, the court dismissed Yahoo's suit.

Yahoo appealed and the Ninth Circuit submitted a certified question to the California Supreme Court, which the state high court rephrased as:

> Does a commercial general liability insurance policy that provides coverage for 'personal injury,' defined as 'injury … arising out of … [o]ral or written publication, in

> any manner, of material that violates a person's right of privacy,' and that has been modified by endorsement with regard to advertising injuries, trigger the insurer's duty to defend the insured against a claim that the insured violated the [TCPA] of 1991 (47 U.S.C. § 227) by sending unsolicited text message advertisements that did not reveal any private information?

Or more simply, did the endorsement cover right-of-seclusion violations litigated under the TCPA? (The parties agreed that the TCPA is not concerned with disclosures that violate the common law right of secrecy).

The California Supreme Court concluded that the endorsement covers right-of-seclusion violations, assuming such coverage is consistent with the insured's objectively reasonable expectations.

Here's how the court got there.

It found a facial ambiguity in the "personal injury" definition. Does the clause "that violates a person's right of privacy" modify the entire phrase "oral or written publication, in any manner, of material" or just the word "material"?

If it modifies only the word "material," then that implies that the privacy violation must refer to the informational content in the material, which the TCPA does not get at. But if it modifies the entire phrase, then even if the published materials were something that was not in the least private (for example, weather forecasts or sports scores), its publication in a manner that violated a person's right of seclusion would still amount to a covered privacy violation.

Under California law, ambiguities are not automatically construed against the insurer. Rather, the court must first try to resolve the ambiguity by applying standard rules of contract interpretation. If the standard rules do not resolve the ambiguity, then the court must interpret

the provision in favor of protecting the insured's reasonable expectations. If that does not resolve the ambiguity, then it will construe the ambiguity against the drafter.

In applying the standard rules of contract interpretation, the court pointed to several things that suggested the policy did not extend to violations of the right of seclusion. And although it found Yahoo's broad reading "far from conclusive," it was persuaded that an ambiguity remained even after applying the standard rules of construction.

Moving on to the second step, the court noted that merely removing an exclusion for TCPA liability is not, by itself, enough to establish coverage. Whether it was objectively reasonable for Yahoo to expect coverage of its TCPA liability, however, couldn't be resolved without further litigation.

As for the final step – construing ambiguities against the drafter – the court considered if the insurer was actually the drafter where a sophisticated party had bargained over the terms of a manuscript endorsement. But because here, the endorsement used language adopted verbatim from insurer-drafted policies, the court found that Yahoo itself could not be charged with creating the ambiguity.

So the court ruled that the provision must be interpreted in a way that fulfills Yahoo's reasonable expectations, which must be determined in further litigation. If that doesn't resolve the ambiguity, then it must be construed against the insurer as the drafter.

The court also disagreed with the district court that the last antecedent rule resolved the ambiguity in favor of the insurer. It explained that the rule of the last antecedent states that "qualifying words, phrases and clauses are to be applied to the words or phrases immediately preceding [them] …." The rule is most readily applied where there is a list of several items, and the modifier comes immediately after the last item on the list. But here, there was no list of items

followed immediately by a modifier; instead, there's the phrase "[o]ral or written publication, in any manner, of material" followed immediately by a modifier.

The Ninth Circuit has since remanded the case to the district court to determine Yahoo's reasonable expectations.

The case is *Yahoo Inc. v. Nat'l Union Fire Ins. Co.,* No. S253593 (Cal. Nov. 17, 2022).

Minnesota Federal Court Holds That Losses from Email Hack Are Covered by Policy's Data Breach Form

Fishbowl is a technical consulting company. It invoices its clients by email. A hacker gained access to the email account of one of Fishbowl's staff accountants and created a series of rules that redirected emails and allowed the hacker to impersonate the staff accountant and Fishbowl's clients.

The hacker next emailed one of Fishbowl's clients and asked that payment be sent to its new bank account. The client unwittingly sent the payment to a bank account controlled by the hacker. When Fishbowl followed up with the client about payment, the hacker intercepted the email and told Fishbowl that payment was on its way.

After receiving a message from its bank, the client contacted Fishbowl to confirm the correct routing number for payment. The hacker, posing as the staff accountant, confirmed the fraudulent routing number and the client wired payment for a second invoice to the same fraudulent account. The two payments totaled $176,962. Only a small portion was ultimately recovered.

Fishbowl had a Technology Professional Liability policy with a Data Breach Coverage Form. Fishbowl notified its insurer, who denied coverage. Fishbowl then sued its insurer. Both parties moved for summary judgment.

The dispute centered on the Cyber Business Interruption and Extra Expense clause. To qualify for coverage, Fishbowl had to show: 1) an actual loss of "business income;" 2) which occurred during the "period of restoration;" 3) directly resulting from a "data breach;" 4) that it discovered during the "policy period;" and 5) which resulted in an actual impairment or denial of service of "business operations" during the "policy period." The parties agreed that Fishbowl experienced a "data breach" and that it was discovered during the "policy period."

The court first took up the issue of whether there was a loss of "business income." And this required the court to consider if the money the client paid to the hacker was Net Income that would have been earned as part of Fishbowl's "business operations." The insurer argued that it wasn't because invoicing clients is not an income-generating activity and that Fishbowl sought recovery of money already earned, rather than money that would have been earned. But the court rejected the insurer's argument, finding that "business operations" was not restricted to only income-generating activities and could reasonably be understood to mean all business activities performed with a certain frequency and consistency. The court also found that Fishbowl's accrual accounting method – income is earned when Fishbowl performs the work and issues an invoice, not when it receives payment – was not relevant because the insured would not have expected the definition of "earned" to depend on the insured's method of accounting.

The next major issue concerned whether Fishbowl's loss "directly" resulted from the data breach. The insurer argued that Fishbowl's loss did not result directly from the conduct of the hacker, but an intervening agency; it was due to the client's negligence in failing to notice warning

signs in the fraudulent emails. But the court said that the client had not been impleaded into the action and it could not rule based on the paucity of evidence that the client's actions constituted an "intervening agency." Because Fishbowl's loss would not have occurred without the hacker accessing the staff accountant's email and sending fraudulent communications, the court found that Fishbowl's loss "directly result[ed] from" the data breach.

The insurer next argued that there was no "impairment" of Fishbowl's "business operations" because it continued to conduct its income-generating activities. But the court disagreed, finding that "impairment" did not require the business to cease functioning entirely. Because Fishbowl's ability to communicate with its clients was diminished, the court found that the hacker's data breach resulted in an "impairment" to Fishbowl's business operations.

Finally, the insurer argued that a finding of coverage would contradict the whole purpose of business interruption insurance. On this point, the court acknowledged that historically the purpose of "business interruption insurance may have been to 'protect the prospective earnings of the insured business only to the extent that they would have been earned if no interruption occurred.'" But the court found this concept applied only to policies that insured against losses from an "interruption" of business, and that here, the policy insured against "actual impairment or denial of service." In upholding coverage, the court reasoned that the policy's use of "impairment" rather than "interruption" meant that it affords coverage when a business suffers something less than a total suspension of operations.

The case is *Fishbowl Solutions, Inc. v. Hanover Ins. Co.*, No. 21-cv-00794 (SRN/DJF) (D. Minn. Nov. 3, 2022).

Harvard's Notice Was Too Late, Massachusetts Federal Judge Holds

Harvard University sought to have its excess insurer pay for Harvard's defense of an affirmative action case. The excess policy was written on a claims-made-and-reported basis, meaning that the claim must be made during the policy period and reported to the insurer within 90 days after the policy ends.

For the policy to apply, Harvard needed to notify its insurer of the suit by January 30, 2016. But Harvard did not notify its insurer until May 23, 2017, which the court observed was "well past the deadline."

The fact that the policy was a claims-made-and-reported policy was important. That's because an insurer doesn't have to show that it was prejudiced by the policyholder's delay in giving notice under this type of policy. As the court observed, notice under a claims-made policy is "of the essence" in determining whether coverage exists and the policyholder's failure to notify its insurer of a claim within the policy period precludes coverage. Under Massachusetts law, the notice requirement in a claims-made-and-reported policy is to be strictly enforced without an exception for lack of prejudice. Requiring the insurer to show prejudice, the court explained, would defeat the fundamental concept on which claims-made policies are premised.

The court also found that the insurer's actual or constructive knowledge of a claim did not excuse the policyholder from complying with the notice obligations in the policy.

As the court put it: "because an unambiguous insurance policy must be applied as written; the notice provision in a claims-made policy must be strictly construed; and Harvard's failure to satisfy a condition precedent vitiates coverage," summary judgment for the insurer was warranted.

The case is *President and Fellows of Harvard College v. Zurich Am. Ins. Co.,* No. 21-cv-11530-ADB (D. Mass. Nov. 2, 2022).

Federal Court in Oklahoma Applies Total Pollution Exclusion to Negligent HVAC Installation Claim

The insured, B&B Heat & Air, Inc. installed heating, ventilation, and air conditioning (HVAC) systems. The claimant alleged that B&B negligently installed her HVAC system and that the system pulled small, poisonous fiberglass particles from her attic into her home. The claimant alleged serious health problems from ingesting these materials and sued B&B.

B&B's insurers denied coverage, citing a total pollution exclusion that barred coverage for bodily injury "which would not have occurred in whole or part but for the actual, alleged or threatened discharge, dispersal, seepage, migration, release or escape of pollutants at any time." "Pollutants" meant "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste."

B&B's insurers filed a declaratory judgment action in federal court. Applying Oklahoma law, the court granted summary judgment to the insurers and held that they had no duty to defend or indemnify B&B for the claim.

That the pollutant – fiberglass particles – wasn't supplied by B&B or used in its normal business activities was immaterial. The court rejected B&B's reliance on the reasonable expectations doctrine. B&B had failed to explain how a reasonable person would believe that the exclusion applied only when B&B used the pollutant as part of its work.

The court also rejected B&B's argument that the claim fell under the policy's "products-completed" coverage and that this coverage was not subject to the pollution exclusion. The court

noted that the definition of "products-completed operations hazard" was in the general definition section of the policy and that definition incorporated other terms used throughout the policy. It did not matter that B&B paid more premium for "products completed" coverage.

The case is *Ohio Sec. Ins. Co. v. B&B Heat & Air, Inc.*, Case No. 21-CV-009-CVE-SH (N.D. Okla. Nov. 23, 2022).

Federal Court in Florida Applies Professional Services Exclusion to Defective Construction Claim

Rosalyne Holdings, LLC sued the insured, Coastal Construction Management, LLC, for defective construction of an apartment complex. Coastal's insurance policy had an exclusion for "professional services." The policy said, "professional services" "includes but is not limited to: "inspection, supervision, quality control, architectural or engineering activities done by or for you on a project on which you serve as construction manager" and "engineering services, including related supervisory or inspection services."

The insurer, Colony Insurance Company, filed a declaratory judgment action in Florida federal court. The court found no coverage under the policies based on the "professional services" exclusion.

The court noted that, although "professional services" was undefined, it was commonly understood to mean services requiring a high degree of knowledge or skill that is primarily mental rather than physical. The court held that "[a]s a matter of common sense," the construction management, supervision, and quality control activities described in the underlying complaint were not activities a layperson could undertake.

The court rejected Rosalyne's argument that the exclusion didn't apply unless Coastal performed these functions as a "construction manager." The court noted that the exclusion applied to all "professional services" and the examples of work as a construction manager in the exclusion were only illustrative. The court held that the nature of the activities themselves controlled, and the activities alleged in the complaint plainly required specialized training and experience. For these reasons, the court ruled for Colony.

The case is *Colony Ins. Co. v. Coastal Constr. Mgmt., LLC*, 8:21-cv-2541-TPB-AAS (M.D. Fla. Nov. 2, 2022).

Oregon Federal Court Applies Time on Risk Allocation to Defense Costs for Long-Tail Environmental Claim

National Surety Corporation (NSC) and TIG Insurance Company insured McKay Investments Company, which beginning in 2009, faced enforcement action by Oregon regulators for pollution from a former dry cleaner at McKay's property. NSC and TIG insured consecutive years. A dispute arose between NSC and TIG about allocation of defense costs. NSC filed a declaratory judgment action in Oregon federal court.

The court, applying Oregon law, held that defense costs should be allocated based on time on risk. The court reasoned that coverage limits do not bear on an insurer's obligation to undertake an insured's defense. The court determined that policy limits should matter only if the insurers policies at least partially overlapped.

But the court held that indemnity costs should be allocated based on an average of each insurer's *pro rata* time on the risk and policy limits percentages. The court noted that using an average of each party's time on the risk and policy limits percentages took into account the fact

that defendant's time on the risk was longer, but plaintiff's policy limits were higher. This method, the court held, best reflected the relative amount of risk each party assumed when insuring McKay.

The case is *Nat'l Sur. Corp. v. TIG Ins. Co.*, No. 3:21-cv-00266-HZ (D. Or. Nov. 2, 2022).