



CAMBRIDGE
PROPERTY & CASUALTY

INSURANCE COVERAGES FOR TECHNOLOGY COMPANIES

In this age of ever advancing technology, Internet related companies, hardware and software companies, and other technology organizations face unique exposures. The Cambridge Group attorneys have written this Special Report to analyze some risks inherent to such companies, and to provide suggestions on how to address those exposures through a property tailored insurance program.

I. PROPERTY EXPOSURES

A. Exposure for Loss or Damage to Owned or Leased Computer Systems

Although all companies face the exposure of damage to property owned or leased by the business, computer and technology companies must deal with the potential for damage to computer systems, networks, software, the loss of data, and the loss of access to information. Standard “contents” insurance is not enough.

Hardware and software can be damaged by electrical arcing, power surge (generated on-site or off premises) as well as by computer viruses or worm viruses. Specialized coverage can be purchased to address these exposures, commonly referred to as “electronic data processing equipment coverage” which is added to the property insurance policy. However, some such policies contain limitations for power surge coverage, requiring that the power surge occur within 1,000 feet of the

premises. This type of limitation should generally be unacceptable to technology companies.

Property that is maintained off-site such as equipment at an Internet Service Provider, should be given special attention. Such property is not automatically covered for significant amounts undermost property insurance policies. If such equipment is permanently located at an off-premises site, that site should be listed as a scheduled location on the property insurance policy.

Many companies today have laptop computers that are used by employees of the company and taken to various locations. Many property insurance policies contain limitations on the extent of such coverage and efforts should be made to obtain broader coverage with higher limits in this area.

B. Loss of Income and Extra Expenses Associated with a Business Interruption

In the event of a power surge, fire, windstorm, theft or other peril that causes loss or damage to property, your company could be exposed to loss of income as well as the incurring of extra expenses such as obtaining a higher paying month-to-month lease, renting temporary equipment, and notifying your customers of your temporary address. You would also most likely incur significant overtime

expenses of your employees in getting back in business.

Business interruption insurance is a critical dimension of a commercial insurance program and should include coverage for loss of income and extra expenses associated with computer hardware and software (EDP) losses.

Many technology companies can suffer contractual penalties arising out of the inability to perform on a contract due to a fire or other covered cause of loss. The better property insurance policies will include some coverage for this exposure.

C. Loss of Favorable Rental on Computer Equipment

Leasehold interest coverage can be purchased to protect the organization for loss of favorable leases on computer equipment that becomes damaged in a fire or other loss. This would pay for the difference between the favorable lease and the amount of a higher replacement lease.

D. Computer Fraud

Computer hackers can invade systems to steal information from your company including money and securities. In this situation, you could suffer significant damage. Most property insurance policies do not cover this risk. As a result, separate coverage should be considered.

E. Exposures to Employee Theft

Even if you buy employee dishonesty coverage, it probably does not automatically cover theft by your employees of information or property of others. Specialized coverage is available to protect you for this contingency, called third party employee dishonesty coverage.

II. LIABILITY INSURANCE EXPOSURES

A. Commercial General Liability Exposures

Most businesses carry commercial general liability (CGL) insurance which covers bodily injury, property damage and some other exposures such as libel, slander, defamation, and wrongful entry or wrongful eviction. For example, if a customer slips on your property and sues you for negligence, such a policy would cover this exposure.

CGL policies also typically include coverage for products liability. For example, if a component you manufacture causes a fire which burns down your customer's building, products liability coverage would pay for the resulting loss, up to your limit of insurance.

As noted below, a CGL policy alone is not sufficient to protect the interests of a technology company. Instead, other policies should be considered in a commercial insurance program for such companies, including a professional liability policy, a cyber-liability policy, an intellectual liability insurance policy, and a directors and officers / employment practices liability policy.

B. Professional Liability

Electronics E & O insurance provides coverage when a product fails to perform as intended due to an act of negligence, error or omission without any physical injury or property damage.

Insurers typically exclude from such policies contractual liability, products recall, wear and tear, electrical power supply change, performance delay, cost guarantees and intentional acts.

Importantly, many such policies also exclude infringement of copyright, trademark or patent as well as unfair competition or piracy.

Security breach due to product malfunction is a coverage that can be added by way of an endorsement to many such professional liability policies.

Examples of professional liability claims:

- a) A software developer gets sued by a customer who alleges that the software was infected with a computer virus.
- b) A customer of a computer company files suit claiming loss of revenue associated with a defective spreadsheet it sold.
- c) In the process of installing upgrades to a network, a computer company accidentally erased millions of dollars in data.
- d) A customer sues claiming that the system recommended by the hardware vendor did not meet its needs.
- e) Unauthorized users invaded a high tech website. The company sued the hosting provider for negligence in the design and monitoring of the system.
- f) A semiconductor manufacturer is sued for not meeting customer specification tolerances.
- g) A security “fire wall” designed by a software developer malfunctions, resulting in a hacker stealing data and infecting the software with a virus.

C. Intellectual Property Liability Exposures

An area of significant exposure for computer and technology companies is the area of lawsuits and claims that “intellectual property” owned by another company have been violated. Intellectual property is a broad term that refers to legally protected work-product. The following are some intellectual property “offenses:”

- Piracy
- Copyright infringement
- Patent infringement
- Trademark or service mark infringement
- Plagiarism or unauthorized use
- Cybersquatting

Examples of intellectual property claims:

- a) An internet concern that offers the downloading of music is found liable by a federal court for infringing copyrights of record companies.
- b) A software company sues its competitors for counterfeiting of its products and piracy.
- c) A high-tech company which manufactured sorting machines that used complicated software programs sues a company for selling its machines that contained the software the manufacturer owned.
- d) A company is sued for “cybersquatting,” or registering a trademark name and later trying to sell that name to a company that holds that trademark. Not all standard liability insurance policies provide coverage for these exposures and a separate policy may be needed.

D. Breach of Privacy Exposures

Internet companies are particularly prone to allegations of breaching someone's right to privacy. For example, gathering consumer buyer habits and linking such information to specific consumers was alleged in one suit to violate the right to privacy. Disclosing confidential information of consumers or others can quickly catapult an organization into litigation for breach of privacy.

New laws in Michigan and other states require immediate notification of all consumers affected by the breach. These can be very costly. Cyber-liability policies can cover this.

The real issue associated with this is that many insurers are wising up to the privacy exposure and are excluding personal and advertising injury from the general liability insurance policies of Internet and technology companies. This takes away significant coverage and alternative coverage should be purchased such as an intellectual property and communications liability insurance policy.

CHECKLIST OF EXPOSURES/INSURANCE COVERAGES FOR TECHNOLOGY COMPANIES

The following checklist is provided as a tool to assist the high tech company with understanding some of the important coverages to consider as part of a commercial property and casualty insurance program. These areas represent the starting point in analyzing many insurance coverage needs based on the experiences of the Cambridge risk managers and attorneys in putting together such insurance programs.

TECHNOLOGY COMPANY EXPOSURE	INSURANCE COVERAGE NEEDED
<input type="checkbox"/> Professional liability for lawsuits or claims involving mistakes in setting up or hosting computer systems, web-sites, or the development of hardware or software	Professional liability / errors and omissions liability insurance policy
<input type="checkbox"/> Liability for fire damage to your customer's building caused by your defective component part	Commercial general liability insurance policy
<input type="checkbox"/> Costs for additional expenses associated with repairing your computer system, obtaining lost data, or setting up at a temporary location and renting temporary equipment while your building is being re-built	Extra expense insurance as an endorsement to your property insurance
<input type="checkbox"/> Loss of data stolen by a computer hacker	Specialized EDP coverage including coverage for theft of data/extra expense coverage
<input type="checkbox"/> Claims of infringement of trademarks or service marks not associated with advertising	Intellectual property liability insurance - can be purchased separately or sometimes as part of a professional liability insurance policy
<input type="checkbox"/> Claims of trademark infringement associated with advertising activities	Commercial general liability insurance (unless excluded); communications liability policy
<input type="checkbox"/> Exposure for damage to computers from electric arcing or power surge	Electronic data processing coverage
<input type="checkbox"/> Exposure for damage to computers or equipment being transported	Transit coverage for EDP
<input type="checkbox"/> Exposure for lawsuits or claims by employees claiming breach of employment contract, discrimination, sexual harassment, etc.	Employment practices liability coverage
<input type="checkbox"/> Exposure for expenses associated with recall of defective products which pose a danger to others	Products recall coverage
<input type="checkbox"/> Exposure for lawsuits or claims by banks, investors or others that officers or directors of the company committed malpractice in the management of the company	Directors and officers liability coverage

<input type="checkbox"/>	Exposure for theft of money or other property by employees	Employee dishonesty coverage
<input type="checkbox"/>	Exposure for computer fraud whereby your employees steal from your customers	Third party employee dishonesty coverage
<input type="checkbox"/>	Exposure for claims by landlord's insurance company that your company was negligent in causing property damage, such as fire, to the landlord's building.	Legal liability coverage as an add-on to your property insurance. Limits should be at least \$1,000,000 rather than the typical \$50,000, and should be broader than for just the peril of fire
<input type="checkbox"/>	Exposure for suit alleging breach of privacy	Commercial general liability or communications liability policy
<input type="checkbox"/>	Exposure for theft of money or other property via computers by other than employees	Computer fraud coverage
<input type="checkbox"/>	Exposure for damage to property off-premises, such as ISP providers	Add location to property insurance policy unless temporary; If temporary, assure that limits are sufficient
<input type="checkbox"/>	Exposure for loss of income because of a computer virus or worm virus that causes a slowdown in the system with no apparent damage	Computer virus / worm virus coverage to property insurance policy
<input type="checkbox"/>	Exposure for loss of favorable lease of computer equipment or software	Leasehold interest electronic data processing coverage
<input type="checkbox"/>	Exposure for loss of income due to new product delay arising out of a fire or other covered loss	Remote and consequential loss coverage should be included with your business interruption coverage
<input type="checkbox"/>	Costs of notification of consumers affected by breach of security and unintended release of information.	Cyber-liability.