Cyber Insurance in Disarray

by Joshua Gold

To say that the insurance market for computer-related perils is in a state of flux is putting it politely. Insuring information assets and covering risks from doing business online has never been more challenging. Policyholders are offered a dizzying array of incomplete, untested and sometimes incomprehensible specialty insurance products supposedly designed to cover this area of risk. Worse still, they are expensive and finding the desired limits can be daunting. So how did we get to this point?

Over the last 10 years, so-called "cyber" risks were covered under a policyholder's existing insurance program. Some manuscript insurance policies actually provided express coverage for loss from, or damage to, software, hardware, programming and other computer hazards under "all risk" provisions. Few liability and property policies contained exclusions aimed at computer perils. Some insurance companies added cyber coverage into their existing product line. General liability policies continued their personal injury and advertising injury coverages, which protected against a host of internet risks, including domain name disputes.

Then Y2K terrified boardrooms around the world. While the brunt of Y2K damage was avoided, it was a chilling message to insurers that the commercial risks they had underwritten for more than a century had shifted markedly. No longer were computer perils just the esoteric risk profile of a few companies in Northern California. Every policyholder now had almost complete reliance upon computers for even the most standard business functions.

But as developed economies have shifted further from manufacturing to information services, the insurance industry has been slow to make the transition with its own product line. Rather than continue to offer coverage for computer-related risks under all risk property and general liability insurance policies, many insurance companies began the process of revisionist history and imposed policy exclusions for a number of online perils. At one stage, an ISO endorsement provided a measure of liability coverage, but sublimited it to $2,500. This was not exactly the kind of risk transfer most businesses were looking for.

So now, policyholders are left with a patchwork of partial insurance coverage options. Some policyholders can find protection for computer perils under existing property, liability and crime insurance policies. Many others are forced to go without or purchase emerging insurance products that are in the process of being modified—for better or for worse. If the insurance industry gets its way, it will likely try to push all commercial policyholders into these new stand-alone, specialty insurance policies by eliminating or restricting coverage under the more conventional programs presently bought by businesses.

This shift toward computer specialty insurance products is emblematic of a broader change under way in the insurance industry—the move away from comprehensive insurance policies to specialty lines. This compounds the terms, conditions, exclusions and endorsements, making synthesis and seamlessness of insurance programs elusive. This shift yields few benefits to policyholders who are forced to double-up on coverage exclusions where specialty coverage is imposed. Arguably, the only ones who benefit from this approach are coverage attorneys and insurance companies, which tend to exploit potential escape hatches when confronted with large or recurring claims.

So, what to do? Policyholders and their brokers have to be vigilant and persistent in getting the best forms available in the market. All terms are not alike. There are brokers who are knowledgeable about the positives and negatives associated with each specialty form. These same brokers are also aware of the modifications that can be made on policy terms to get back that which the fine print robs. More importantly, policyholders need to consider building into their existing policies some of these specialty coverages by way of endorsement, rather than by stand-alone coverage. If an endorsement's insuring promise is broad enough, endorsing the coverage to an existing form with adequate policy limits is often a better course than becoming saddled with yet another stand-alone policy. ■