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Surprise! Your Company May Have Insurance Coverage for a Consumer Class Action

By Finley T. Harckham

Every day, class actions are commenced on behalf of consumers against manufacturers, retailers, financial institutions and service providers. Some companies assume that such cases are not covered by their insurance because class actions must be crafted to address issues common to all of the plaintiffs and therefore tend not to seek monetary damages that are covered by liability insurance. That skepticism is understandable because many, or even most, consumer class actions seek only relief that is not covered, such as damages for defective products failing to perform as intended, or to punish for deceptive practices barred by consumer protection statutes. However, all class action complaints should be read carefully for any covered claims, bearing in mind that most companies have coverage under their general liability policies not only for third-party property damage and bodily injury, but also for personal and advertising injury.

Policyholders may also have coverage for a variety of "wrongful acts" under directors and officers, errors and omissions, and employment practices liability policies. Further, invasion of privacy claims may be covered personal injury under general liability policies, covered under cyber policies, or in cyber coverage found in other types of policies. Most importantly, even if a class action complaint does not clearly contain covered allegations, it will frequently assert claims that are *potentially* covered, and that is all that is needed to trigger valuable defense coverage.

Here are a few examples of class action complaints that may be covered in whole or in part:

Product defect claims: As a general rule, claims alleging product defects are covered by general liability insurance if they seek damages for bodily injury or damage to third-party property, but not if they are based solely upon purely economic loss resulting from a product that does not function as expected. Many class action complaints allege that products are dangerous due to a design or manufacturing defect. Often, they provide examples of alleged bodily injuries or damage to third-party property that have been caused by the product. Such complaints often use vague and general terms to describe the relief sought, including "damages," and should be read carefully to determine whether they leave open the possibility that the plaintiffs are alleging covered harm. The answer can often be found in two places in the complaint: (1)

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the section describing the class, which may or may not specifically exclude individuals who have suffered damage or injury; and (2) any alleged statutory basis for claims, such as the Uniform Commercial Code, or warranty or consumer protection acts, which address not only the repair, replacement or sale of defective products but may also allow recovery of undefined damages that result directly from a breach of warranty. Such damages may be based upon alleged bodily injury or third-party property damage.

Product defect claims where the product has affected the functionality of third-party property: For example, a claim that adulterated heating oil has affected the performance of a furnace could be covered "loss of use," which commonly falls within the definition of "property damage" in general liability policies. Indeed, a number of cases have interpreted loss of use coverage to include damages for diminished functionality. Also, coverage may exist for defect claims if replacing the defective product would cause damage to other property. For example, allegations that electrical wiring used in homes is defective would not ordinarily be covered if the plaintiffs sought only to recover the cost of the product, but damage caused to other property in order to remove and replace the product, such as walls, might be covered.

Claims of improper fees or other charges by financial institutions: Numerous class actions have alleged that banks and other financial institutions have charged hidden fees or otherwise improperly handled transactions or accounts. Such claims seek the recovery of improper charges, which generally fall within the coverage grant of D&O and E&O policies. However, insurance companies typically deny coverage for these claims based upon exclusions that apply to the disgorgement of ill-gotten gains. However, those exclusions are often found in court not to apply, either because they are limited to instances where there has been a judicial determination that the policyholder was not entitled to the money, or because the enrichment of the policyholder is not a necessary element of the claim.

Invasion of privacy claims: Many class actions assert invasion of privacy by employers or by a wide array of players in the computer, internet and telecommunications industries. Such claims may be covered under a variety of insurance policies, including general liability (personal injury), employment practices liability, cyber, D&O and E&O. For example, in recent class actions alleging that personal information was acquired by an application installed into mobile phones, some defendants successfully invoked invasion of privacy coverage under their general liability policies.

The Value of Defense Coverage

Policyholders should not give up if a covered claim does not jump off the page of a class action (or any) complaint, or if the main thrust of the action is an excluded claim. Under most liability policies the insurance company's defense obligation is triggered as long as any claim in the complaint is potentially covered. So, all that must be shown in order to secure defense coverage is that the plaintiffs might be able to prove that something is not excluded. This standard is to be liberally applied by the courts. In most jurisdictions the duty to provide defense coverage is an issue of law that is typically decided on summary judgment based only upon a comparison of the complaint and the insurance policy, without discovery or consideration of any other extrinsic evidence. Therefore, the defense obligation often can be determined quickly and inexpensively —at least compared to litigating other issues.

The question of whether the defense obligation is triggered may not be the end of the dispute over defense coverage. Whether the insurance company must pay all defense costs or just those necessary for potentially covered claims, and whether the insurer may later be able to recoup defense costs depending upon the outcome of the case, varies from policy to policy. Nonetheless, defense coverage is valuable not only for the payment, or at least advancing, of litigation costs, which are often the greatest expense of a class action, but also because an insurance company that is incurring defense costs is likely to be willing to pay, or at least contribute to, the settlement of a class action to bring finality to its obligation.

Thus, corporate policyholders should not assume that class actions against them by consumers will not be covered. Instead, they should review the complaints carefully and consider the potential for coverage under all their insurance policies.

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