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Technical Advisory

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Subject: Is Electronic Data “Tangible Property” in the CGL?

Background: Those who think “*there’s nothing new under the sun*” have never worked in insurance. While it may be stressful, hectic and occasionally chaotic, insurance is never dull. In fact, one of the most interesting things about insurance is that it is often on the cutting edge of what’s going on in the world. The Information Age has brought incredible resources and capabilities to anyone with a computer. At the same time, information stored in a digital format has challenged the traditional insurance definition of what constitutes “property” – from both a first party and a third party standpoint.

At least as far back as the late 19th century, it was recognized that *information, ideas and other forms of expression* had value, separate from the paper or other medium it was produced on. The 1883 Paris Convention for the Protection of Industrial Property, and the 1886 Berne Convention for the Protection of Literary and Artistic Works, laid the groundwork for protecting what was later called “intellectual property.” Another milestone was the 1967 Convention Establishing the World Intellectual Property Organization (www.wipo.int/).

Insurance coverage forms have long recognized that the *information* being stored or recorded on various media had a value. Such coverage was incorporated into Valuable Papers & Records coverage, and similar coverages, such as Accounts Receivable coverage, etc. Later, Electronic Data Processing (EDP) policies came to market, as computers and computerized records expanded into mainstream business use.

Today, with digital records ubiquitous in both business and personal use, the insurance world has strived to develop and refine coverages appropriate for these new exposures. At the same time, traditional policies which provided coverage for one’s own property (first party), or for damage done to someone else’s property (third party), have

attempted to clarify how the long-established understanding of “property” dealt with information stored in an electronic format.

Main Points. The insuring agreement for Coverage A in the CGL provides coverage as follows:

“We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies.” [Emphasis added.]

In the 2001 edition of the CGL, the Definitions section revised the term “*property damage*” to reflect the intent that damage to electronic data was not considered within the definition. Revised language appears in **bold**:

“Property damage” means:

a. Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or

b. Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the "occurrence" that caused it.

For the purposes of this insurance, electronic data is not tangible property.

As used in this definition, electronic data means information, facts or programs stored as or on, created or used on, or transmitted to or from computer software, including systems and applications software, hard or floppy disks, CD-ROMS, tapes, drives, cells, data processing devices or any other media which are used with electronically controlled equipment.

However, this change did not address broader aspects of certain claims related to or arising out of damage to electronic data. There remained an unresolved issue of a potential conflict (or ambiguity) between removing electronic data from the definition of “property damage,” and the coverage provided within that definition for “*b. Loss of use of tangible property that is not physically injured.*” In numerous cases involving losses of and to electronic data, claims were also made for the inability of the computer system to operate without the electronic data. In such cases, the argument was made (sometimes successfully) that a computer system, or a computerized production machine, etc., suffered loss of use even though the system itself wasn’t damaged.

In an attempt to reconcile this, the 2004 edition of the CGL added an exclusion under Coverage A for Electronic Data:

p. Electronic Data

Damages arising out of the loss of, loss of use of, damage to, corruption of, inability to access, or inability to manipulate electronic data.

As used in this exclusion, electronic data means information, facts or programs stored as or on, created or used on, or transmitted to or from computer software, including systems and applications software, hard or floppy disks, CD-ROMS, tapes, drives, cells, data processing devices or any other media which are used with electronically controlled equipment.

At the same time, endorsement CG 04 37 12 04 Electronic Data Liability was introduced, which offered a buy-back for some of the potential claims a CGL insured might face who has damaged electronic data. This endorsement basically provided coverage for losses of and to electronic data that “*result from physical injury to tangible property.*”

In addition, ISO also introduced a separate coverage form in 2004 – the CG 00 65 12 04 Electronic Data Liability Coverage Form. This new form is on a claims made basis, and provides broader coverage than the CG 04 37 12 04.

Below is an excellent article reprinted from the IIABA Virtual University (VU), which discusses the various issues involving damage to electronic data and the CGL. This particular article is a posting of a question from one of the 25,000 VU subscribers from around the country, and responses from some of the VU volunteer faculty. The VU has hundreds of articles on a wide variety of subjects important to independent agents. The VU is a great resource, and best of all access to the VU is free to all member agencies. There is a link to the VU on the IIABL home page (www.iiabl.com). Just use your ID and password (provided free).

[Insuring Liability for Loss of Electronic Data](#)

Abstract

In [VUpoint Newsletter Vol. 7, No. 22, November 3, 2006](#), we featured two articles about insuring and risk managing the theft of customers' information. In this article, we'll look specifically at coverage under the CGL program. The CGL policy excludes "electronic data," for which there is something of a buy-back with the CG 04 37 endorsement, contingent on physical damage to tangible property. So, just what does the CG 04 37 cover and how?

Question: “Please give us your opinion(s) of the interpretation of coverage for the referenced forms, and hopefully, provide some simple examples of a covered loss.

"On paragraph p. Electronic Data of the [CG 00 01 12 04](#), damages to 'electronic data' is excluded. That exclusion for 'electronic data' can be bought back through form [CG 04 37 12 04](#) provided there is physical injury to tangible property. Since this is a CGL policy, I am saying that the buy-back is moot because property in the CCC that is being

worked on by the Insured is separately excluded. So please disregard all other parts and direct your attention only to tangible property and the electronic data sections we are referencing.

"If an Insured causes a loss and there is physical damage to tangible property, does the buy-back portion mean there is coverage for the restoration of the damaged 'electronic data' or does that only mean the replacement of blank 'electronic data'? Please provide some simple examples of a covered loss and what is 'owed' (restoration of files?) in the settlement of this loss."

Editor's Comments: The issue of insuring loss of data or information — on a first or third party basis — is a difficult one. As mentioned in the abstract above, we recently discussed the issue of theft of information and the applicability of liability vs. crime forms. In this case, we'll take a broader view of the exposure from a liability standpoint.

Faculty Response #1. The latest CGL definition of "property damage" is damage to tangible property. However, the definition states that electronic data is not tangible property. Therefore, if the insured caused a PD loss that resulted in loss of electronic data, there would be no coverage. For example, I install wiring in a building. During the installation, I cause a power outage in the building which results in the loss of electronic data. The unendorsed CGL would not cover this loss.

In fact, the latest version of the CGL emphasizes this fact even further by adding an exclusion for electronic data. The policy does not cover damages from the loss, loss of use, damage to, corruption of, inability to access, or inability to manipulate electronic data. The exclusion also includes a definition of electronic data.

Endorsement [CG 04 37 12 04](#) provides a means for buying back liability coverage for damage to electronic data. The endorsement adds a provision specifying that "loss of electronic data" is a category of "property damage." Such loss must, however, result from "physical injury to tangible property"—presumably some direct damage to software media or the computer hardware itself. The endorsement provides for a "loss of electronic data limit"—a sublimit of the occurrence limit—to be specified in the endorsement schedule.

In this form, "electronic data" means information, facts or programs stored as or on, created or used on, or transmitted to or from computer software (including systems and applications software), hard or floppy disks, CD-ROMS, tapes, drives, cells, data processing devices or any other media which are used with electronically controlled equipment.

The ISO 2004 filing introduced a new new coverage form - Electronic Data Liability Coverage Form ([CG 00 65 12 04](#)). The form provides coverage broader than that available under the CGL electronic data endorsement (CG 04 37), since it covers actual loss of data without requiring associated "physical injury to tangible property." But it does not address coverage of the consequential property damage exposures, which is

eliminated by the CGL electronic data exclusion. The form is written on a claims-made basis and covers loss caused by an "electronic data incident." "Electronic data incident" is defined as "an accident, or a negligent act, error or omission, or a series of causally related accidents, negligent acts, or errors or omissions, which results in loss of electronic data."

Per [IRMI](#), an "electronic data incident" is a broader concept than an "occurrence," since it may consist either of an accident (as an occurrence does); or a negligent act, error, or omission; or a series of accidents, negligent acts, errors, or omissions. Extension of coverage to losses caused by an error or omission avoids potential coverage disputes based on the intentionality of the act that caused the loss, or the fortuity of the loss given a particular act.

Faculty Response #2. The writer is correct if all of the electronic data in question is contained within a computer or other media which at the moment of loss resides in the CCC of the insured.

Any other situation represents possible coverage created by the endorsement. For example, the insured's employee, while delivering another piece of equipment in the vicinity of the computer, accidentally backs his forklift into the computer, heavily damaging the computer and all its contained data. This could be particularly onerous if the computer was the main server rack for an entire company computing network.

Or an insured landscaper could short out incoming power lines while planting or removing a tree, causing a power surge which shorts out the computer and/or fries the hard drives, resulting in the destruction of the data. Even with sufficient backup files for the data in place, the resultant downtime and expense to fully restore data usage could be extremely expensive.

Faculty Response #3. If the insured causes physical damage to another's property that results in the loss of another's electronic data, the endorsement will pay for the damage to the data. Under the law (a dangerous phrase for a non-lawyer like me), your insured is liable for the damaged property's value. That could be the cost to replace the data (information) or the court could set a value on the loss that is less than that amount.

If your insured is doing operations on the building and accidentally starts the building on fire or your insured's electrical appliance malfunctions and starts the building on fire, that would be physical damage that could result in the loss of electronic data.

Now you just need to find an insurer who is writing the endorsement.

Faculty Response #4. Maybe this excerpt from a seminar manual of mine will help.

ELECTRONIC DATA LIABILITY ENDORSEMENT CG 04 37

IT PROVIDES A MEANS FOR BUYING BACK LIABILITY COVERAGE FOR DAMAGE TO ELECTRONIC DATA. THE ENDORSEMENT ADDS A PROVISION SPECIFYING THAT "LOSS OF ELECTRONIC DATA" IS A CATEGORY OF "PROPERTY DAMAGE." SUCH LOSS MUST, HOWEVER, RESULT FROM "PHYSICAL INJURY TO TANGIBLE PROPERTY"

Presumably THERE MUST BE some direct damage to software media or the computer hardware itself.

The endorsement provides for a "loss of electronic data limit"—a sublimit of the occurrence limit—to be specified in the endorsement schedule.

ENDORSEMENT IS COMPANY RATED.

Examples of how the endorsement might work:

Example 1:

ABC SUITS Inc, a clothes maker which is insured by a Commercial CGL with CG 04 37 arranges for distribution of its clothing through DOBSON Shoppe, online catalog services. The DOBSON Shoppe Webmaster receives a link to a download site from ABC, Inc. He downloads the product and other information from ABC, Inc. and installs a link and ordering information at the DOBSON Shoppe site.

Immediately, the DOBSON site experiences problems and has to be shut down for a couple days. It is later discovered that a hacker had broke into ABC'S site and hid a virus. The virus was released after it was accessed by DOBSON. This loss would not be covered by the endorsement.

The loss was due directly to hostile coding, not a loss to tangible property.

Example 2:

LUTHER'S Luggers, a trucking firm, serves ABC SUITS. Inc., which now has its own computerized distribution center. LUTHER is insured by a Commercial CGL that is endorsed with CG 04 37.

One wintry day, a LUTHER fork lift unloading a LUTHER semi-trailer truck loses control during a delivery to ABC. The fork lift smashes through the distribution center's rear wall.

The employees are removed from that part of the building and the hole in the wall takes hours to get covered and sealed. In the meantime, the elements have free access to the center's computer dept.

Later, the servers and peripherals are unharmed, but the cold destroyed the electronic inventory records.

This loss would be covered since it arose from damage to physical property (the distribution center exterior wall).

Necessary Action: As always, discuss this coverage with your underwriter, since they may have their own proprietary endorsement or coverage form. Circulate this Technical Advisory to all appropriate Commercial Lines staff.

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