WILHELM
RECHTSANWÄLTE

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Versicherungspraxis, March 2017

Cyber-Insurance

Who pays for cyber damage?

Difficulties in the relation of cyber coverage with other insurance contracts

1. INTRODUCTION

The functionality and thus the value of insurance will be seen at the latest in the case of loss. In cyber policies, one aspect is more important than in case of "classic" insurance contracts: the question of when the cyber policy provides cover if there is other insurance coverage for the risk or the loss - the problem of multiple insurance. This article aims to identify potential conflicts for policyholders and to show solutions for the avoidance of coverage gaps and to prevent difficulties in the insured event.

2. THE PROBLEM OF MULTIPLE INSURANCE

The problem of multiple insurance exists if an interest is insured against the same risk with several insurers (cf. sec. 78 para. 1 Insurance Contract Act “VVG”). Which insurer will pay in the insured event to what extent? Is the policyholder able and forced to claim against one of the insurers with priority?

The policyholder is interested in avoiding multiple insurance. It is in its own interest to avoid double premiums due to multiple insurance. The policyholder’s primary target though is a comprehensive, reliable insurance coverage with a clear scope of application and without any coverage gaps. If the policyholder has to dispute in the insured event with the insurer (or the insurers) about the question which insurer is to perform, the insurance cover will soon be ineffective.

For the following reasons, the problem of multiple insurance is more virulent in cyber insurance than in other lines of business:

2.1 Cyber policies have more interfaces with other policies

Cyber policies have more interfaces with other policies than other insurance contracts with one another. Cyber policies cover certain liability risks and certain first party losses. For this reason there are possible overlaps not only with (other) liability insurance contracts, but also with own damage coverages, e.g. in case of financial loss after computer misuse, which might both fall under a professional indemnity insurance and cyber insurance.

There are also interfaces with property insurances. Cyber coverages offer insurance protection in case of hacker attacks. Hacker attacks affect the IT-infrastructure of the policyholder. If the policyholder holds IT-cover, certain (cyber) damages might also fall under IT-cover.

Other lines of business might be affected as well. An increasing cyber risk is the danger resulting from random software (thus the blocking of data/data processing systems by third parties and the consequential extortion to release of data).

Usual cyber policies (optionally) cover payments of the policyholder for the data release as insured first party damage. If the policyholder also holds a Kidnap & Ransom policy, there might as well be coverage under this policy.

2.2 No consistent coverage standards and clear distinction from other insurance contracts

In „traditional“ lines of business, coverage standards and standard terms have evolved (e.g. through usual definitions of insured events such as the – though disputed in terms of legal effectiveness – claims-made-principle in D&O-insurance) In general liability insurance there is a distinction of insurance contracts through “zero setting” for risks which might be insured via special coverage. For cyber risks there are currently no consistent coverage measures and no evolved distinction of cyber policies from other insurance contracts, because the cyber insurance market is still under development.

One and the same set of fact may typically results in insured events under cyber coverage and other insurance contracts.

3. PROVISIONS IN INSURANCE CONTRACTS – SPECIFICATION OR PRACTICALLY WORTHLESS?

A possibility to avoid multiple insurance is respective provisions in the insurance contract.

The VVG provides in sec. 78 that insurers shall be liable as joint and several debtors in case of multiple insurance. Insurance contract law allows the parties to the insurance contract within the limits of the law on terms and conditions to regulate the relation of several insurance contracts to one another deviating from sec. 78 VVG.

Just like other insurance contracts, cyber coverages regularly contain contractual provisions about the question of the relation of insurance cover to other cover. These contractual provisions might be very different from one another – with the consequence of far-reaching insurance cover or else a practical worthlessness of cover.

3.1 Potential conflicts subsidiarity clause

Cyber coverages partly contain – just like other insurance contracts – subsidiarity clauses. In case of multiple insurance, these clauses shall limit the liability of the insurer. The insurer wishes to create a priority between itself and other insurers of the same risk and intends to perform only with secondary ranking in the insured event. Subsidiarity clauses are phrased differently. Depending on the scope of the clause used, it is distinguished between so-called simple (limited) and qualified (unlimited) subsidiarity clauses.[1]

A cyber policy may for example contain the following (qualified) subsidiarity clause:

> *„Other insurances*
>
> *If a claim under this insurance contract is also insured under another insurance contract, the policyholder is obliged to assert the claim first under the other insurance contract. The performance obligation of the insurer under this insurance contract only applies if and insofar as the other insurer does not provide cover for the claim...“*

For the policyholder, such subsidiarity might mean the practical worthlessness of cover in case of cyber damage.

[1] Cf. about the functioning and effectiveness of subsidiarity clauses A. Meyer in VP June/2014, p. 108 et seqq.

According to our opinion, it is questionable under the view of general terms and conditions, whether the insurer may in the individual case rely on the qualified subsidiarity clause. For the policyholder, however, the following is decisive in case of a cyber incident:

The policyholder depends on a quick and effective claims handling. As soon as the policyholder detects a hacker attack, he immediately has to take measures to restore data and IT-systems and to mitigate a business interruption. If the policyholder loses millions of personal-related customer data sets due to a cyberattack, the policyholder has to inform authorities and affected parties straight away. The policyholder has to take immediate decisions on media information in order to avoid an eventually existence-threatening reputational damage.

The policyholder's possibilities to act are endangered if he has to fear that the cyber insurer will first relegate to another insurance contract. The problem is even more severe as cyber coverages usually provide for assistance services in case of a cyber incident. Insurers for example promise to provide experts (e.g. IT forensic experts or PR consultants) – exactly in order to have the policyholder, who does often not possess respective competences and capacities, act quickly in case of need.

All in all, subsidiarity clauses in cyber policies (as well as in other insurance contracts) mean severe uncertainty and the risk of decisive coverage gaps for the policyholder. The policyholder might eventually not get any cover, but can in any case not rely on the cyber insurer to settle immediately.

3.2 Specialty clauses as solution approach

Depending on the individual case, the policyholder will prefer clauses which clearly regulate the priority of cyber coverage before other insurance contracts.

A cyber policy may for example determine:

> *"If an insured event or damage is also insured under another insurance contract, this contract shall prevail as the more specialized one"*

The clause solves the problem of multiple insurance contrary to subsidiarity. The insurer clearly positions itself and declares its performance promise in favor of the policyholder as having priority over another insurance contract (priority of special coverage over general coverage). At contract conclusion and in case of loss, the policyholder knows where he stands and can rely on the cyber insurer as special insurer. The cyber insurer will calculate the premium referring to the clear priority of cyber coverage over all other insurance contracts, but hereby offers its customers a clear promise to perform.

3.3 Cyber exclusions increasing in other insurance contracts

If another insurance contract excludes cyber risks from coverage, the question of multiple insurance does not arise – the other insurance contract does simply not grant cover. When concluding insurance contracts or agreeing on new terms, policyholders have to take into account that insurers have reacted to the increasing development of cyber risks and cyber coverage. Classical insurance contracts more and more often explicitly exclude cyber risks resp. cyber damages – unlike in the past. Policyholders who have been able to assume that certain damages associated with cyber risks are insured under existing, classical insurance must therefore pay attention to further cyber exclusions when concluding new insurance contracts/terms.

4. CONCLUSION

Cyber insurances have more interfaces to other insurance contracts than "classical" insurance contracts among one another. In the insured event, the demarcation of insurance contracts is decisive for the policyholder as it decides about reliable damage settlement or in the most serious case about loss of cover.

Policyholders should make sure that cyber coverages do not contain any qualified subsidiarity clauses. Specialty clauses may provide for clarity to the policyholder’s benefit and ensure priority of the cyber policy.

A future-oriented possibility of effective cover concepts might be combined coverage. Combined coverage offers the possibility of avoiding demarcation difficulties and to offer the policyholders new, needs-oriented cover concepts. This applies in particular to combined elements of cyber insurance and fidelity insurance, E&O- and D&O-insurance, but also to cover loss of reputational damage. This requires the insurers' potential for innovation in order to provide answers to the legitimate reservations of policyholders.

In case of further questions, please do not hesitate to contact the author:

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