Year 2000 perils are not waiting for the new millennium to strike. With the new millennium fast approaching, year 2000 loss and liability are beginning to surface. As such, businesses of all kinds should begin thinking now about their insurance coverage for year 2000 losses and liabilities.

Whether it is referred to as the “Year 2000 Computer Crisis,” the “Year 2000 Glitch” or the “Millennium Bug,” the scenario is the same, a computer meltdown of sorts which could possibly cause severe system problems and outages. This potential problem could be a catastrophe. It is estimated that businesses worldwide eventually will spend between $300 billion and $600 billion, even up to $1 trillion, to remedy computer systems which will mistake the turn of this century with that of the previous century. Even if a business solves its own Year 2000 bugs, other companies may not have solved theirs. A company’s supplier, landlord, bank, joint venturer, retail distributor, or any other entity with which it transacts business could simply be unable to conduct business under normal circumstances, thus imposing a severe strain even upon those businesses which were successful in eradicating their own millennium bugs. As a result, some predict that the Year 2000 problem will spur as much as $1 trillion in litigation costs.

The Year 2000 Computer Crisis Is Upon Us Now

Indeed, it is not even necessary to wait for the Year 2000 in order to witness millennium bug litigation. In what is believed to be the very first Year 2000 case, a supermarket owner has commenced a lawsuit against a cash register supplier and maker for the cash registers’ alleged inability to process transactions for credit cards with expiration dates after 2000. The supermarket owner has asserted that his business has lost hundreds of thousands of dollars due to the credit card transactions causing the computerized tills to shut down.

In another Year 2000 lawsuit, a $50 million class action suit was recently filed in state court in California against an accounting software developer. The class action lawsuit alleges, among other things, that certain software packages developed and marketed by the defendant:

> are materially defective and will not function properly with regard to dates after December 31, 1999. Those [software] packages are afflicted with what has become known as the “Year 2000 Problem” or the “Millennium Bug.”

And in yet another Year 2000 case, Capellan v. Symantec Corp., a class action has been filed against a computer software developer and vendor. The class action alleges, among other things, that there are Year 2000 defects in the defendant’s Norton Antivirus software in versions sold prior to September 1997. The complaint alleges that versions of the software sold prior to September 1997 “will not be certified, or even tested, for Year 2000 compliance. Norton AntiVirus software prior to Version 4.0 is materially defective and will not function properly with regard to dates after December 31, 1999.”

Insurance Coverage Considerations

Any business that becomes the target of a Year 2000 lawsuit or suffers a loss related to the Year 2000 should look to their liability and property insurance policies for insurance coverage.

1. D&O Insurance Coverage

Directors and officers of companies may become the frequent targets of claimants alleging
that they have suffered losses caused by Year 2000 system problems. The two main claims that directors and officers may face stem from allegations: (1) that the company’s Year 2000 compliance program was mismanaged and thus failed to remedy the company’s computer operations before the new millennium; and (2) that the company failed to properly disclose the magnitude of the company’s Year 2000 problem. For either type of claim, directors, officers and their companies should immediately consider insurance coverage under their D&O liability insurance policies.

Under the insuring provisions of many D&O policies, insurance companies are obligated to provide insurance coverage to their policyholders by:

pay[ing] the Loss of each and every Director or Officer of the Company arising from a Claim first made against the Directors or Officers during the Policy Period . . . for any actual or alleged Wrongful Act in their respective capacities as Directors or Officers of the Company except when and to the extent that the Company has indemnified the Directors or Officers.

“Wrongful Act” is often defined as any breach of duty, neglect, error, misstatement, misleading statement, omission or act by the directors or officers. Many claims made against directors and officers arising out of their alleged failure to disclose the scope of the company’s Year 2000 exposure or to properly manage the conversion efforts of the company’s computer systems may be covered as “wrongful acts” under the company’s D&O liability policy.

2. E&O Insurance Coverage

Many businesses which provide computer services will have to look to their professional malpractice insurance (often known as E&O liability insurance) to cover losses and liabilities stemming from the Year 2000 glitch.

Under the insuring provision of a typical E&O liability policy, the insurance company is obligated to:

pay on behalf of the insured those sums which the insured becomes legally obligated to pay as damages because of a negligent act, error or omission in the performance of the insured’s professional services.

Some insurance companies try to reduce the scope of insurance coverage under the above provision, by arguing that “negligent” modifies not only “act,” but “error or omission” as well. Courts have reached differing conclusions on this issue, but several have found that there is insurance coverage for non-negligent errors, and, therefore, an insurance company cannot deny insurance coverage by arguing that “negligent” modifies “error and omission” as well as “act.” As a result, policyholders may have significant E&O coverage for Year 2000 related E&O type claims absent some specific Year 2000 exclusion.

3. CGL Insurance Coverage

Commercial and comprehensive general liability (“CGL”) insurance policies typically provide insurance coverage for property damage, bodily injury, personal injury and advertising injury claims. For decades, CGL insurance policies have been marketed and sold to policyholders as providing broad protection against liabilities.

Recognizing that there is potentially significant insurance coverage under the CGL insurance policy for Year 2000 related claims, the Insurance Services Office, Inc. (“ISO”) a prominent insurance industry trade group, has crafted several insurance policy exclusions for insurance companies to use to exclude insurance coverage for Year 2000 claims under CGL insurance policies. ISO, in its “Filing Abstract,” recognizes that there are no CGL exclusions which particularly exclude insurance coverage for Year 2000 claims. Specifically, ISO states that “there is presently no explicit treatment of the Y2K exposure within the CGL.”

ISO further states that those insurance agents wishing to sell the broadest CGL insurance coverage to policyholders for Year 2000 related claims should sell an “unendorsed standard CGL or Products Liability form.” In other words, the broadest CGL insurance coverage for Year 2000 related claims is available under the currently existing CGL insurance policy.

4. Other Insurance Coverage

Policyholders should also remember that they may have insurance coverage for Year 2000 loss or liability under a host of different insurance policies that they may possess, such as business interruption insurance (especially business interruption policies written on an “all risk” basis), inland marine policies, business owners policies and other property and liability policies.
Conclusion

Businesses of almost every kind should be aware that there is a potential for severe interruptions in commerce due to the Year 2000 glitch. Whether there is a resulting litigation barrage remains to be seen. Nevertheless, one thing which policyholders can do when liabilities or losses arise, is to immediately consider any possible avenue of insurance coverage to address their claims.

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