

Intentional Acts Exclusion Precludes Coverage

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A Minnesota intermediate appellate court, applying Texas law, has held that the intentional acts exclusion in a technology E&O policy issued to a computer manufacturer precluded coverage for two class action lawsuits alleging that the manufacturer intentionally sold computers that it knew were defective. *Compaq Computer Corp. v. St. Paul Fire & Marine Ins. Co.*, 2003 WL 22039551 (Minn. Ct. App. Sept. 2, 2003).

The coverage action arose after two class action lawsuits were filed against the policyholder computer manufacturer, alleging that the manufacturer intentionally and knowingly designed and sold computers that contained defective hardware and codes, causing the loss of use, corruption and destruction of data. The insurer provided coverage to the manufacturer under a package policy that contained technology E&O, general liability and umbrella excess liability insuring agreements. The technology E&O insuring agreement provided coverage for loss resulting from "error," which the agreement defined as "any error, omission, or negligent act." The policy excluded coverage for criminal, dishonest, fraudulent or other "intentionally wrongful act[s]." After the insurer disclaimed coverage, litigation ensued.

The court first concluded that Texas law applied because "[t]he primary contacts in this controversy are centered in the state of Texas": the package policy was issued in Texas, the insurer was licensed in Texas and the policyholder's principal place of business was in Texas. Next, the court held that the intentional acts exclusion in the E&O insuring agreement precluded coverage under that agreement for the two class action lawsuits. The court reasoned that "the overwhelming majority of the factual allegations" in one complaint "allege[d] intentional and knowing conduct," and the other complaint "repeatedly referred to [the manufacturer's] knowing conduct." Consequently, even though a paragraph in one of the complaints alleged that the policyholder "should have been aware" of the problems in question, these "few isolated sentences...are insufficient to create a duty to defend."

The court further concluded that the complainants' allegations that the policyholder violated the Computer Fraud and Abuse Act were not covered under the E&O policy because that is a criminal statute and the exclusion precluded coverage for criminal acts. The court also explained that, even if the underlying claimants could have alleged a violation of the same statute without alleging intentional action, the complaint's actual allegations—not what the claimants could have alleged—controlled the analysis. Since the complaints alleged intentional conduct, the E&O agreement's intentional acts exclusion precluded coverage.

Finally, the court held that the policy did not afford coverage for allegations that the policyholder had failed to take adequate steps to prevent the problems. Distinguishing cases cited by the manufacturer to demonstrate that such a failure constituted negligent, rather than intentional, conduct, the court ruled that regardless of what plaintiffs could have alleged, they had alleged that the actions and resulting damages were intentional.

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