

Exclusion for Claims "Arising out of" Misappropriation of Trade Secrets Interpreted Broadly

January 2009

The Massachusetts Supreme Judicial Court has held that an exclusion for claims "arising out of" the misappropriation of trade secrets should be read "expansively" to exclude coverage for a claim based on a third party's conduct. *Finn v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 2008 WL 5050170 (Mass. Dec. 2, 2008).

An insurer issued an errors and omissions policy to a company that provided litigation support, such as records and document management, to a law firm. As a part of the litigation support, the insured company's employees worked at the law firm's office. The employees signed confidentiality agreements and agreed not to remove documents from the office. The company authorized an employee to bring a family member to help with the work in order to meet certain deadlines. The family member discovered documents containing a client's confidential trade secrets and sent that information to a public website. The law firm wrote off substantial legal fees for that client because of the disclosure of the trade secrets and demanded reimbursement from the company. The company agreed to settle the matter for \$1,175,000.

The company tendered the law firm's demand to its errors and omissions insurer. The insurer denied coverage on the basis of an intellectual property exclusion that precluded coverage for "any claim arising out of any misappropriation of trade secret or infringement of patent, copyright, trademark, trade dress or any other intellectual property right."

In the coverage litigation that followed, the company argued that the exclusion was ambiguous because it was "silent as to whether it applies to third-party conduct" The court disagreed. Reviewing other cases interpreting exclusions that applied to third-party conduct, the court concluded that the exclusion at issue here did as well. In this connection, the court pointed out that, under Massachusetts law, the phrase "arising out of" incorporates "a greater range of causation than that encompassed by proximate cause under tort law" and "the breadth of the phrase . . . in conjunction with the words 'any claim,' unambiguously encompasses claims based on third-party conduct." Based on this determination that the exclusion was unambiguous, the court also declined to consider the insured's reasonable expectations.

In addition, the court rejected the insured's argument in favor of coverage that there was no causal connection between the excluded conduct and the law firm's injury—that is, forgone legal fees. Noting that the record was devoid of any evidence that the law firm "would have incurred any loss in the absence of the [family member's] misappropriation" of trade secrets, the court concluded that the injury suffered arose out of such misappropriation.