

Pennsylvania Law Permits Misrepresentation Claim Based on E&O Insured's 'Reasonable Expectations'

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In an unpublished decision, a federal district court, applying Pennsylvania law, has denied an E&O insurer's motion to dismiss an insured's claims of negligent and intentional misrepresentation, holding that Pennsylvania law permits an insured to state a cause of action based on the insured's "reasonable expectations" if the insurer's agent made fraudulent or negligent misrepresentations concerning coverage. *Frontier, Inc. v. Gulf Underwriters Ins. Co.*, 2005 WL 1353614 (E.D. Pa. June 3, 2005).

The insurer issued an E&O policy to an Internet advertising company. The policy provided coverage for "claim expense" and damages arising out of claims of, *inter alia*, "infringement of copyright, plagiarism or misappropriation of ideas under implied contract; . . . misuse of intellectual property right in Content;" and "errors, omissions, and negligent acts committed by the Insured . . . in performing Cyberspace Activities . . . including obtaining, processing, uttering, or disseminating Content." The policy excluded coverage for "any act, error or omission intentionally committed while knowing it was wrongful" or "an act, error or omission that a jury finds dishonest, fraudulent, criminal or malicious."

A competitor sued the company and an employee who left the competitor to work for the company. The competitor alleged that the employee wrongfully downloaded the competitor's business manual onto the company's computer system. The competitor's complaint contained nine tort and statutory causes of action, each of which alleged intentional conduct. At trial, the jury found for the company on all claims against it, but found the employee liable for violating the Digital Millennium Copyright Act and awarded damages. The insurer denied coverage for the competitor's claims, asserting that the claim did not arise out of covered "Cyberspace Activities." The company brought the instant coverage action, alleging breach of contract, breach of the common law duty of good faith, intentional misrepresentation and negligent misrepresentation.

The court granted the insurer's motion to dismiss the breach of contract and breach of the duty of good faith claims. Noting that intentional wrongful conduct was alleged and was a necessary element of each of the competitor's tort claims, the court concluded that the policy exclusions barred coverage for those claims.

The court refused, however, to dismiss the company's intentional and negligent misrepresentation claims. The company alleged that the insurer's agent made false and material misrepresentations, leading the company reasonably to expect that the insurer would provide coverage for claims relating to the company's advertising activities not covered by other insurers. Relying on *Tran v. Metropolitan Life Insurance Co.*, 2005 WL 1229696 (3d Cir. May 25, 2005), the court concluded that, "under certain circumstances," Pennsylvania law recognizes a cause of action based on an insured's "reasonable expectations" if the insurer's agent made fraudulent or negligent misrepresentations regarding coverage. The court declined to dismiss the company's misrepresentation claims at the pleading stage, noting that whether recovery is available on such a theory "is at the very least a fact-intensive inquiry."

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