

CYBER LIABILITY

Zurich 'War Exclusion' Lawsuit Remains in Limbo as Judge Rules in Similar Case

By Tom Davis

OLDWICK, N.J. //BestWire// - A possible precedent-setting \$100 million lawsuit over Zurich American's use of the rarely applied war exclusion to deny coverage remains in legal limbo, court documents show — even as a judge ruled in early January against an insurer in a similar case.



Attorneys for Mondelez and Zurich American, which was sued over its denying the snack manufacturer coverage when Mondelez's computer systems were corrupted by the 2017 NotPetya cyberattack, are waiting for the judge to schedule oral arguments in the four-year-old Illinois case.

The case remains at a standstill just as a New Jersey Superior Court has ruled in favor of pharmaceuticals company Merck Inc. and its captive insurer in a summary judgment against a Chubb Ltd. affiliate and other defendants related to the NotPetya attack (*BestWire*, Jan. 17, 2022).

Merck's computer systems were also infected by the NotPetya malware, which struck computers worldwide, with the plaintiff alleging 40,000 computers were affected, resulting in more than \$1.4 billion in losses. The defendant insurers had cited language in its policy excluding hostile and warlike acts as a reason to exclude the cyberattack.

Judge Thomas J. Walsh in the Superior Court of New Jersey Law Division, Union County, wrote the insurers "did nothing to change the language of the exemption to put this insured on notice that it intended to exclude cyberattacks."

Michael Menapace, an insurance lawyer and cybersecurity counsel, said he believes the Chubb affiliate will "undoubtedly" appeal. As for its impact on the Zurich-Mondelez case, Menapace said the trial court proceeding in the Merck case may be persuasive to the Illinois judge, "but not binding."

"In my estimation, the New Jersey decision reads as though it is outcome-oriented and I am not sure how persuasive its rationale will be on an Illinois court," he said.

Much like the New Jersey case, the outcome of the Mondelez lawsuit could hinge on the interpretation of policy language.

Fred Eslami, associate director at AM Best, said since NotPetya, insurers have been tightening their policy languages, terms and conditions and the limits that they provide. Prior to the New Jersey court ruling, "the big unknown was whether or not an act of cyber sabotage similar to NotPetya met the criteria for being a hostile or warlike action," he said.

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“War exclusions are generally written in broad terms and are not well equipped to handle today’s constantly evolving cyberrisk landscape,” he said. “The outcome of this case highlights the importance of insurers to continue to add greater clarity of what is and isn’t covered within their policies.”

Both Zurich and Mondelez have recently asked for summary judgment, saying the material facts they’ve presented can’t be disputed and the case doesn’t need a full trial.

In its filing, Zurich maintains NotPetya was a “hostile or warlike action” within the terms of its hostile actions exclusion. The policy includes “broad and unambiguous” language signaling the NotPetya cyberattack was an act of war by a “government or sovereign power” or military — in this case, Russia, Zurich says.

“Courts addressing the hostile acts exclusion make clear that the exclusion — consistent with its plain terms — is applicable even to acts that are neither ‘acts of war’ nor traditional armed conflict,” Zurich wrote in its court filing.

Alan Rutkin, a partner in the law firm Rivkin Radler LLP who has written on the growing impact of cybercrimes on insurance, said he expects use of the exclusion will become more frequent in the near future as ransomware attacks continue to escalate.

“The use of cyberattacks has, in recent years, become part of conflicts between nations. The 2015 hack of Sony Pictures was caused by North Korea,” he said. “In January, as Russia was threatening Ukraine, Russia hacked Ukraine sites.”

“When hacking is part of war-time activity, like in these two instances, its consequences may well be barred by war risk exclusions,” he said.

Menapace said the creation and reliance of the concept of “traditional form of warfare” is not found in the text of such policies. The war exclusion was developed long ago, he said, and “certainly, damages from cannon fire or other forms of warfare no longer in use were excluded when it was drafted.”

“I can’t imagine anyone would argue that the insurers should have updated the exclusion to account for the modern missile. Why is it such a leap that a cyberattack causes warlike collateral damage to insured computers?” he said.

Mondelez, however, argues Zurich has provided no technical or forensic evidence regarding who was responsible for NotPetya. “There is no publicly available forensic evidence linking NotPetya to Russia,” the company said in recent court filings.

It also can be disputed, Mondelez said, that Russia and the Ukraine were actively at war around the time of NotPetya. “Even if Russia and the Ukraine were in an armed conflict at the time of NotPetya, over which the parties have a genuine dispute, Zurich has not met its burden to prove NotPetya was part of that purported armed conflict,” the company claims.

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In its summary judgment request, Mondelez argues hostile or warlike action must be suggestive of armed physical conflict that can cause physical violence to people or property. "Computer code that is incapable of causing, and indeed does not cause, any human casualties or physical destruction, and that non-violently self-propagates while encrypting private civilian computer devices around the world, plainly does not constitute a 'hostile or war-like action,'" the company said in court records.

The Mondelez lawsuit was filed after the NotPetya malware, in June 2017, rendered dysfunctional 1,700 of Mondelez's servers and 24,000 of its laptops. It also disrupted distribution, leaving customer orders unfulfilled, the company says.

Mondelez filed an insurance claim for damages incurred. It sought coverage under its property policy, not a cyber policy. Subsequently, in a letter dated June 1, 2018, its property insurer, Zurich American Insurance Co., denied the claim, citing the policy's war exclusion as its reason.

At the time, the decision was unprecedented. The war exclusion, also known as the hostile acts exclusion, historically has applied to conventional armed conflicts. Never before had it been invoked for a cyberattack.

In the original complaint filed on Oct. 10, 2018, Mondelez called the coverage denial "wrongful and improper" and argued the incursions of malicious code "did not constitute 'hostile or warlike action.'"

According to court documents, Mondelez purchased an all-risks property policy from Zurich for coverage beginning Nov. 1, 2016. The policy included coverage for "physical loss or damage to electronic data, programs, or software, including physical loss or damage caused by the malicious introduction of a machine code or instruction."

In the New Jersey court case, Merck and its captive insurer International Indemnity had bought \$1.75 billion in property insurance to protect against this type of loss, the ruling said, adding Merck's all-risks policies provide coverage for loss or damage resulting from destruction or corruption of computer data and software.

Merck also argued the NotPetya attack was not a state action but a form of ransomware, and even if it was instigated by Russia, the war exclusion would not apply, the ruling said.

Most underwriting entities of Chubb Ltd. have current Best's Financial Strength Ratings of A++ (Superior). Underwriting entities of Zurich Insurance Group Ltd have current Best's Financial Strength Ratings of A+ (Superior) and A (Excellent).

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