

Client Alert

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New York Court Says E&O Insurer Must Cover Claims for Statutory Damages Despite Exclusion for Fines, Penalties, Forfeitures and Sanctions

On July 28, 2015, the New York Supreme Court in *Navigators Insurance Company v. Sterling Infosystems, Inc.*, Index No. 653024/2013, (N.Y. Sup. Ct. July 28, 2015), held that Navigators Insurance Company must defend and indemnify its policyholder for claims seeking statutory damages under the Fair Credit Reporting Act (FCRA), 15 U.S.C. § 1681 *et seq.*, despite a policy exclusion for claims involving “[f]ines, penalties, forfeitures or sanctions.” The decision may have broad implications for policyholders pursuing coverage for the defense of lawsuits seeking statutory damages under privacy and consumer credit statutes, as well as other statutes that have traditionally been viewed to be punitive in nature.

Background

In *Sterling Infosystems*, Scott Ernst, a satellite dish technician, alleged that Sterling Infosystems, Inc. (“Sterling”) violated the FCRA by providing Ernst’s employer with outdated information that the employer relied upon in its decision to terminate Ernst’s employment. Ernst alleged that Sterling further violated the FCRA by failing to provide Ernst with the sources of that outdated information. Ernst initiated a putative class action seeking statutory damages “of not less than \$100 and not more than \$1,000” per violation, available under the FCRA for willful violations of the statute.

Sterling tendered the Ernst lawsuit to Navigators Insurance Company (“Navigators”) under an errors and omissions insurance policy, requesting a defense and indemnity. The policy provided coverage for suits seeking “damages,” which the policy defined as “any compensatory sum” including “a judgement [sic], award, or settlement, provided any settlement is negotiated with the Company’s written consent.” Notably, the policy excluded coverage for “[f]ines, penalties, forfeitures or sanctions.”

Navigators initiated a declaratory judgment action, seeking a declaration that it owed no defense or indemnity to Sterling because the FCRA’s statutory damages constitute a “penalty” for which coverage is expressly excluded. Sterling argued that FCRA’s statutory damages are compensatory in nature, not penal, and are therefore covered under the policy.

Holdings

The court awarded summary judgment in favor of Sterling, holding that statutory damages for willful violations of the FCRA are compensatory in nature in light of FCRA’s overall statutory scheme, and that the damages are therefore covered under the policy. The court reasoned that the statutory damages “of not less than \$100 and not more than \$1,000” were more akin to actual damages, and not punitive damages, because the FCRA separately authorized punitive damages under a different provision of the statute. Therefore, because actual damages are considered compensatory, statutory damages that substitute for actual damages should also be considered compensatory. Additionally, the court emphasized that statutory damages under the FCRA, like other privacy and consumer protection statutes, are intended to facilitate compensation in instances where actual damages are difficult or impossible to

calculate. Thus, the court concluded that Navigators was obligated to defend and indemnify Sterling against Ernst's FCRA claims.

Implications

Sterling Infosystems stands as the latest among a recent line of cases affording coverage for amounts paid as statutory damages. The decision may have broad coverage implications for claims brought under privacy and consumer protection statutes that provide for both statutory damages and punitive damages, as the former may be viewed as "compensatory" in light of the latter. Moreover, the court's reasoning demonstrates that policyholders may still have protection against the often daunting costs of defending and settling class actions seeking punitive as well as other types of statutory damages.

Hunton & Williams LLP's insurance recovery lawyers assist policyholders secure the full benefits to which they are entitled in the event of any type of loss, including amounts spent to defend or settle large-scale litigation. For more information, please contact the members of the firm's Insurance Coverage Counseling and Litigation team.

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