Do Insurers Have a Duty to Defend as a Result of a Failure to Comply with PCI — DSS

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On April 4, 2016, the Québec Court of Appeal issued its decision in *Aldo Group Inc. c. Chubb Insurance Company of Canada* 2016 QCCA 554 which addressed the question of whether Chubb had a duty to defend and indemnify Aldo in respect of penalties assessed against it for its breaches of PCI DSS.

Background: What is PCI DSS?

The Payment Card Industry Data Security Standards (PCI DSS) are a contractual standard for protection of data about payment cards issued by major card brands including Visa, MasterCard and American Express. Most organizations that accept credit card payments, including the Aldo Group Inc. ("Aldo"), a Canadian footwear retailer, are contractually required to comply with these standards.

Aldo entered into an agreement with Moneris for the processing of electronic payments made by cards issued by BMO/MasterCard. As part of its agreement with Moneris, Aldo was required to comply with PCI DSS. A failure to do so could result in the imposition of fines, fees, and assessments. Under this agreement, Aldo also agreed to indemnify Moneris for any fines, fees, or assessments imposed on it by the card issuer which was BMO/MasterCard.

In 2008 Aldo was the victim of a cyber-attack which risked exposing information associated with transactions made by BMO MasterCard users. Following an investigation, MasterCard found that Aldo had failed to comply with PCI DSS and assessed penalties in the amount of $4.9 million which were debited from Aldo's account by Moneris. The penalties were contractual penalties and not compensation for damages suffered by cardholders themselves due to fraudulent use of their card or identity theft.

Aldo's action against Chubb

As outlined in our January 2016 bulletin, "An Introduction to PCI DSS", Aldo sued Moneris and MasterCard in Ontario for breach of contract due to the assessment of the penalties. This action was later discontinued, presumably as part of a settlement.

Aldo then looked to its insurer, Chubb Insurance Company of Canada ("Chubb"), for reimbursement of the legal fees it incurred in pursuing the Ontario action against Moneris and MasterCard. Chubb refused coverage on the basis that Aldo was not entitled to coverage under the wording of the insurance policy.

Aldo commenced an action against Chubb in Québec where the policy had been issued and brought a motion for a declaratory judgment for coverage based on the wording of the insurance policy. The motion was dismissed and Aldo appealed to the Court of Appeal.

Decision of the Court of Appeal

The Court of Appeal upheld the Superior Court's decision. In doing so, however, it was careful to state that its decision was limited to its particular facts of this case and limited evidence before it. Notwithstanding this caveat, the Court's review is instructive.

The first issue before the Court of Appeal addressed was whether Chubb had a duty to defend Aldo, notwithstanding the fact that Aldo was the Plaintiff in the action against Moneris and MasterCard. The Court found that the loss suffered by Aldo was an "Entity Claim", as defined in the Policy, as Moneris had made a "written demand for monetary damages".

On this basis, the Court of Appeal agreed with the Superior Court's conclusion that Chubb had a duty to defend. The Court, however, underlined that this particular finding should not be seen as precedent setting. Having determined that Chubb had a duty to defend, it was required to consider the exclusions for coverage of Entity Claims under the policy.

In particular, the Court reviewed the following exclusion found at Clause 6-13.2(b):

6. The following is added to the Policy as subsections 13.1 and 13.2, respectively, *Exclusions Applicable to Insuring Clause 5 Entity Liability Coverage & Security Holder Derivative Demand Coverage*, and 13.2, *Exclusions Applicable to Insuring Clause 5 Entity Liability Coverage & Security Holder Derivative Demand Coverage*:

[…]

13.2 The Company shall not be liable under Insuring Clause 5 for Loss on account of any Entity Claim:

[…]

(b) based upon, arising from or in consequence of any actual or alleged liability assumed under or as a result of any oral or written contract or agreement with the Insured Organization. Provided, however, that this exclusion shall not apply to Loss for which the Insured Organization would be liable in the absence of such a contract or agreement.

Aldo and Chubb were in agreement that the obligations under PCI DSS were liabilities assumed under a contract. Aldo, however, argued that because it could also be liable in

negligence, in particular to MasterCard/BMO cardholders due to a failure to comply with PCI DSS, Chubb was required to provide coverage.

The Court of Appeal rejected this argument. It examined the specific nature of the fines imposed by MasterCard and determined that they were pure contractual penalties and unrelated to any damages which may have been suffered by cardholders. The Court also examined the contract between Aldo and Moneris and found that it was only as a result of an indemnity in that agreement, that Aldo was liable to MasterCard. As such, the Court of Appeal concluded that the only basis upon which Aldo had suffered a loss was due to the contract and rejected Aldo's appeal.

Comment

The application of the Court of Appeal's decision is likely limited to the particular circumstances under which the penalties were imposed on Aldo. The result, however, may have been different if the penalties had been imposed due to damages suffered by card holders. The lesson from this case is that businesses which are subject to monetary penalties due to non-compliance with PCI DSS should consider working with their insurers to determine whether there is coverage for a finding of non-compliance.

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