

Cyber-Fraud

Computer Fraud and
Funds Transfer Fraud Coverages under
Fidelity and Commercial Crime Policies

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Overview

- **Computer Fraud Coverage**
 1. "Use" of a Computer
 2. Whose Computer?
 3. What is a "Direct" Loss?
- **Funds Transfer Fraud Coverage**
 1. Fraudulent instructions
 2. Unauthorized access
- **Key Exclusions**

Computer Fraud Coverage

- Various Forms of the Coverage
- Typical requirements:
 1. the **use** of Insured's (or a) **Computer**, to
 2. cause a **transfer** of Money, Securities or Other Property, from
 3. inside the Insured's **Premises** or the Insured's Financial Institution's Premises

Use of a Computer

- U.S. authority: generally, “use” must be unauthorized access or a “hacking” incident: *Pestmaster* (2014)
- Authorized use of system to commit a fraud based on **existing** fraudulent instructions or data may not be enough: *Universal American* (2013)

Whose Computer?

- Insuring Agreement will specify either “**Insured’s**” computer, “**a**” computer or “**any**” computer
- Can make a difference where there is a chain of computers, *e.g.* insured’s **vendor’s** computer has authorized access to insured’s payment system

“Direct” Loss

- Part of a bigger debate in fidelity insurance
- Most U.S. courts reject proximate causation; support for this in Canadian law as well
- Where too many intervening parties/acts, “direct” causation may not be established, *e.g.* *Methodist Health System Foundation* (2011)

“Premises” Requirement

- “Bright-line” test for coverage (so far)
- Courts have rejected insureds’ efforts to expand “premises”: *e.g.* **Brightpoint** (2006)
- Future issues:
 1. **Cloud Computing**

2. **Bitcoin**



Funds Transfer Fraud

- Various wordings
- Typical requirements:
 1. an **instruction** to a Financial Institution
 2. directing the Financial Institution to **transfer** funds
 3. without the insured's **consent or knowledge**
- Other specialty coverages, *e.g.* Fraudulent Voice Transfer Instructions

Fraudulent Instructions

- Instructions must themselves be fraudulent
- Unwitting, but authorized, instruction by Insured typically insufficient: *Northside Bank* (2002)
- Issue: application in “phoney collection” scam

Unauthorized Access

- Courts limit Funds Transfer Fraud coverage to “impostor” coverage
- Fraudulent misuse of authorized access may be insufficient: *Morgan Stanley Dean Witter* (2005)

Other Transfer Coverages

- Extremely technical coverages under both Commercial Crime and F.I. Bonds
- Example: **Fraudulent Voice Transfer Instructions**
 - may have specific requirements for contractual relationship between bank and customer; if not met, no coverage

First National Bank (9th Cir., May 13, 2015)

Key Exclusions

- Theft of Confidential Information
- Exchange or Purchase
- Accounting Errors

Thank you!

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Called to the Bar of
Ontario, 2003

LL.B., University of
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Member, Law Society of
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Member, The Advocates'
Society

Member, Metropolitan
Toronto Lawyers
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Member, Canadian
Defence Lawyers

Member, American Bar
Association – Fidelity &
Surety Law Committee

Chris McKibbin, a partner in the firm's Insurance Litigation Group, has a broad-based insurance practice that is anchored by his extensive experience in fidelity insurance law. His insurance expertise also includes fraud recovery, commercial general liability (CGL) coverage and defence work, subrogation and directors' and officers' (D&O) liability insurance. Chris joined Blaney McMurtry in 2014 after practicing for 11 years with an insurance litigation boutique.

Chris' fidelity practice encompasses all aspects of coverage analysis and litigation, involving fidelity bonds, commercial crime policies and financial institution bonds. Chris was associate counsel before the Court of Appeal in an appeal arising from the largest fidelity insurance claim ever litigated in Canada, as well as in another Court of Appeal case, which made several significant holdings regarding the interpretation of fidelity bonds. Chris is frequently invited to speak on fidelity insurance law and fraud recovery and also writes on these topics, including postings on [Blaneys Fidelity Blog](#) and articles for *Canadian Insurance* magazine, the *National Banking Law Review* and the American Bar Association's *Fidelity & Surety Law Committee Newsletter*.

Chris' fraud recovery practice includes serving as lead counsel in obtaining *Mareva* and other injunctive relief against former employees in connection with theft of money and of confidential business information. He also secures *Normich* orders to successfully trace defalcated funds. Chris obtains significant recoveries in claims against alleged fraudulent employees, co-conspirators, auditors and financial institutions, including claims on cheque fraud losses pursuant to the *Bills of Exchange Act*.

Chris acts for subrogating insurers in pursuing construction defect claims, products recall liability claims and other subrogated claims. He also has experience in CGL coverage analysis and duty-to-defend applications, as well as the defence of insureds under liability policies. Chris provides coverage advice to D&O insurers and serves as defence counsel under D&O policies. He served as counsel for a D&O insurer in resisting an application for court approval of a settlement arising out of the Hollinger International-Conrad Black dispute.

Chris graduated from the University of Toronto Faculty of Law, winning several academic awards and earning Dean's Honour List standing in his final year. At the time of his call to the Bar, he received the Osgoode Society Award as one of the top 25 Bar Admission Course students in Ontario. Prior to law school, Chris attended the University of Manitoba, where he earned the Gold Medal for highest standing in his program and was a finalist for the Rhodes Scholarship.

SIGNIFICANT DECISIONS:

Iroquois Falls Community Credit Union Ltd. v. Co-operators General Insurance Co. (2009), 73 C.C.L.I. (4th) 157 (Ont. C.A.)

Co-counsel for the successful appellant fidelity insurers in a major appeal resulting from the collapse of a credit union. The Court of Appeal made significant holdings with respect to the manifest intent and direct loss requirements for coverage; the termination condition; and the unfaithful performance exclusion.

Royal Bank of Canada v. Société Générale (2006), 31 B.L.R. (4th) 63 (Ont. C.A.), leave to appeal ref'd (2007), 377 N.R. 400n (S.C.C.)



Co-counsel for two of the successful appellant fidelity insurers in an appeal arising from the largest fidelity insurance claim ever litigated in Canada, which also involved significant issues of loss allocation as between banks under the *Bills of Exchange Act* and the Canadian Payment Association's Automated Clearing Settlement System Rules and Standards. The Court of Appeal's decision provided important guidance with respect to summary judgment practice and procedure in Ontario.

Aviva Insurance Company of Canada v. Regional Hose Toronto Ltd. (2010), 82 C.C.L.I. (4th) 283 (Ont. S.C.J.)

Successfully obtained a declaration of no duty to defend under a CGL policy, relying on jurisprudence establishing that defective manufacture does not constitute an "occurrence" within the meaning of CGL coverage. Also successfully obtained two procedural rulings, both of assistance to insurers. First, the Court struck out an affidavit from the insured's principal purporting to explain the "true facts" relating to the underlying dispute, on the basis that it was not proper evidence on a duty-to-defend application. Second, the Court rejected the insured's attempt to rely on its statement of defence in the underlying action to "clarify" the allegations in the statement of claim.