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INSURANCE ERA: RISK, GOVERNANCE, AND THE PRIVATIZATION OF SECURITY IN POSTWAR AMERICA: AN ESSAY REVIEW

KATHERINE HEMPSTEAD

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I. INTRODUCTION

We live in a world structured by insurance, one in which the parameters of our social and economic security are largely determined by what risks we choose to (or can afford to) cover, and under what terms. This is discussed in *Uncovered: The Story of Insurance in America*, my book on the "history of the insurance business and its relationship with government from the late nineteenth through the end of the twentieth century."[1]

> Perched precariously at the intersection of public and private life, insurance has long drawn the attention of scholars. Theoretical work has illuminated the criticality of insurance to social organization. Far more than a business, insurance is more broadly a system of risk management and governance that can be deployed by public or private actors. The choices a society makes about how to share risk among its members reflect its deepest values about fairness, equality, and what it means to belong, or to use the words of [the early twentieth century] British civil servant Llewellyn Smith, where it has drawn the line between "free adventure and economic security."[2]

Given the quasi-public role of insurance, the insurance industry has cultivated a notably *governmental* persona, in terms of its self-perception and behavior.[3] But at the same time, given the ever-present threat of the state provision of insurance, insurers' stance toward government itself has—until recently—been largely oppositional.[4]

In *Insurance Era: Risk, Governance, and the Privatization of Security in Postwar America*, Massachusetts Institute of Technology historian Caley Horan describes some of the manifestations of these tendencies in the mid-twentieth century, illustrating insurers' efforts to counteract the growing role of government and also revealing the role the industry played in shaping social inequality and discouraging a more collective approach to sharing risk.

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1. KATHERINE HEMPSTEAD, UNCOVERED: THE STORY OF INSURANCE IN AMERICA, at x (2024).

2. *Id.* at ix (quoting Llewellyn Smith, *Economic Security and Unemployment Insurance*, 20 ECON. J. 513, 519 (1910).

3. *See generally id.* at ix–xvi (describing insurers as quasi-public and summarizing some of the industry's more governmental behaviors).

4. CALEY HORAN, INSURANCE ERA: RISK, GOVERNANCE, AND THE PRIVATIZATION OF SECURITY IN POST-WAR AMERICA 2–3 (2021).

Insurers viewed the government as a competitor and feared replacement by publicly provided social insurance.[5] In response, the industry sought to persuade Americans that their security can and should be provided by the private sector.[6] Yet, while resisting a larger role for government, the industry was, at the same time, quite governmental itself in terms of both behaviors and impact. Horan shows how, through massive investments in urban and suburban residential and commercial real estate, the insurance industry shaped the development of public and private spaces in ways that increased racial segregation and economic inequality.[7] Additionally, *Insurance Era* illustrates how the insurance industry has influenced societal norms about what is fair. By successfully defending gender-based discrimination in the 1970s on the grounds of actuarial fairness, insurers encouraged the rejection of a more egalitarian basis for risk-sharing.[8]This review essay situates Horan's *Insurance Era*, which begins in the post-World-War II period, in the larger historical context provided by *Uncovered*'s analysis of the American insurance industry in the nineteenth century and early twentieth century.

II. THE QUASI-PUBLIC ASPECTS OF INSURANCE

Horan provides ample evidence of governmental behavior of the insurance industry. For example, the Institute for Life Insurance (ILI), an association of life insurers, executed an ambitious mid-century publicity campaign promoting a vision of privatized security in which expanded government services were not needed.[9] The project of the ILI was an unabashedly propagandic attempt to change mindsets about the proper role of government in society.[10] The insurers employed the services of academic experts such as psychologists and sociologists to help make their efforts more persuasive.[11] By today's standards, the effort is unsophisticated and heavy-handed, with the irony of assuming a posture of state-like authority to argue for a smaller state

5. *Id.* at 7.

6. *Id.* at 40.

7. *See id.* at 139–67 ("'Communities Without Hope': Urban Crisis and Insurance Redlining.").

8. *See id.* at 167–189 ("The Unisex Insurance Debate and the Triumph of Actuarial Fairness.").

9. *Id.* at 17, 33–41, 46, 58, 69.

10. *E.g.*, *id.* at 58 ("Even faith was portrayed as a pursuit that required calculated planning and a willingness to manage the future's risks. 'I Pray the Lord My Soul to Keep,' an ILI ad that ran nationally . . . urged readers to seek out faith as a 'bedrock of family unity' and instructed readers that 'to keep alive the family's faith calls for a positive plain—just as you plan for your family's material welfare.'").

11. *Id.* at 56.

presumably lost on the campaign's architects. One example illustrated in Horan's book is a full-page ad placed in magazines in 1952.[12] The illustration depicts a smartly dressed couple mailing a letter to their elected officials, asking for reduced government spending. The copy reads in part: "[n]on-defense spending must be cut to the bone—for the good of all of us."[13]

Another example of governmental behavior comes from automobile insurance, where Horan describes extensive efforts by insurers to promote driver safety. By creating driver training devices and placing them in high schools, insurers were able to promote their brand and reduce future claims costs, while they collected valuable data on driver behavior.[14] This close mingling of public education and commerce, and of the public and private roles in promoting safety, well represents the quasi-public position of the insurance industry. Horan also shows how, in their highly consequential residential and commercial real estate investments—such as their development of suburban malls and urban residential communities like Stuyvesant Town—insurers made decisions about racial segregation[15] and acted on their preference for large versus small businesses in ways that shaped social and economic opportunity in both urban[16] and suburban locations.[17]

These mid-twentieth century examples are a revealing cross-section. They track well with the historical evolution of the insurance industry and give a nod to the subsequent trajectory. From the outset, insurers were conscious of the special role they occupied, proclaiming in the nineteenth century that their business was socially beneficial.[18] Because it reduced poverty and dependency, insurance was inherently aligned with the objectives of the public sector.[19] Since their business was so special, insurers consistently argued for full support from government, which largely meant mild regulation that benefitted the largest companies.[20] Policymakers tended to agree that the

12. *Id.* at 37 fig.1.4.

13. *Id.*

14. *Id.* at 61–62.

15. *See id.* at 139–166 ("'Communities without Hope': Urban Crisis and Insurance Redlining.").

16. *Id.* at 73–103 ("'Public Enterprises in Private Hands': Investing in Urban Renewal.").

17. *Id.* at 104–138 ("'A Mighty Pump': Financing Suburbanization.).

18. HEMPSTEAD, *supra* note 1, at xii.

19. *E.g.*, *id.* at xii ("[P]residents and other prominent citizens were out of their way to heap praise upon the [insurance] industry. Grover Cleveland even served as the head of a life insurance association after leaving office, noting that the management of life insurance involves 'a higher duty and more constant devotion than we associate with a mere business enterprise.'").

20. *Id.* at 24.

insurance business transcended "mere commerce."[21] In fact, in a consequential nineteenth-century Supreme Court decision, *Paul v. Virginia* enshrined that point of view, finding that sales of policies did not constitute commerce and granting regulatory purview to the states.[22] Insurers were thereby able to avoid federal regulation and greatly influence the state regulation that emerged in its stead.[23] There, problems stemming from unmet demand were addressed inadequately or more likely, not at all.[24] Even though insurance was described as having a broader social purpose, those who could not afford premiums or meet underwriting conditions would be deprived of its benefits.[25]

The ILI's propaganda campaign that Horan highlights had a distinctive historical context due to the infusion of Cold War anxieties that permeate the advertising copy.[26] Yet it is generally consistent with many earlier examples of governmental language and behavior from the life insurance industry. While life insurers in the early twentieth century did not speak as an industry or direct campaigns about the size of government at a general audience, they frequently spoke of their own efforts as though they were primarily engaged in a public service. This included the impossibly grandiose proclamation of New York Life's president George Perkins, upon the company's 60th anniversary in 1905, that one could assess the company's impact by reviewing the progress of the world, since "our great Company, has, in several notable respects, been a leader in the most potent influences that have been working for the betterment of humanity."[27] Metropolitan Life's president Haley Fiske,

21. *Id.* at xi.

22. Paul v. Virginia,75 U.S.168, 183 (1869), *overruled by* United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533 (1944); HEMPSTEAD, *supra* note 1, at 25.

23. *See* HEMPSTEAD, *supra* note 1, at 33–37 (describing ways that insurers influenced state regulation after the *Paul* decision).

24. *Id.* at 44–57.

25. *Id.*

26. *E.g.,* HORAN, *supra* note 4, at 27 ("Cold War ideology in the United States called for the active participation of citizens in defending 'distinctly American' values from the threat of communism. . . . [This] aided the insurance industry in its efforts to privatize security and elevate individual responsibility over collective risk sharing.").

27. LAWRENCE F. ABBOTT, THE STORY OF NYLIC: A HISTORY OF THE ORIGIN AND DEVELOPMENT OF THE NEW YORK LIFE INSURANCE COMPANY FROM 1845 TO 1929,at 125 (1930); HEMPSTEAD, *supra* note 1, at 204.

who described the company as a "trusteeship",[28] adopted a philanthropic tone in describing his company's mission as "the bettering of human conditions."[29]

Another example of the quasi-public role played by life insurers comes from the administration of "industrial" insurance—i.e., low-cost policies designed for the working poor,[30] sometimes also called "burial insurance."[31] The public health and sanitation measures undertaken by insurers, none more so than Metropolitan Life,[32] were in many ways precursors of future actions of urban public health departments. For example, there were educational programs for enrollees, particularly children, that tried to teach behavior that would improve health through better hygiene and sanitation.[33] A particular focus was on control of the housefly population.[34] Not only were the specific activities involved in the management of industrial insurance governmental in nature, but insurers—especially Metropolitan Life—described this line of business as "public service work" and spoke of it as though it were a charitable mission, which indicated their concern about government encroachment.[35] Similarly, companies that did not sell industrial insurance made a point to publicize new efforts to provide insurance policies for "impaired lives," meaning people with what we now call pre-existing conditions.[36] In these ways, life insurers tried to signal that their system of voluntary collectivism could meet the population's need for economic security, and that government intervention was not necessary.

Another example from *Insurance Era* is the insurance industry's promotion of driver safety instruction for teenagers.[37] Here there is rich historical precedent regarding the insurance industry's interventions to promote safety. Perhaps more than any other issue, efforts to increase safety illustrate the quasi-public purpose of insurance, and by extension insurers. In the earliest days of commercial fire insurance, insurers helped support voluntary firefighting organizations with signs on windows to signal to firefighters whether

28. MARQUIS JAMES, THE METROPOLITAN LIFE: A STUDY IN BUSINESS GROWTH 214 (1947); HEMPSTEAD, *supra* note 1, at 204.

29. LOUIS I. DUBLIN, A FAMILY OF THIRTY MILLION: THE STORY OF THE METROPOLITAN LIFE INSURANCE COMPANY 80 (1943); HEMPSTEAD, *supra* note 1, at 204.

30. HEMPSTEAD, *supa* note 1, at 201–02.

31. Gabriel J. McGlamery, *Race Based Underwriting and the Death of Burial Insurance*, 15 CONN. INS. L. J. 531, 535 (2008).

32. HEMPSTEAD, *supra* note 1, at 205.

33. HORAN, *supra* note 4, at 45.

34. HEMPSTEAD, *supra* note 1, at 81.

35. HORAN, *supra* note 4, at 43.

36. HEMPSTEAD, *supra* note 1, at 206.

37. HORAN, *supra* note 4, at 42–69.

a particular dwelling was insured by a sponsor company.[38] Before the turn of the twentieth century, insurers were beginning to set homeowners insurance rates based partly on public sector features such as municipal water supply and building codes.[39] They used the pages of their trade publications to exhort state and local government officials to improve safety infrastructure, positioning themselves as protectors of the public's safety.[40] One good example is the Insurance Company of North America (INA)'s "White Fireman" campaign in the 1930s, which depicted a fireman dressed in a white uniform, symbolizing the company's less visible but no less important contribution to safety that came not just from research and advocacy, but also from the incentives conveyed in policy language.[41]

The risk avoidance of individuals was another common source of fire insurer commentary, and excessive carelessness was frequently invoked as a problem that reflected a defect in the American character and drove up claim costs.[42] Focusing on carelessness (along with arson) was a good way to deflect attention from other potential causes of high and rising fire insurance rates, particularly at a time when state insurance regulators were powerless and unsophisticated, and data on losses and expenses were not regularly submitted.[43] This attention to carelessness was fused with World War I anxiety in a propaganda campaign carried out by the nation's first trade association, the National Board of Fire Underwriters.[44] In a book for children entitled *The Flame Fiend*, a genie makes a surprise visit "to a group of boys playing carelessly with an oil lamp and tries to both terrify them and use their patriotism to enlist them in a new war against an old enemy—fire waste."[45] The genie tells the boys that reducing fires is the only way to reduce insurance costs, and that people who are careless about causing fires "are traitors and criminals" who "should be put to death!"[46]

From the earliest days of the industry and across all lines of business, insurers adopted a quasi-public role to reduce losses and signal that their business was adequately meeting public needs, making additional government

38. HEMPSTEAD, *supra* note 1, at 104.

39. *Id.* at 106.

40. *Id.* at 18, 108.

41. Ins. Co. of N. Am., Illustration of advertisement with White Fireman at worksite, *in* LIFE, Sept. 11, 1939, at 5.

42. HEMPSTEAD, *supra* note 1, at 177.

43. *Id.* at 108.

44. *Id.* at 177.

45. *Id.* at 177–78.

46. *Id.* at 178.

involvement unnecessary.[47] To a large degree, this was a natural role for the insurers to inhabit. The insurance industry had preceded government in many "governmental" activities such as researching the causes of fire and accidents, educating people about disease prevention, maintaining statistics about morbidity and mortality, that ultimately became largely the purview of the public sector. And while state regulators attempted to temper some aspects of insurer business practices to protect consumers, they mounted no credible threat to the status quo, despite growing concerns about coverage gaps in many lines of business. And until the First World War, insurers did not have serious concerns about the potential for a significant federal role in the business.[48]

III. THE OPPOSITIONAL STANCE TOWARD GOVERNMENT

World War I provided the first important national example of federal government activity that concerned the insurance industry.[49] Prior to the War, most industry dealings with the government were at the state and local level.[50] While they sought favorable and generally mild types of insurance regulation, insurers generally advocated for stronger government intervention on issues of public health and safety that could reduce losses.[51] There was relatively little interaction with the federal government.[52] Yet the nation's entry into World War I catapulted the federal government into the role of the insurer.[53] Life insurers' inability to price war risk, along with the government's desire to incentivize men to enlist and hopefully avoid an expensive veterans' pension, led to an ambitious program that offered generous life insurance policies to soldiers at below-market rates.[54] The newly created Bureau of War Risk Insurance encouraged servicemen to keep their policies after they returned to civilian life.[55]

Life insurers assisted the government in the design of the new program, which also included disability benefits and support payments to family

47. *See generally id.* at ix–xvi (describing insurers as quasi-public and summarizing some of the industry's more governmental behaviors).

48. *Id.* at xiii–xiv.

49. *Id.*

50. *Id.* at xii–xiii.

51. *Id.* at 175.

52. *Id.* at 173.

53. *E.g.*, *id.* at 66 ("The federal government made an unexpected entry, providing low-cost life insurance to soldiers in World War I, a move that challenged private industry . . . .").

54. *Id.* at 85–86.

55. *Id.* at 87–90.

members.[56] Lee Frankel, head of Metropolitan Life's social welfare department, was one of many industry experts who joined academics and other social reforms to assist with the design of the wartime coverage.[57] The crisis of the war constrained insurers from being overly critical, but they secretly cheered when the effort collapsed in the post-war period due to the government's inability to collect premiums from returning soldiers.[58] This led to the formation of a new trade association, the American Life Conference, devoted in part to maintaining a vigilant posture against potential federal encroachment.[59] Haley Fiske, president of Metropolitan Life, watched government activity warily and estimated that if they could achieve twenty million enrollees, they could stop worrying about a government takeover.[60] This defensive posture by the industry foreshadows Horan's description of the creation of the ILI in response to New Deal oversight activities.

For property and casualty insurers, the risks from the federal government were actually far smaller but seemed no less concerning.[61] During World War I, the government temporarily managed marine insurance, and assumed control of the railroads, choosing to self-insure.[62] The industry, however, also got a voice in the wartime efforts, obtaining a position on the War Industries Board to advocate for fire prevention.[63]

Many social reformers in the United States hoped that the post-war period would see an extension of European trends towards more extensive social insurance.[64] Workers' compensation, which was spreading throughout the states, was envisioned as the first step in a more comprehensive public program of health, old age, and unemployment insurance.[65] But insurers emerged from the war hoping to reset the boundary with government, and the "Americanization" ethos, that infused business in the 1920s, advocated for the non-interference of business with government and denounced any form of state insurance as a stepping stone to socialism.[66] This rhetoric helped to

56. *Id.* at 86.

57. *Id.* at 88.

58. *See id.* at 89–90 (describing life insurers' concerns about the federal government taking part in their industry, while recognizing it as a necessity during World War I).

59. *Id.* at 210.

60. *Id.* at 210–211.

61. *Id.* at 174–75.

62. *Id.* at 166.

63. *Id.* at 141.

64. *Id.* at 144.

65. *Id.* at 143–44.

66. *Id.* at 162.

defeat efforts to expand social insurance or state involvement in insurance wherever they appeared.[67] The "Americanization" effort can be seen as an early precursor to the ILI campaign described in *Insurance Era*.[68] While government officials and academics may have become increasingly interested in the potential use of insurance as a policy tool, those in the industry did not seek the role of thought partner. When invited to testify before Congress in the 1920s, property and casualty insurers were sullen and resistant; they displayed no interest in brainstorming with the federal government about how to create all-hazard crop insurance.[69] Insurers wanted the freedom to choose their risks, and market failures were seen as things to avoid, rather than problems to solve through public policy.[70]

IV. THE QUASI-PUBLIC ROLE BECOMES A BURDEN

As the twentieth century progressed, the quasi-public role of insurers became increasingly difficult to sustain. For life insurers, the Depression was an inflection point.[71] The creation of Social Security was, in part, a recognition of the inadequacy and unaffordability of life insurance for many people.[72] Most life insurers, particularly the larger ones, quietly acknowledged this truth.[73] They accepted Social Security as a complement to their businesses and began to refer to it in marketing materials as a base upon which to build.[74]

However, the New Deal led to a broader critique of the insurance business. President Franklin Roosevelt's Temporary National Economic Commission (TNEC), established in 1938, held a series of critical hearings about life insurance, some of which castigated the economics of industrial insurance.[75] Horan describes how the creation of the ILI was, in part, a panicked response to the TNEC inquiries and the potential for greater federal regulation of the insurance business. [76]

To fend off the threat from the federal government, insurers were under increasing pressure to demonstrate that they could meet the public's

67. *Id.* at 168.
68. HORAN, *supra* note 4, at 17, 33–41, 46, 58, 69.
69. HEMPSTEAD, *supra* note 1, at 175–76.
70. *Id.*
71. *Id.* at 201.
72. *Id.*
73. *Id.* at 201–02.
74. *Id.* at 219.
75. *Id.* at 127, 221–27.
76. HORAN, *supra* note 4, at 24–26.

needs.[77] Large and systemic coverage gaps created bad publicity and difficult conversations, which increasingly took the form of Congressional oversight hearings.[78] The lack of affordable health insurance for older Americans ultimately became a bridge too far.[79] In 1965, just a little more than a decade after the ILI's publicity campaign about privatized security, Medicare and Medicaid were established.[80] By then, most life and health insurers had acknowledged the limits of what they could provide, and many could already see the business opportunity that would come from government-financed insurance.[81] This evolution reflected the growing consensus that coverage gaps and many other social problems could only be addressed through public policy and public funding. Horan provides an example of how this new dependency played out with regard to urban reinvestment, where life insurers sought help from the government and ultimately were forced to acknowledge the limitations of private enterprise.[82]

For property and casualty insurers, the fear of a federal takeover was less credible, but an analogous type of challenge occurred as insurers faced increasing pressure from states to provide coverage to everyone. A good example is mandatory auto insurance. Correctly fearing that mandates would create the expectation that nearly everyone should be able to get insurance, insurers initially opposed the policy,[83] then complained that states were not doing enough to enforce traffic safety rules and revoke the driving privileges of those who violated them.[84] The investments in driving safety described in *Insurance Era* were part of a multi-pronged effort on the part of insurers to reduce losses and improve their ability to select risks.[85] Critiques of arbitrary and potentially discriminatory aspects of auto underwriting practices started in the mid-twentieth century[86] and have persisted to the present.[87] While finding ways to avoid bad risks is a persistent tactic in home and auto insurance,

77. HEMPSTEAD, *supra* note 1, at 234.

78. *Id.*

79. *Id.*

80. *Id.*

81. *Id.* at 234–35.

82. HORAN, *supra* note 4, at 154.

83. HEMPSTEAD, *supra* note 1, at 276–77.

84. *Id.* at 276.

85. HORAN, *supra* note 4, at 59–69.

86. HEMPSTEAD, *supra* note 1, at 279–80.

87. *E.g.*, Emily Flitter, *Seeking the 'Right' Customers, an Insurer is Accused of Discrimination*, N.Y. TIMES (Oct. 30, 2023), https://www.nytimes.com/2023/10/30/business/erie-insurance-lawsuit-maryland.html.

market exit is sometimes more attractive, and insurers have been increasingly exercising that option as costs associated with climate change rise.[88]

State and federal governments have become involved on the peripheries of poorly functioning property and casualty markets. In most states, insurers have been required to jointly contribute to some type of "coverage of last resort" in secondary markets for home and auto insurance.[89] Some states have begun to play larger roles in subsidizing loss mitigation in home insurance markets, where climate is a growing factor, though not enough to keep up meaningfully with rising costs.[90] The federal government has provided financial backstops for certain parts of property markets, such as federal reinsurance for losses caused by acts of terrorism.[91] Another example is the National Flood Insurance Program, where insurers distribute and service plans while the government is at risk.[92]

In life and health insurance, the growing unacceptability of coverage gaps over the course of the twentieth century forced the industry to retreat somewhat from their quasi-public role and cede ground to government. Historically, insurers have sought to navigate "hard" property and casualty markets by reducing losses and selecting risks, and thus far, the public role has been limited. Yet growing losses, as exemplified by the recent California wildfires, suggest that the limits of what a state regulated private market can do to provide affordable coverage are being tested.[93] Realistic approaches for

88. Christopher Flavelle, *Insurers are Deserting Homeowners as Climate Shocks Worsen*, N.Y. TIMES (Dec. 18, 2024), https://www.nytimes.com/interactive/2024/12/18/climate/insurance-non-renewal-climate-crisis.html.

89. *E.g., What is the New York Automobile Insurance (NYAIP)*, N.Y. MOTOR INS., https://www.newyorkmotorinsurance.com/blog/what-is-the-new-york-automobile-insurance-plan/ (last updated Sept. 23, 2020). *See generally* Mel Duvall, *State Insurers of Last Resort: How FAIR Plans Work and Which States Have One*, INSURANCE.COM, https://www.insurance.com/home-and-renters-insurance/home-insurance-basics/insurers-of-last-resort (last updated Jan. 9, 2025) (explaining what last-resort insurance is and which states have these plans in place).

90. *E.g.*, Sheldon Dutes, *Pricey Premiums Persist Despite Stabilizing Home Insurance Trends in Florida*, WESH 2, https://www.wesh.com/article/florida-home-insurance-prices-premium/62881670 (last updated Nov. 13, 2024, 7:22 AM).

91. Anne Gron & Alan O. Sykes, *Terrorism and Insurance Markets: A Role of the Government as Insurer*, 36 IND. L. REV. 447, 447–48 (2003).

92. NAT'L FLOOD INS. PROGRAM, https://www.floodsmart.gov/ (last visited Feb. 15, 2025).

93. *E.g.*, Alex Brown, *California Fires Show States' 'Last Resort' Insurance Plans Could Be Overwhelmed*, STATELINE (Jan. 16, 2025, 5:00 AM), https://stateline.org/2025/01/16/california-fires-show-states-last-resort-insurance-plans-could-be-overwhelmed/.

loss prevention will likely require a larger role for government and a different kind of public-private collaboration.

V. CONCLUSION

The insurance industry and government are increasingly co-dependent. Government provides some insurance directly and purchases or subsidizes the cost of insurance in many other markets.[94] It has become increasingly clear that most problems in insurance markets can only be solved through some combination of regulation and public funding. Yet that does not necessarily lead to a consensus on whether or how these problems should be solved.

We stand at an interesting crossroads with regards to insurance. Property and casualty markets, which have historically been far more privatized than life and health insurance, are under increasing pressure as losses mount and affordability problems affect markets for new and existing housing in many states.[95] There is a growing discussion of a larger federal role, such as national disaster re-insurance,[96] but talk of such ideas kicks the hornet's nest of federalism, as well as the traditional opposition to increased government spending.[97] In health insurance, there are potential policy proposals that would roll back coverage gains and increase premiums for millions.[98] The new Administration claims they are committed both to smaller government

94. *E.g.*, Sheldon Dutes, *Pricey Premiums Persist Despite Stabilizing Home Insurance Trends in Florida*, WESH 2, https://www.wesh.com/article/florida-home-insurance-prices-premium/62881670 (last updated Nov. 13, 2024, 7:22 AM).

95. Trân Nguyễn, *California's Insurer for People Without Private Coverage Need $1 Billion More for LA Fires Claims*, ASSOCIATED PRESS, https://apnews.com/article/california-wildfires-insurance-fair-plan-dfb7cda506560ec50edee8ad72cbcda8 (last updated Feb. 11, 2025, 8:15 PM). *See generally*, HEMPSTEAD, *supra* note 1; HORAN, *supra* note 4.

96. *See, e.g.*, INSURE Act, H.R. 6944, 118th Cong. (2024) (establishing, if enacted, a catastrophic property loss reinsurance program).

97. *E.g.*, Jen Frost, *The 'Red Flags' in INSURE Act Natural Catastrophe Reinsurance Program Bill*, INS. BUS. (Feb. 5, 2024), https://www.insurancebusinessmag.com/us/news/catastrophe/the-red-flags-in-insure-act-natural-catastrophe-reinsurance-program-bill-475765.aspx.

98. *See* ALLISON ORRIS & CLAIRE HEYISON, CTR. ON BUDGET & POL'Y PRIORITIES, REPUBLICAN HEALTH COVERAGE PROPOSALS WOULD INCREASE NUMBER OF UNINSURED, RAISE PEOPLE'S COSTS 1, (2024) (discussing how certain Medicaid and Marketplace proposals would reduce coverage, increase premiums, or reduce benefits).

and reducing economic pressure for average Americans.[99] Given the challenge of insurance affordability, this may be a difficult needle to thread.[100]

From the earliest days of the business, insurers have acted the part of a government providing a public service, while maintaining fierce opposition to the actual government and expressing little or no concern for those that could not obtain the protection that insurance afforded. Over time, publicly subsidized insurance has slowly and imperfectly filled some of the coverage gaps that exist. However, public efforts have largely been structured to fit around the footprint created by the private market. *Insurance Era* is an astute distillation of a period in our history when the insurance industry's vision of a "privatized security" first began to die. Yet many aspects of that dream are part of our collective legacy today—not just in our insurance markets, but also in our urban and suburban landscapes, and in our understanding of what is fair.

99. *See, e.g.*, Justin Lahart, Ruth Simon, & Paul Kiernan, *Trump's Conflicting Business Policies Sow Economic Uncertainty*, WALL STREET J. (Feb. 10, 2025, 9:00 PM), https://www.wsj.com/economy/trump-business-uncertainty-tariffs-immigration-energy-ef57cfbb (describing the Trump Administration's plans to reduce the size of the federal government, implement pro-business policies, and raise tariffs, as well as the tension around these goals).

100. *Id.*

E/INSURING THE AI AGE: EMPIRICAL INSIGHTS INTO ARTIFICIAL INTELLIGENCE LIABILITY POLICIES

ANAT LIOR*

ABSTRACT

Insurance represents an important but underappreciated part of our lives. Both individuals and corporations gain from purchasing coverage from insurers to manage and hedge their risks. It is a necessary mechanism in modern society to support innovation while ensuring that its unavoidable victims will be compensated. The innovation of emerging technologies alters the existing risk landscape, challenging insurance companies, innovators, and individuals' ability to manage their risks. The current emerging technology of Artificial Intelligence (AI) significantly emphasizes this trend. Insurance companies are grappling with the notion of AI. They are exploring different traditional and novel insurance products that they can offer both corporations and users to manage the risks associated with AI. In return, the market for AI coverage presents unprecedented growth and revenue opportunities. Insurance is set to play a pivotal role in AI's development and distribution, actively shaping risk mitigation strategies and regulatory frameworks for AI users and companies. This is not just an academic gap — it is a pressing regulatory issue with tangible, real-world implications.

This paper examines the intersection of AI and insurance from an empirical perspective. It presents empirical findings from the insurance sector, delving into the operational dynamics of liability policies covering risks associated with AI. Through in-depth interviews with key industry stakeholders, including underwriters, brokers, and AI users navigating the uncharted risks AI presents, this paper offers a deeper understanding of three crucial questions. First, is there a need for a specialized AI insurance policy, and how should underwriting adapt to AI's unpredictable risks? Second, do existing liability policies, such as cyber insurance and product liability, adequately cover AI-related risks, or do they leave dangerous gaps that could expose both insurers and policyholders (known as "silent AI")? Third, what role should legislators play in crafting policies that equitably manage AI risks for all stakeholders?

The findings reveal a rapidly evolving insurance market where underwriters, brokers, and AI users recognize the deep connection between anticipated AI regulation, substantial financial penalties, and the emergence of

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an AI-specific insurance sector. Bridging theory with practical applications is pivotal in academic and theoretical writing. This holds particular significance in the insurance realm, impacting AI users and innovators. Collaboration is necessary between those who discuss insurance for AI from a legal perspective and those who underwrite AI policies from an actuarial perspective, as new AI regulations and litigation are likely to create a new insurance market for AI.

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I. INTRODUCTION

If an autonomous vehicle collides with a parking car, injuring passengers in both cars and causing severe damage to the vehicles, which automobile policy will cover the damage?[1] What about a doctor using an AI algorithm to determine the best treatment, resulting in harm to their patient?[2] Will the doctor's professional indemnity liability policy step in and pay if malpractice is proven? What if a company's Director asks a Generative AI application to decide if liquidating the company will be a good business decision,[3] but it gets it wrong? Will a Director and Officers policy protect them? These and similar questions are a significant source of concern for insurance companies offering policies to individuals and corporations adopting AI, as well as policyholders who are unclear whether they will be covered by their existing policies as they increasingly begin to adopt AI.

Insurance is ubiquitous and omnipresent in our society.[4] It is indisputable that insurance is a significant part of our personal lives, from health insurance to automobile insurance, homeowners or renter insurance, and even pet insurance.[5] It is also a significant part of the commercial ecosystem, from malpractice to Error and Omission and Commercial General Liability policies. Liability insurance is a valuable tool for managing future risks associated with the emerging technology of artificial intelligence (AI). It is predictable that the increasing usage of AI, especially Generative AI (GenAI), in the upcoming years will alter the risk landscape as we know it today. Casualties, liability, and property harm seem unavoidable as AI will take a more prominent place in our personal lives and the commercial market. This presents a

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1. *Insurance for Self-Driving Cars*, PROGRESSIVE, www.progressive.com/answers/insurance-for-driverless-cars/ (last visited Mar. 26, 2025).

2. Marialuisa Gallozzi & Megan Mumford Myers, *AI Brings New Insurance Concerns for Healthcare Providers*, LAW 360 (Dec. 6, 2023, 2:21 PM), www.cov.com/-/media/files/corporate/publications/2023/12/ai-brings-new-insurance-concerns-for-healthcare-providers.pdf.

3. Fin. Servs. Grp., *The Growing Use of Artificial Intelligence: D&O Risks and Potential Coverage Solutions*, AON (Apr. 2024), www.aon.com/risk-services/financial-services-group/the-growing-use-of-artificial-intelligence-d-and-o-risks-and-potential-coverage-solutions.

4. It is also notoriously hated. *See, e.g.,* Inez Cooper, *Why Do Insurance Companies Have Bad Reputations?*, WILLIAM RUSSELL, www.william-russell.com/blog/insurance-companies-bad-reputations/ (last visited Mar. 26, 2025).

5. *Types of Insurance*, OFFICE OF THE INSURANCE COMMISSIONER, WASHINGTON STATE, www.insurance.wa.gov/types-insurance. A new policy also offers insurance against being culturally "canceled." Chris Morris, *Yes, You Can Get Insurance to Protect Yourself From Being 'Canceled'*, INC. (Jan. 31, 2025), www.inc.com/chris-morris/cancel-culture-insurance-for-executives-celebrities/91141847.

unique challenge to the insurance industry. Insurers are attempting to adapt themselves and the policies they offer to the uncertain risks associated with AI and its unavoidable harm.

Those risks might include harms that insurance companies already offer coverage for via one of their traditional policies. For example, risks of data privacy and hacking due to social engineering via AI should be covered under existing cyber insurance policies; workforce disruptions and discrimination carried by employers using AI algorithms during their hiring process should be covered by Employment Practices Liability (EPL) policies;[6] Professional Indemnity (PI) policies should cover lawyers' and doctors' malpractice while using AI in different aspects of their work; mistakes made by officers and directors of corporations in running their companies should be covered by Directors & Officers (D&O) policies; and much more.[7] But are these policies sufficient to handle the added risks manifested by AI? Should the insurance industry strive to offer a new designated AI policy like it did with cyber insurance or operate to tweak its existing policies? And what, if any, is the role of legislation? This paper tackles these three topics from an empirical standpoint to better understand and guide the role liability insurance has and will have in the AI age.

Emerging technologies, such as AI, are imperative in today's commercial market worldwide.[8] Innovation has become an inseparable part of our day-to-day lives by improving it in new and unexpected ways. These improvements, however, come at a cost when these new technologies alter the current threat landscape and lead to different (but not necessarily new) scopes and types of risks, losses, and damages. The insurance industry could help to transfer the risks associated with AI, distribute that cost better, and even reduce it. Insurance has had, and continues to have, a significant role in managing threats and losses resulting from innovation.[9]

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6. Miranda Bogen, *All the Ways Hiring Algorithms Can Introduce Bias*, HARV. BUS. REV. (May 6, 2019), hbr.org/2019/05/all-the-ways-hiring-algorithms-can-introduce-bias; Daniel Wiessner, *Workday Must Face Novel Bias Lawsuit Over AI Screening Software*, REUTERS (Jul. 16, 2024), https://www.reuters.com/legal/litigation/workday-must-face-novel-bias-lawsuit-over-ai-screening-software-2024-07-15/.

7. *See infra* Chapter V.

8. *See generally*, GRAND VIEW RESEARCH, ARTIFICIAL INTELLIGENCE (AI) IN MARKETING MARKET SIZE, SHARE & TRENDS ANALYSIS REPORT BY COMPONENT (SOFTWARE SERVICES), BY APPLICATION (SOCIAL MEDIA ADVERTISING, SEARCH ENGINE MARKETING), BY TECHNOLOGY, BY END-USER INDUSTRY, BY REGION, AND SEGMENT FORECASTS, 2025 – 2030, www.grandviewresearch.com/industry-analysis/artificial-intelligence-marketing-market-report.

9. *E.g.*, Michelle Chia, *Steering Through A Transitioning Cyber Insurance Market*, RISK & INS. (Mar. 19, 2025), https://riskandinsurance.com/steering-through-a-transitioning-cyber-insurance-market/ (describing how the cyber

AI could present what is known in the insurance industry as a black or grey swan event. Black swan events are "sudden shocks that could not have been foreseen or predicted."[10] These include the COVID-19 pandemic and massive cyberattacks. Grey swan events are "predictable but unlikely surprises."[11] For example, the 2007/08 financial crisis.[12] Grey swans involve some sort of a "knowledge gap, a misalignment in plans, expectations, or incentives, or other errors, particularly those arising from biases."[13] Individuals usually prefer to be optimistic and thus ignore or disregard a chance of bad outcomes when they are unlikely but still predictable.[14] We do not pursue the relevant information or flat-out ignore what is right in front of us. These types of events put enormous stress on the insurance industry, which wants to offer coverage but might overpromise and underdeliver if a black or grey swan transpires.

AI technology is the modern epiphany of the black-grey swan. Consumers and innovators have limited data on the risks associated with AI events, and while these threats are conceivable, they are currently mostly neglected.[15] Insurance companies have struggled to address the risks associated with these events but are gaining valuable information from their relative repetition in today's modern age.[16] It seems that these black-grey swan events

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insurance field address—or sometimes fails to adequately address—the constantly-evolving risk of cyber threats).

10. Keith Tracey, *Black and Grey Swans: 5 Ways to Avoid Shocks*, AON (Feb. 2022), www.aon.com/risk-services/professional-services/black-and-grey-swans-5-ways-to-avoid-shocks.jsp. These could be either positive or negative, and are considered a rare and highly unpredictable event that has a severe (non-linear) impact. *Id.*

11. *Id*.

12. DEBORAH PRETTY, RESPECTING THE GREY SWAN: 40 YEARS OF REPUTATION CRISES, AON 8 (2021), www.aon.com/getmedia/03965282-4d98-49c3-9e4c-97d4fbfb2c3e/Respecting-the-Grey-Swan.aspx.

13. Tracey, *supra* note 10.

14. Pretty, *supra* note 12, at 7 ("We are aware of the possibility of these events but, equally, understand their occurrence to be unlikely. Should such an event befall us, its impact will be significant. We have been warned that it could happen but believe that it is unlikely to happen to us, and have invested our scarce resources elsewhere").

15. *See, e.g.*, The Gray Area with Sean Illing, *Is Ethical AI Possible?* (Sep. 1, 2023), podcasts.apple.com/us/podcast/is-ethical-ai-possible/id1081584611?i=1000593166307.

16. *See. e.g.*, Gary Pearce, *An Insurance Pro's Practical Guide to 'Black Swan' Events*, ALM (Mar. 19, 2020, 6:30 AM),www.propertycasualty360.com/2020/03/19/an-insurance-pros-practical-guide-to-black-swan-events/?slreturn=20241209115239; Sean King, *Using Captives to*

require a different approach in the AI context. As such, simple auditing would probably not suffice for the insurance industry to manage AI-associated risks.[17] A deeper understanding of AI is required to adjust current actuarial approaches for AI. Some of it is already available through ongoing AI regulation and litigation, the latter of which has increased recently due to the prevalent usage of GenAI.[18] AI litigation provides important information to insurance providers by detailing the claims, the scope of damages, and how the court evaluates said damages when granting compensation.

Though the topic of insurance and emerging technologies is gaining interest,[19] this intersection remains vastly underexplored.[20] This is especially true given the current disconnect between those who research insurance policies covering emerging technologies from a legal perspective, and those who practice insurance and underwrite these policies from an actuarial perspective. This paper aims to bridge this gap by presenting insights from interviews with stakeholders from the insurance industry. It provides a combination of literature review and empirical research findings within the insurance industry, focusing on the operational aspects of liability policies concerning AI and how these can benefit the AI industry and its consumers.

Insure Against Black Swan Events, RISK MGMT. MONITOR (Apr. 24, 2020), www.riskmanagementmonitor.com/using-captives-to-insure-against-black-swan-events.

17. Zoom Interview with George Lewin-Smith, CEO and Co-Founder, Testudo & Mark Titmarsh, CPO and Co-Founder, Testudo (Jun. 24, 2024). They emphasize that simply relying on audits will not be a good predictor of risk for insurers as this is a gross oversimplification of how a complex system works. *Id.* They provide an example of relying on evaluations as a predictor of liability risk, which is a "green lumber problem." *Id.* The data suggests that evaluations have little predictive power when assessing the probability of litigation *Id.* (A green lumber problem refers to a cognitive bias where one misinterprets an apparent surface-level detail (like the "green" color of freshly cut lumber) as the key factor in a situation, thus overlooking deeper, more important underlying complexities that could significantly impact the outcome). *Id.*

18. Insurance companies are creating database litigation to receive a better understanding of the risks, harms, and actual cases that emerge from AI usage, at least when it comes to damage that occurred to third parties. For more information on these datasets, *see infra* note 240 and accompanying text.

19. *See, e.g.*, Phila. Ins. Co., *How Insurance Can Help Manage the Darkside of 4 Emerging Technologies*, RISK & INS. (Nov. 18, 2024), riskandinsurance.com/sponsored-how-insurance-can-help-manage-the-darkside-of-4-emerging-technologies/.

20. For example, a recent comprehensive report reviewing the possible ways to govern GenAI doesn't mention insurance as a possibility. *See* Florence G'sell, *Regulating Under Uncertainty: Governance Options for Generative AI*, STANFORD CYBER POL'Y CTR. (2024), cyber.fsi.stanford.edu/content/regulating-under-uncertainty-governance-options-generative-ai.

The interviewers' identities are disclosed if they have agreed to do so. Otherwise, their thoughts and answers are anonymously incorporated. The interviews presented here were conducted with stakeholders in the field, including small to medium AI companies, individual AI consumers seeking coverage from insurance carriers, brokers facilitating this process, and insurance and reinsurance companies operating in this field or considering providing coverage to AI companies.

The empirical research focuses on, among other things, the underwriting and risk assessment process, which determines if an insurance carrier will offer coverage and, if so, for what price (i.e., premium). A close examination of insurance firms' underwriting practices for AI aims to uncover nuanced insights into their strategies and challenges in assessing a new technology without a substantial data set, which puts insurers at a disadvantage in offering adequate coverage. This exploration also extends to examining insurers' comprehension of acting as 'quasi-regulators,'[21] elucidating their strategies to navigate and manage the risks associated with AI technologies entering the market.

When it comes to emerging technologies, insurance companies have two distinct purposes that pull them in different directions. On the one hand, they strive to maintain a constant level of risk in the world to ensure that there will always be a demand for their policies.[22] For example, there will be no demand for fire policies in a world without fire, or automobile insurance in a world without car accidents. Thus, it is in their interest to maintain constant levels of risk to ensure the industry's viability. In that sense, offering coverage for AI technologies is a smart business decision as the levels of risk associated with this technology are high. On the other hand, AI is posed as a safety-enhancing mechanism; as such, it might eliminate the current steady levels of risk we are experiencing in the world as consumers.[23] This may lead to a future where insurance companies have a pervasive incentive to stifle the development of AI rather than support it. This unique tension stands at the heart of the intersection between AI and the insurance policies covering it. Still, it

21. This refers to entities that have no regulatory authorization but hold the capacity to enforce rules within their industry, acting as a semi-regulator in its domain. For more information on insurers as quasi-regulators, *see infra* Chapter VII.2.

22. *See generally* Ronen Avraham & Ariel Porat, *The Dark Side of Insurance*, 19 REV. L. & ECON. 13 (2023) (arguing that the insurance industry has a "dark side" because insurers employ tactics to shift losses onto their insured rather than engaging in loss reduction to decrease risks in the world, possibly creating more risk).

23. *Id.* at 16 ("Notably, insurers have an individual short-term interest in providing their insureds with incentives to reduce risks. But all insurers as a group have a long-term interest to provide all insureds with incentives not to reduce risks and sometimes even to increase them.").

does not seem to influence insurers' decision to offer coverage for AI, at least at the moment.

Additionally, the interviews revealed how the insurance industry perceives the legislator's role in this domain. Interviewers shared their expectations from legislative bodies to facilitate a conducive environment for offering coverage in the rapidly evolving landscape of AI technology. Understanding insurers' perspectives on legislators' roles and responsibilities concerning AI's impact on insurance is pivotal to navigating this field's regulatory and operational challenges. US insurance companies have historically wielded significant influence through their strong lobbying efforts on legislation.[24] Thus, it is crucial to explore the intersection points between legislation and the insurance industry's actions when it comes to policies offered to cover risks associated with AI technology.

An example could be derived from the cyber insurance context via the New York Cyber Insurance Risk Framework, published in 2021.[25] This framework is aimed to, "foster the growth of a robust cyber insurance market that maintains the financial stability of insurers and protects insureds."[26] Certain perspectives suggest that proactive engagement from legislators is crucial to sustaining the availability of innovative insurance products tied to new technology, acknowledging the challenges insurance carriers face in effectively providing these offerings.[27] Moreover, there is a clear governmental desire to support AI technologies' safe but rapid development.[28] Ensuring the availability of a robust set of insurance products via legislation is an important path legislators are considering.

The interviews were conducted with global stakeholders, mostly located in the United States and the United Kingdom, who provide services worldwide, thus providing a comparative perspective of liability policies covering AI technology. Despite the lack of physical borders when offering coverage via a liability policy, each region is dominated by different regulatory landscapes, norms, and cultural approaches regarding AI policy. Each jurisdiction has a different appetite and capacity to manage risks, and thus, they present somewhat different approaches and insights. The EU AI Act will

24. *See, e.g.*, HOT COFFEE (HBO Apr. 22, 2011) (analyzing tort reform in the United States).

25. For more on this, *see infra* Chapter VII.1.

26. Insurance Circular Letter No. 2 from Linda A. Lacewell, Superintendent, N.Y. Dep't Fin. Servs., to All Authorized Property/Casualty Insurers, N.Y. State Dep't of Fin. Serv. (Feb. 4, 2021), www.dfs.ny.gov/industry_guidance/circular_letters/cl2021_02

27. *Id.*

28. *See, e.g.*, Staff of H. R. Subcomm. on Rsch. & Tech., 118th Cong., Bipartisan House Task Force Rep. on A.I., at v (Dec. 2024) www.speaker.gov/wp-content/uploads/2024/12/AI-Task-Force-Report-FINAL.pdf.

significantly affect global tech companies' compliance as it will become effective in the next two years.[29] These companies might fear operating in the EU, given this Act. This is evident from Apple's recent decision not to deploy its AI technology in Europe.[30] Given its broad applicability, the EU AI Act also has a significant influence on the current discussion in the US, which is opting for a more fragmented and flexible approach to AI policy, as was evident from Former President Biden's recently revoked administration's Executive Order on the Safe, Secure, and Trustworthy Development and Use of Artificial Intelligence.[31] President Trump's new Executive Order signals that the same fragmented approach will be taken in the near future.[32] Regulations set in different countries are an important part of insurers' ability and motivation to offer policies covering AI worldwide.

The paper continues as follows: Chapter II provides a brief historical background for the role of insurance in supporting emerging technologies. Chapter III presents the current suggested AI-specific policies that are currently offered or developed. Chapter IV introduces the notion of "silent AI" and discusses the lessons that could be learned from the history of cyber insurance and its applicability to the AI market. Chapter V delves into the available traditional policies and their ability, or lack thereof, to offer coverage for AI activities. Chapter VI presents the underwriting process and risk perception of AI harms. It also delves into the case of big AI companies, using Amazon as a case study, that presents a unique challenge in the context of liability policies. It is more likely than not that these companies will not view insurance as a preferable means of risk-hedging, given the extremely high volume of potential damages and their ability to self-insure. Chapter VII discusses the market dynamics and regulatory landscape, focusing on insurance law, insurers' role as quasi-regulators, including consumer education, and the influence of liability legislation on the development of a new insurance market for AI. Chapter VIII showcases specific case studies, industries, and sectors of particular interest to the insurance industry–such as autonomous vehicles and AI used in the healthcare system.[33] Chapter IX concludes.

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29. Joshua McAlpine, *The EU AI Act is Coming into Force. Here's What It Means for You*, Morningstar (Mar. 18, 2025, 1:45 PM), https://www.morningstar.co.uk/uk/news/262229/the-eu-ai-act-is-coming-into-force-heres-what-it-means-for-you.aspx.

30. Ivana Saric, *Apple Says It Won't Roll Out AI Features in Europe Due to Regulatory Concerns*, AXIOS (Jun. 21, 2024), www.axios.com/2024/06/21/apple-ai-features-europe.

31. Exec. Order No. 14,110, 88 Fed. Reg. 75,635 (Oct. 30, 2023).

32. Exec. Order No. 14,179, 90 Fed. Reg. 8,741 (Jan. 23, 2025).

33. Rachel Phillips, *AI in Healthcare: How to Manage Artificial Intelligence Risk*, WTW (Nov. 6, 2023), www.wtwco.com/en-gb/insights/2023/11/ai-in-healthcare-how-to-manage-artificial-intelligence-risk.

II. BRIEF HISTORICAL BACKGROUND

To better understand the vital role insurance can have concerning the safe development and implementation of AI into our commercial market, two historical examples are apt: policies covering risks associated with steam boilers and fire policies during the first industrial revolution. These examples assist in establishing the important role insurance can and should have in offering coverage to new emerging technologies such as AI.

First, the steam engine, a machine using steam power to perform mechanical work via heat, was an essential part of the first industrial revolution in the eighteenth century.[34] It enabled faster manufacturing practices.[35] Unsurprisingly, the new usage of steam power to operate machinery led to increased injuries and deaths due to frequent steam boiler explosions.[36] For example, in New York, "the Hague Street Disaster of 1850 claimed the lives of sixty-seven workers."[37] Shortly after, in 1853, a statute was enacted by the legislature of New York authorizing the formation of companies to issue policies "upon steam-boilers, against explosion, and against loss or damage to life or property resulting therefrom."[38] Insurance firms offering coverage for boiler accidents "estimated that over seven thousand people were killed in boiler explosions in the United States between 1833 and 1907."[39]

On June 30, 1866, The Hartford Steam Boiler Inspection and Insurance Company (HSB) was founded, considering itself "the first company in

34. *The History of HSB*, HSB, https://perma.cc/KH5G-87KW (last visited Apr. 13, 2025).

35. *Id.*

36. *Id.* ("With thousands of boilers in operation throughout the country, there was also widespread ignorance about the properties of steam and the causes of boiler explosions. During the 1850's, explosions were occurring at the rate of almost one every four days."). *See also* ALAN MCEWEN, HISTORIC STEAM BOILER EXPLOSIONS (2009).

37. John Fabian Witt, *Speedy Fred Taylor and the Ironies of Enterprise Liability*, 103 COLUM. L. REV. 1, 31 (2003).

38. Chicago Sugar Ref. Co. v. American Steam-Boiler Co., 48 F. 198 (N.D. Ill. 1891).

39. Witt, *supra* note 37, at 30–31. ("A growing number of establishments turned to steam power, and as boilers became more and more powerful, boiler explosions wreaked havoc in early American manufacturing. Fatal boiler explosions were reported as early as 1838, and in the 1850s and 1860s disastrous boiler catastrophes made headlines.").

America devoted primarily to industrial safety."[40] HSB estimated that between 1880 and 1886, about one thousand boiler explosions occurred in the U.S., causing damage to property in the amount of three million dollars and around 1,500 deaths and injuries.[41] HSB provided safety information about the steam engine to its policyholders as a loss prevention tool—information aimed at minimizing the occurrence of accidents and maximizing available safety instruments.[42] Insurance companies offering coverage for boiler damages, such as HSB, "collected comprehensive statistics on boiler accidents, which made it possible for the first time to make scientific investigations into the relative merits of alternate boiler design."[43] As a result, the safety measures taken by insurance carriers, including inspections conducted by engineers, "sharply reduced the incidence of boiler explosions."[44] This example demonstrates the power insurers have to advance a better understanding of new technologies, given their incentive to reduce the risks associated with them. As we will see below, to this day, HSB provides insurance for technology-related products today, including AI products.[45]

Second, the product of fire insurance policies underwent an extensive evolution process in response to the challenges the insurance industry faced in the last quarter of the eighteenth century.[46] Fire insurance was well established during the years preceding the First Industrial Revolution, but the complexity of industrial property and the risks associated with it were foreign to the information and calculations insurers used before.[47] Unlike previous domestic workshops, the emergence of factories and the above-mentioned steam engines created a far more excessive concentrated risk, which was not in line with previous information on calculated premiums. Despite these difficulties,

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40. *The History of HSB*, *supra* note 34. The UK equivalent were the Vulcan Boiler & General Insurance Company (1859) and British Engine Insurance (1878). MCEWEN, *supra* note 36.

41. Witt, *supra* note 37, at 31.

42. For more on steam boiler insurance, *see* Richard J. Martin & Ali Reza, *What is an Explosion? A Case History of an Investigation for the Insurance Industry*, 14 J. LOSS PREVENTION PROCESS INDUS. 491 (2000); DAVID JOHN DENAULT, AN ECONOMIC ANALYSIS OF STEAM BOILER EXPLOSIONS IN THE NINETEENTH-CENTURY UNITED STATES (1993).

43. Witt, *supra* note 37, at 32.

44. *Id.*

45. *See Products*, HSB, https://perma.cc/BL2S-DU5M (last visited Apr. 13, 2025). *See infra* Chapter III.

46. ROBIN PEARSON, INSURING THE INDUSTRIAL REVOLUTION: FIRE INSURANCE IN GREAT BRITAIN, 1700-1850, AT 10–11 (2017).

47. M.W. Beresford, *Prometheus Insured: The Sun Fire Agency in Leeds During Urbanization, 1716–1826*, 35 ECON. HIST. REV. 373 (1982); S.D. CHAPMAN, THE DEVON CLOTH INDUSTRY IN THE EIGHTEENTH CENTURY 23 (1978).

the insurance industry continued to act as a risk-hedging mechanism supporting the advance of machinery into our commercial markets.[48]

Insurance carriers collected new information and rapidly adjusted their premiums without changing their underlying policy, enabling extensive protection as factories grew and machines became an integral part of mass production.[49] Insurers suffered losses at the beginning of this process, given the discrepancy between the premiums they charged and the losses they were obligated to pay or indemnify.[50] Considering the new information insurance carriers accumulated and their incentive to generate profit by minimizing losses, their underwriting practice nudged their insureds to create safer infrastructures, for instance, by determining "the material and design of a mill, warehouse or workshop construction."[51]

In these two examples, insurers significantly impacted the safety of emerging industries, from their infrastructure to their actual practice.[52] The abovementioned alignment of interests between insurance carriers and policyholders led insurers to proactively find and implement methods to reduce risks associated with innovation. This is also true today, and this paper further establishes this from an empirical perspective concerning the burgeoning field of AI technology.

Before delving into the empirical insights detailed below, it is important to note that insurance, as an industry, as well as the products it offers, are in no way perfect. They are not a panacea to the risks associated with AI. Though this paper tends to be optimistic when it comes to the intersection of insurance and AI, insurance has many drawbacks, including moral hazard risks, regulatory capture, and adverse selection.[53] Despite these deficiencies

48. Rowell v. Railroad, 57 N.H. 132, 139 (1876) ("There is no doubt that one of the objects of insurance against fire is to guard against the negligence of servants and others; and therefore the simple fact of negligence has never been held to constitute a defence.").

49. *Id.*

50. Robin Pearson, *Fire Insurance and the British Textile Industries During the Industrial Revolution*, 34 BUS. HIST. 1, 4 (1992) ("From the 1790s textiles proved increasingly troublesome for the metropolitan insurers. Frequent mill and warehouse fires meant that often premiums failed to cover losses. The extension of some manufacturing activities into cotton warehouses, the increasing size and density of industrial plant in urban locations, and the expansion of multiple occupation, all complicated the underwriting of textile risks.").

51. *Id.* at 2.

52. Such was the case with regards to the then-booming textile industry during the Industrial Revolution. *Id*. at 8.

53. On which I have elaborated elsewhere, see Anat Lior, *Innovating Liability: The Virtuous Cycle of Torts, Technology and Liability Insurance*, 25 YALE J.L. & TECH. 448, 491 (2023).

and the embedded limitations of the insurance industry, this paper maintains the position that insurance has an important role in supporting, encouraging, and ensuring the safe integration of new technologies into our society, even if it is limited at times. Furthermore, given the lack of current AI regulatory clarity, insurance is invaluable in the upcoming implementation of AI into our lives. This does not disregard the inherent flaws this industry has, but its imperfection might be useful as AI regulation and litigation continue to advance slowly.

III. THE CURRENT SUGGESTED AI-SPECIFIC POLICIES

Several companies and start-ups in the insurance industry are currently focusing on the AI sphere, offering various products and coverage for AI-related activities. This paper has identified a few ongoing undertakings in this field and will describe each in this chapter. These are Munich Re's aiSure™, Armilla AI, Vouch, CoverYourAI, Relm Insurance, Aishelter, and Testudo.

Munich RE, the first major player to offer coverage for AI activities, created its first AI product in 2018 due to consumer demand.[54] As described by Iris Devriese,[55] AI Liability Lead North America at Munich Re, a company that developed an AI solution approached Munich Re as they were having difficulties convincing their customers about the safety and capabilities of AI.[56] They were looking for performance-guarantee coverage to back up their product. Munich Re decided to underwrite this product and wanted to scale it out.[57] This meant that if the product did not live up to its promise, Munich Re would have to finance the guarantee made by the AI company. This emphasizes how trust can be created through the mere existence of insurance, driving innovation and growth. The need for AI coverage came from the market, which led to creating an AI insurance team at Munich Re.

Munich RE offers three versions of AI insurance via its aiSure™ product. The first type of coverage (aiSure™ – Contractual Liabilities) protects corporations using AI, where Munich Re guarantees a certain performance-threshold delivered by an AI vendor, its policyholder.[58] This product

54. *Insure AI*, MUNICH RE, www.munichre.com/en/solutions/for-industry-clients/insure-ai.html; Sharon Moran, *AI Regulation and Risk Management in 2024 – with Micheal Berger of Munich Re*, EMERJ, emerj.com/ai-regulation-and-risk-management-in-2024-micheal-berger-munich-re/ (last updated Feb. 17, 2025).

55. Zoom Interview with Iris Devriese, AI Liability Lead North America, Munich Re (Jul. 10, 2024).

56. *Id.*

57. *Id.*

58. MUNICH RE, INSURING GENERATIVE AI: RISKS AND MITIGATION STRATEGIES 10 (2024),

covers AI solutions or contractual performance-guarantees an AI vendor provides to a corporation using their AI.[59] For example, a cybersecurity AI provider guarantees that their AI will block certain malware types, or a GenAI provider announces copyright infringement guarantees, similar to the course OpenAI is taking.[60] In this case, Munich Re will financially back up these guarantees.

The second type of coverage (aiSure™ – Own Damages) is a direct policy between Munich Re and a corporation using AI that they built themselves for their own use as a third-party policy.[61] For example, if a bank uses AI to evaluate a property for mortgage processing and that AI makes an error, such as overestimating the property, the bank using it is covered by the Munich Re policy. This policy also applies to GenAI products that are used by corporations.[62]

Lastly, aiSure™ – Own Damages can also include liability coverage to address new third-party risks.[63] It protects corporations using AI from lawsuits from affected individuals, such as consumers.[64] For example, hospitals and banks using AI to improve their services might be sued for discrimination. The same can happen with GenAI, when corporations may use misleading, harmful, or false data to make decisions. These may lead to fines or lawsuits, which are covered by this third type of product.

Hartford-HSB, a Munich Re company, is also offering AI products to companies that are developing and using this technology. Most recently, this includes WINT (Water Intelligence Technology), which uses AI to detect water leaks and damages in construction, commercial, and industrial locations.[65] HSB's coverage combines a more traditional property policy with an innovative AI coverage component, guaranteeing the performance of WINT's

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https://www.munichre.com/content/dam/munichre/contentlounge/website-pieces/documents/MR_AI-Whitepaper-Insuring-Generative-AI.pdf/_jcr_content/renditions/original./MR_AI-Whitepaper-Insuring-Generative-AI.pdf (last visited Mar. 27, 2025).

59. *Id.*

60. Kyle Wiggers, *OpenAI Promises to Defend Business Customers Against Copyright Claims*, TECHCRUNCH (Nov. 6, 2023, 10:15 AM), techcrunch.com/2023/11/06/openai-promises-to-defend-business-customers-against-copyright-claims/.

61. MUNICH RE, supra note 58.

62. *Id.*

63. *Id.* at 10–11.

64. *Id.*

65. Press Release, Munich Re, HSB Adds WINT Water Intelligence Technology To Water Leak Detection Portfolio, HSB (Jun. 24, 2024), www.munichre.com/hsb/en/press-and-publications/press-releases/2024/2024-06-24-wint-water-intelligence-technology-leak-detection.html.

technology. WINT's then Head of Global Insurance, Shkya Ghanbarian, stated that their partnership with HSB, which offers performance warranties, is the first of its kind in the leakage detection market. [66] Furthermore, HSB partners with WINT and offers the latter's technology as an incentive mechanism for HSB's policyholders to mitigate potential risks. Ghanbarian stated that there are many stakeholders depending on these AI technologies, such as the one offered by WINT, and they enable tech companies to minimize risks for the benefit of both the policyholder and the insurance provider.[67] "Given that there are always risks," Ghanbarian continues, "purchasing AI policies seems like the next logical step in this industry."[68]

Armilla AI, a Toronto-based start-up, offers an AI liability insurance product and a product warranty backed up by reinsurers, including Swiss Re, Greenlight Re, and Chaucer.[69] This warranty ensures that the AI models will operate in the way their sellers guarantee.[70] The company relies on eight dimensions to evaluate the risk of each AI model and offers a premium to a policy covering any potential model failures.[71] These dimensions include the training data the AI model used, the entity that created the model, testing performance, and methods of usage by customers.[72] When the AI model fails, Armilla reimburses the customer of the model up to the amount the customer paid for licensing fees to the AI vendor.[73] The collected premium for the policy is essentially a percentage of those licensing fees, which vary for each AI model depending on its risk and complexity.[74]

Karthik Ramakrishnan, CEO and co-founder of Armilla, stated that their goal is to, "identify, mitigate, and protect" against risks associated with AI technology.[75] Working in the AI industry for more than a decade before co-founding Armilla, Karthik stated that the biggest pushback he received

66. Zoom Interview with Shkya Ghanbarian, Head of Global Insurance, WINT (Sep. 12, 2024).

67. *Id.*

68. *Id.*

69. *Solutions for AI Assessment & Risk Transfer*, ARMILLA, www.armilla.ai/solutions (last visited Mar. 26, 2025).

70. *Id.*

71. Belle Lin, *Is Your AI Model Going Off the Rails? There May Be an Insurance Policy for That*, THE WALL STREET JOURNAL (Oct. 2, 2023), www.wsj.com/articles/is-your-ai-model-going-off-the-rails-there-may-be-an-insurance-policy-for-that-adf012d7.

72. *Id.*

73. *Id.*

74. *Id.*

75. Zoom Interview with Karthik Ramakrishnan, CEO & Co-Founder, Armilla AI (Jul. 15, 2024).

from potential clients was that the technology is built on a probabilistic system, meaning there is always a level of error.[76] This means that the nature of software is fundamentally changing. This is an essential part of our conversation about insurance. He stated that traditional policies were built for absolute worlds with a solid understanding of their projection.[77] However, as we move to AI, the software is different, and so is the level of uncertainty. This led him to establish Armilla and focus on creating a model to quantify the risk.[78] Armilla identifies where the risks are and provides coverage specifically for the possible error emanating from the underperformance of the AI model.[79] He claims, "the risks are not new, but their source is." This leads the insurance industry to rethink the products it offers. Daniel Woods, a senior security researcher at Coalition, also expressed this notion by stating that there are, "marginal developments in threat actor behaviour, but not fundamental changes in cyber risk."[80] This approach aligns with that of Lauren Finnis, Consulting Leader – Commercial P&C and Specialty Insurance, from WTW. She states that to manage novel risks, we should, "apply the same traditional risk management lens that we have used in the past."[81] This is because the fundamental principles of risk management remain the same, even if the risks seem new or unfamiliar.

Vouch is a US-based business insurance company with a designated AI insurance program that launched in February 2024.[82] Their AI insurance product aims to cover AI start-ups for their financial losses resulting from lawsuits related to their products or services.[83] Vouch AI provides affirmative coverage for various risks, including AI Error & Omissions (E&O), bias and discrimination, IP infringement claims, and regulatory investigations.[84] The latter refers to providing defense cost coverage for AI-specific regulation. In quotes published online, Sophie McNaught, the director of AI at Vouch, and

76. *Id.*

77. *Id.*

78. *Id.*

79. *Id.*

80. Zoom interview with Daniel Woods, Senior Security Researcher, Coalition (Aug. 13, 2024).

81. R&I Editorial Team, *WTW's Lauren Finnis Discusses the Evolution and Future of Commercial Insurance*, RISK & INS. (May 6, 2024), riskandinsurance.com/wtws-lauren-finnis-discusses-the-evolution-and-future-of-commercial-insurance/.

82. Jack Willard, *Vouch Launches Novel Insurance Product to Help AI Startups Innovate Faster*, REINSURANCE NEWS (Feb. 12, 2024), www.reinsurancene.ws/vouch-launches-novel-insurance-product-to-help-ai-startups-innovate-faster/.

83. *Id.*

84. *Id.*

John Wallace, the Chief Insurance Officer at Vouch, strike a clear tune in helping innovation and supporting start-ups in the AI field. McNaught stated, "Vouch's AI Insurance is a critical financial backstop that helps AI startups innovate boldly and survive challenges."[85] Wallace stated, "we knew the AI industry couldn't afford to wait the years it typically takes insurance to catch up."[86] Vouch's AI insurance website claims to cover more than 500 AI start-ups. It also states that several key factors are considered in determining AI insurance premiums, including, "the nature and scope of the AI technology used, the industry in which your startup operates, the size of your company, and your company's claim history."[87]

CoverYourAI is a use-case-specific policy covering business interruption resulting from a B2B relationship.[88] They offer a first-party policy purchased by a vendor of AI technology and paid to businesses that suffered losses connected with business interruption resulting from said AI.[89] An example provided by the co-founder of CoverYourAI, Josh Fourie, illustrates this business model.[90] Corporation X provides an autonomous vehicle (AV) to Corporation Y, a mining company that uses it for its work. The AV slows down due to weather conditions and then speeds up to compensate for lost time, hitting a different vehicle and leading to shipment delays. CoverYourAI policy will pay for said delays (i.e., the business interruption) directly to the mining company.[91] The policy does not currently offer coverage for bodily or property damages, nor does it cover litigation costs. The interesting approach of this company, as will be elaborated below, is that its underwriting process is not focused on historical data similar to traditional insurance but on case-specific instances and models focused on prediction estimations (i.e., risk profile) and the value provided by the specific AI vendor.[92]

Relm Insurance (Relm), a Bermuda-domiciled specialty insurance carrier serving innovative and emerging industries,[93] announced three AI-

85. Vouch, *AI Startups Move Faster With "AI Insurance", First-of-its-Kind Coverage for New AI Risks*, PR NEWSWIRE (Jan. 30, 2024), www.prnewswire.com/news-releases/ai-startups-move-faster-with-ai-insurance-first-of-its-kind-coverage-for-new-ai-risks-302047320.html.

86. *Id.*

87. *See* Vouch, www.vouch.us/coverages/ai-insurance (last visited Apr. 16, 2025).

88. *CoverYourAI*, coveryourai.com/ (last visited Apr. 16, 2025).

89. *Id.*

90. Zoom Interview with Josh Fourie, Co-Founder, CoverYourAI (Jul. 12, 2024).

91. *Id.*

92. *Defining, Deriving & Quantifying AI Risk*, DECODED.AI, decoded.ai/.

93. Relm Insurance, relminsurance.com/ (last visited Mar. 14, 2025); Gia Snape, *Relm CEO on Insuring the 'Next Economic Frontiers' – AI and Space*, INS.

specific policies in January 2025.[94] Relm presents its AI products as, "designed to provide tailored coverage for the dynamic companies creating and adopting AI technology."[95] The first product is NOVAAI, built as a cyber and Tech E&O policy aimed at AI platform companies and, "AI-based product and service companies who have a liability and cyber security exposure due to the AI software they are developing and selling."[96] The second product is PONTAAI, an Excess Difference in Conditions (DIC) wrap policy aimed at "organizations with third-party liability exposure due to their AI use or development, but whose existing liability programs may exclude AI."[97] A DIC refers to a type of policy that acts as an additional layer of coverage on top of existing primary policies. These are specifically designed to cover perils and risks that could be excluded or partially covered by traditional policies[98] and could be of great value in the AI risk landscape. The last product Relm offers is RESCAAI, a first-party response policy protecting against risks the policyholder faces. This product is aimed at "organizations that use third party AI for business operations" and "organizations that embed third-party AI solutions within their own products."[99] This third product will cover, among other things, harm resulting from business interruption, reputational harm, product recall expenses, and incident response costs.[100] According to Claire Davey, Head of Product Innovation and Emerging Risk at Relm, both NOVAAI and PONTAAI affirmatively cover intellectual property infringement (focusing on copyright and trademark) and discrimination, which offers added value to policyholders who are looking to manage their AI risks.[101]

BUS. (Jan. 20, 2025), www.insurancebusinessmag.com/us/news/breaking-news/relm-ceo-on-insuring-the-next-economic-frontiers—ai-and-space-521283.aspx.

94. *Relm Insurance Launches AI Liability Solutions to Address Emerging Risks in the AI Ecosystem*, RELM INS. (Jan. 14, 2025), relminsurance.com/relm-insurance-launches-ai-suite/.

95. *Id.*

96. *Id.*

97. *Id.*

98. *Additional Information*, IRMI , www.irmi.com/term/insurance-definitions/difference-in-conditions-insurance.

99. *Relm Insurance*, supra note 93.

99. *Id.*

100. *Id.*

101. Zoom Interview with Claire Davey, Head of Product Innovation and Emerging Risk, Relm Ins. (Feb. 4, 2025).

Lastly, *AiShelter*,[102] and *Testudo*[103] are two start-up companies operating in this field that do not offer products to the public yet. They are currently focused on product development and research in the US and UK, respectively. AiShelter is looking to be the first provider of individual AI liability insurance policies specifically geared for end users of AI systems. AiShelter also aims to provide AI liability coverage to businesses that either develop or deploy AI systems.[104] Testudo leverages proprietary data and risk analytics technology to enable companies to pinpoint and manage emerging AI liability exposures. By combining their proprietary data with risk analytics technology and insurance capacity, "Testudo offers enterprises a seamless route to adopting AI technologies confidently and responsibly."[105]

Other insurance companies have discussed AI coverage, mostly focusing on utilizing existing traditional policies to address risks associated with AI. In their publication aimed at AI startups, Founder Shield focuses on operational continuity and investor confidence as explanations for the importance of insurance for AI. They provide E&O, Cyber liability, and Product liability as existing general coverage and policies for AI. The publication refers to Tech E&O, D&O, and IP policies as AI-specific coverage. This division of general AI coverage and specific AI coverage could be disputed, given the ongoing rise of AI-specific coverage. Still, this division seems reasonable if one considers AI's current usage in the corporate world and sees AI as a form of software/technology covered via existing policies.

Another example is Koop Insurance, which presents itself as a compliance and insurance platform for tech and has also discussed insuring AI.[106] In their publication, Koop Insurance states, "traditional insurance policies were not designed with AI's unique risks in mind, leading to gaps in coverage."[107] They give examples of data breaches and cybersecurity threats, AI bias and ethical issues, autonomous system failures, and IP risks as harms that might not be covered by standard policies. Like Founder Shield, they do not discuss or offer AI-specific policies but only start to tease out the meaning of AI risks in the evolving landscape of insurance and AI risks.[108]

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102. AiShelter, www.aishelter.com/ (last visited Mar. 14, 2025).

103. Testudo, www.testudo.co/ (the author is a consultant of Testudo).

104. Zoom interview with Jeremy Carr, CEO, AiShelter (Jul. 3, 2024).

105. Zoom interview with George Lewin-Smith & Mark Titmarsh, *supra* note 17.

106. *How Do You Insure AI?*, KOOP INS. (Feb. 29, 2024), www.koop.ai/blog/how-do-you-insure-ai.

107. *Id.*

108. For more on the traditional policies and their applicability to AI, see Chapter V.

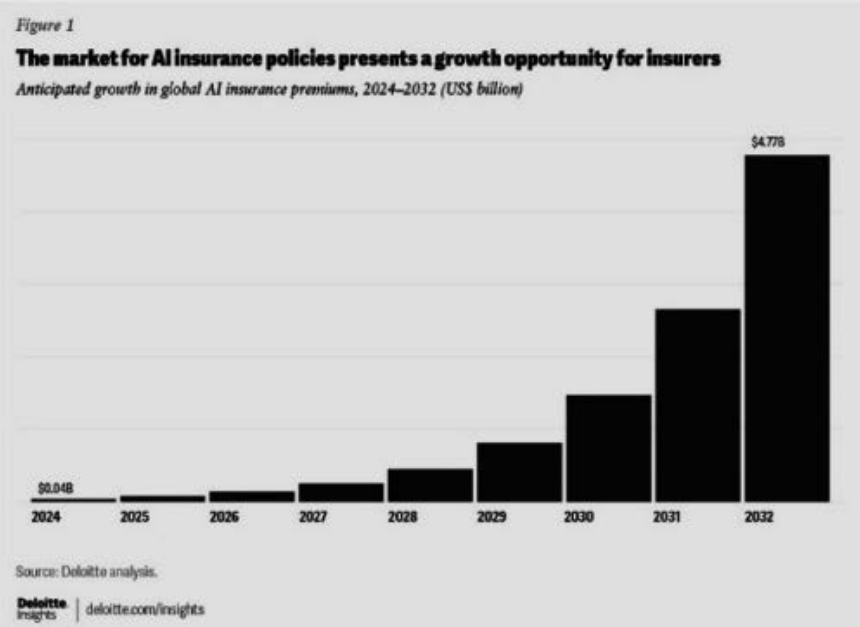
On top of the above companies operating in this unique intersection, the underlying conversation about offering insurance to cover AI activities has significantly increased in the last couple of years.[109] This includes discussions regarding the creation of a specialized market and the need for it as AI continues to grow.[110] Deloitte sees great potential in the market of insurance for AI, calling it a "blue ocean opportunity."[111] It forecasts that by 2032, insurers could potentially generate approximately $4.7 billion in annual global AI insurance premiums, with a compounded annual growth rate of around 80%.[112] This is an unparalleled opportunity for all the stakeholders involved, and there is a strong incentive to ensure that insurance will be proactive rather than reactive in this field. Insurance companies are already taking the lead in AI liability, not waiting for the legislators and courts to set up the standards while closely monitoring them for any legal developments.

109. *See, e.g.*, Sergio Padilla, *Businesses Want Insurance for AI Risks, but Insurers Are Still Figuring Out How to Offer It*, INC. (Jun. 14, 2024), www.inc.com/sergio-padilla/businesses-want-insurance-for-ai-risks-but-insurers-are-still-figuring-out-how-to-offer-it.html; Sean Shecter, *Insuring Against AI Risk: How Coverage Will Evolve (Feat. Ashley Bennett Jones & Logan Payne) (Podcast)*, MONDAQ (Feb. 6, 2024), www.mondaq.com/unitedstates/new-technology/1549006/insuring-against-ai-risk-how-coverage-will-evolve-feat-ashley-bennett-jones-logan-payne-podcast.

110. Russ Banham, *AI Insurance Takes a Step Toward Becoming a Market*, CARRIER MGMT. (Nov. 28, 2022), www.carriermanagement.com/features/2022/11/28/242708.htm?bypass=e3a499e2a59c457bbaeb794a2ae30c46.

111. Sandee Suhrada, Kate Schmidt & Dishank Jain, *Providing Insurance Coverage for Artificial Intelligence May Be a Blue Ocean Opportunity*, DELOITTE (May 29, 2024), www2.deloitte.com/us/en/insights/industry/financial-services/financial-services-industry-predictions/2024/risk-insurance-for-ai.html#endnote-20.

112. *Id.* (Figure 1 is taken from this report).



It is also important to mention the Lloyd's of London re-insurance market. Lloyd's will hold an integral place in AI coverage development. Lloyd's is a re-insurance market, and it is the world's largest marketplace for specialist risks.[113] It is not an insurance company but rather a marketplace with different groups of underwriters who offer insurance to Lloyd's brokers, known as syndicates.[114] A customer will approach a Lloyd's broker, who will approach different syndicates to underwrite a specific risk and eventually return to the customer with the best offer.[115] At Lloyd's, risks are allocated by risk codes; the most relevant to AI is ICX, which is labeled as "innovation risk."[116] ICX currently represents 5% of Lloyds' overall market gross written

113. *Our Market*, LLOYD'S, www.lloyds.com/about-lloyds/our-market.

114. *Syndicate*, LLOYD'S, www.lloyds.com/join-lloyds-market/underwriter/syndicate.

115. PropertyCasualty360, *Inside Lloyd's: Demystifying the Inner Workings of the World's Most Famous Insurance Market*, YOUTUBE (Sep. 29, 2016), www.youtube.com/watch?v=ugRFJv_93ZU&t=158s.

116. *Innovation ICX*, LLOYD'S, www.lloyds.com/news-and-insights/lloyds-lab/programmes-and-initiatives/icx (last visited Apr. 16, 2025).

premium,[117] a 3% increase since 2023.[118] This represents a steady trend of Lloyds' position in supporting innovative risks, especially AI. Lloyd's also operates a lab focused on innovation in the insurance market,[119] and indeed, two of the alumni of this lab are the above-mentioned companies Armilla AI,[120] and CoverYourAI.[121] Lloyd's of London has a critical role in offering coverage for new technologies and supporting new and existing insurance companies operating in this field.[122] It also has a proven track record of supporting an innovative insurance market in the crypto, drones, cyber, and space fields. It is highly likely that it will also have an essential role in covering AI, starting with GenAI and agentic AI services.[123]

IV. "SILENT AI" AND THE HISTORY OF CYBER-INSURANCE

The risk landscape presented by AI constantly evolves and changes as this technology continues to be developed, sold, and licensed for individuals and companies. This change in the risks associated with AI technology will profoundly impact the insurance industry. It will expose gaps in the

117. *Innovation ICX: Guidance on the 5% Innovation ICX Class*, LLOYD'S, (May 16, 2024), assets.lloyds.com/media/1377bbe7-b5dc-4520-ae67-5f125f0177ab/Innovation%20ICX%20Class%20Guidance%20-%20May%202024%205%20percent.pdf.

118. *Innovation ICX: Guidance on the 2% Innovation ICX Class*, LLOYD'S, (Jul. 25, 2023), assets.lloyds.com/media/aaac1223-fae3-452e-ae28-978e42587aba/Innovation%20ICX%20Class%20Guidance%20-%20September%202023.pdf.

119. *Welcome to Lloyd's Lab*, LLOYD'S, www.lloyds.com/news-and-insights/lloyds-lab.

120. *Armilla AI*, LLOYD'S, www.lloyds.com/news-and-insights/lloyds-lab/insurtech/lloyds-lab-accelerator/alumni/armilla-ai ("Armilla AI focuses on AI assurance and risk management. Its capabilities include evaluating AI model performance, AI audits and due diligence. Armilla AI currently works with AI vendors and enterprises to guarantee the quality of their AI products and mitigate risks and is looking to become an MGA to offer insurance products covering AI risks.").

121. *CoverYourAI*, LLOYD'S, www.lloyds.com/news-and-insights/lloyds-lab/insurtech/lloyds-lab-accelerator/alumni/cover-your-ai ("CoverYourAI helps enterprise teams leverage AI through their dynamically-priced, parametric product protection plan embedded at the checkout. They close the AI adoption gap by making AI risk transferable so that coverholders can achieve more with AI.").

122. *Technology*, LLOYD'S, www.lloyds.com/news-and-insights/risk-reports/library/technology ("Innovation and expanding access are transforming the role of technology in society, and insurance has a key role to play in enabling effective risk management.").

123. Zoom Interview with Mark Titmarsh, CPO and Co-Founder, Testudo (Dec. 17, 2024) ("Everything that is weird and wonderful could be insured at Loyd.").

current liability policies offered to the public and raise complex issues of "silent AI" coverage that insurers did not mean to cover.[124] "Silent coverage" or "non-affirmative coverage" refers to a situation where a traditional insurance policy does not explicitly state if it covers or excludes specific types of risks. This creates uncertainty for both policyholders and insurers. The term was popularized when cyber insurance emerged in response to "silent cyber" coverage.[125] "Silent AI" presents similar challenges as stakeholders try to understand the scope of policies that are already in place and might cover AI risks and accidents.[126]

When discussing the development of an AI coverage product, many consider the intuitive comparison of its development and future trajectory to the history of cyber insurance.[127] A white paper by Munich Re stated, "if we continue drawing this parallel into the future, the emergence of a standardized AI insurance market seems a likely consequence – comparable to the cyber insurance market."[128] Munich Re predicts that, similar to cyber losses and risks, AI-related losses will increase, leading risk managers, brokers, and insurance carriers to think about AI risks more systemically and strategically.[129] Similar to cyber risks, AI risks will also be excluded from traditional policies, given correlated risks and "silent AI" exposure. Furthermore, regulatory landscapes, led by the current EU AI Act initiative, could direct businesses to follow evolving guidelines and adopt responsible AI practices, similar to what happened in cyber insurance and the General Data Protection Regulation

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124. Rayne Morgan, *'Silent AI': Consulting Firm Alerts Insurers about Risks*, INS. NEWSNET (Aug. 27, 2024), insurancenewsnet.com/innarticle/silent-ai-consulting-firm-alerts-insurers-about-risks. *See also* Chapter IV.

125. *See, e.g.*, *The Noise About "Silent Cyber" Insurance Coverage*, COVINGTON (Jan. 14, 2020), www.cov.com/-/media/files/corporate/publications/2020/01/the-noise-about-silent-cyber-insurance-coverage.pdf; Catherine L Trischan, *End of Silent Cyber in Property Insurance*, IRMI (Jan. 19, 2024), www.irmi.com/articles/expert-commentary/end-of-silent-cyber-in-property-insurance.

126. Sonar, *AI – Unintended Insurance Impacts and Lessons from "Silent Cyber"*, SWISS RE (Jun. 12, 2024), www.swissre.com/institute/research/sonar/sonar2024/ai-silent-cyber.html ("With silent AI, it is time to prevent repetition of the same mistakes by understanding which risks traditional policies already (silently) cover.").

127. See Padilla, *supra* note 109 ("Like cyber insurers in the late 1990s, insurance companies today are figuring out how to determine risk for artificial intelligence and set prices.").

128. IRIS DEVRIESE & MIKE CROWL, MUNICH RE, MIND THE GAP: A US-FOCUSED ANALYSIS OF AI LIABILITY RISKS AND THE IMPLICATIONS FOR INSURANCE 22 (2024), www.munichre.com/en/solutions/for-industry-clients/insure-ai/ai-white-paper.html.

129. *Id.*

(GDPR).[130] Munich Re concludes by stating that once the regulatory landscape becomes more clearly defined, the market in the AI sphere will move into the compliance phase and develop standards that align with the set regulatory norms, similar to the history of cyber insurance.[131] Once these are in place, the underwriting processes are simplified, indicating a transition towards "an informed, standardized market practice, echoing the journey of other established insurance sectors."[132]

However, not all stakeholders in the industry share this prediction. Many underwriters in tech-oriented insurance companies believe that the risks associated with AI are not similar enough to those presented by cyber risks with the emergence of the Internet and the Cloud in the 2000s. The different nature of the underlying technology and AI's wide scope of application lead people in the insurance industry to believe that, with some adjustment, traditional policies should be sufficient to tackle the uncertainty brought about by AI technology. However, there is overall agreement between those who think that AI coverage will imitate cyber coverage and those who do not that the pace should be much faster than it was in the cyber insurance context. This is because AI technology progresses and is being developed at a higher speed, and the demand for risk-hedging mechanisms is much more evident.[133] Still, the adversaries claim this does not necessarily mean a specialized market is the best approach for the insurance industry.

Josh Fourie, co-founder of CoverYourAI, stated that there is a great resemblance between cyber insurance and the way AI coverage is currently being developed.[134] He cautions that we need to learn from the "early arrogance of data" surrounding cyber insurance policies when they were first offered commercially.[135] With cyber insurance, there was a substantial underestimation of risks associated with cyber activities, such as ransomware attacks, that were not considered at the early age of cyber insurance.[136] The opposite trend is apparent in the AI context. Insurance companies overestimate the risks associated with AI, leading to policies that might not

130. Arjun Dhar, *Deciphering the Insurability of GDPR Fines*, STEWARTS (May 28, 2024), https://www.stewartslaw.com/news/deciphering-the-insurability-of-gdpr-fines/.

131. Devriese & Crowl, *supra* note 128.

132. *Id.*

133. Anand S. Rao & Marie Carr, *Is AI Risk Insurance the Next Cyber for Insurers?*, CARRIER MGMT. (Jun. 6, 2023), www.carriermanagement.com/features/2023/06/06/249172.htm.

134. Zoom Interview with Josh Fourie, *supra* note 90.

135. *Id.*

136. *Id.*

significantly contribute to the policyholder's risk management strategy.[137] Policies covering AI should move fast, as the technology itself is fast developing. However, this shift should not be done recklessly, as there is potential for policies developed in the coming years to be irrelevant, misleading, and inadequate to AI's risk landscape.

Karthik from Armilla AI agrees with this overall approach.[138] He reflects on the lessons learned from cyber insurance and cyber security, striving to achieve *clarity* in what is covered and what is not covered regarding AI activities.[139] Eliminating "silent AI" coverage is key, as Armilla is creating affirmative policies to combat this phenomenon, which was extremely prevalent when cyber insurance was first created.[140] Karthik claims that the cyber insurance carriers that survived in the market took a quantified approach by gathering and analyzing data to follow the harms created in cyberspace.[141] He believes that the same should apply to the AI policies market.[142]

Even though there is much to learn from previous policies and product developments within the insurance industry, specifically regarding coverage of emerging technologies, it remains unclear how similarly AI policies will evolve. This is primarily due to the unique aspects of AI technologies, both in scope and severity of risks, which fundamentally differ from previous emerging technologies. There is an opportunity, however, to learn from past mistakes in emerging technologies coverage, regardless of the potential differences between the trajectory of those insurance lines and AI-based coverages.

From a client's perspective it seems that given the existence of cyber insurance, there is no obvious or current need to create a stand-alone AI product, even for companies working with AI extensively. Exclusions of AI activities are only now slowly appearing,[143] meaning "silent AI" might be sufficient for many seeking coverage for their AI-related activities. The clients' perspective seems different from those of insurance companies working on

137. *Id.*

138. Zoom Interview with Karthik Ramakrishnan, *supra* note 75.

139. *Id.*

140. *Id.*

141. *Id.*

142. *Id.*

143. Michael S. Levine & Alex D. Pappas, *Understanding Artificial Intelligence (AI) Risks and Insurance: Insights from A.F. v. Character Technologies*, NATI'L L. REV. (Jan. 6, 2025), natlawreview.com/article/understanding-artificial-intelligence-ai-risks-and-insurance-insights-af-v ("Conversely, some insurers like Hamilton Select Insurance and Philadelphia Indemnity Company are introducing AI-specific exclusions that may serve to widen coverage gaps. These evolving dynamics make it prudent for businesses to review their insurance programs holistically to identify potential uninsured risks.").

AI products. Unsurprisingly, individuals from the cyber insurance industry share the sentiment that AI products will not be necessary in the near future. Those three groups—cyber insurance providers, AI insurance providers, and potential clients—have different incentives for creating, offering, and purchasing new types of insurance products, leading to different approaches regarding the future evolution of AI vis-à-vis cyber policies. The appetite of the specific insurer may also vary, with more conservative insurance companies preferring to stick to traditional coverages and not challenge the industry's status quo opposite to start-ups which are dedicated to the innovation of AI insurance lines. While no definitive conclusion can be drawn today about the future of the industry, distinct AI insurance lines are already emerging. It is appealing to at least some, similar to previous new products that entered the insurance market.

With regards to "silent AI", the Head of North America Cyber and E&O at WTW foresees that the insurance industry will eventually see enough claims to resolve this issue.[144] They claim that because ambiguity driven by "silent AI" works in favor of the insureds, the insurers will drive contractual reform in policies with the potential to cover AI to help protect their possible exposure.[145] They believe that this will be done within the scope of existing policies, in particular Tech E&O policies.[146]

Regarding legislation, Woods of Coalition noted that regulators could have a role in clarifying the "silent AI" challenge.[147] Regulators could affirmatively "provide some guidance on what AI insurance is" and the distinction between traditional policies like Commercial General Liability (CGL) and novel technology insurance policies, namely cyber insurance and Tech E&O.[148] Otherwise, there is a good chance that startups in this field would present their policies in an arguably irresponsible way to their potential clients. This could also include important clarifications about "silent AI" coverage in the context of employment practice liability (EPL) policies,

144. Zoom interview with Head of North America Cyber and E&O, WTW (Sep. 16, 2024).

145. *Id.*

146. *Id.* They further clarify that "because AI is typically silent in today's Cyber policies, I don't anticipate carriers moving to affirm coverage. Email from Head of North America Cyber and E&O, WTW, to author (Feb. 17, 2025) (on file with author). It's included in the definition of cyber incident – computer systems given AI is a part of an insured's IT infrastructure. *Id.* Where we will more likely see policy language revision are other coverage parts such as Media or Crime to ensure the intention of the policy is clear." *Id.*

147. Zoom interview with Daniel Woods, *supra* note 80.

148. *Id.*149.Zoom Interview with Lauren Finnis, head of Commercial Lines Insurance Consulting & Technology, WTW (Jul. 25, 2024).

discrimination coverage, and General Liability policies. The next Chapter delves into these traditional policies and their utility in the AI context.

V. THE TRADITIONAL LIABILITY POLICIES

In her interview, Lauren Finnis from WTW stated that she believes it is unnecessary to have a specific AI insurance policy in place, and that current gaps can be filled with existing policies and models with some customization of the policies' language.[149] She emphasizes that AI is very difficult to define, and so, "carving it out of existing coverage or carving it into existing coverage, is going to be terribly challenging."[150] The present market path seems to adhere to traditional policies, and a better understanding of these policies is crucial to enable this process.

On top of cyber insurance, various liability policies are currently being discussed as potentially covering some parts of the different risks associated with AI, but presumably not all of them.[151] This part will describe 12 of these policies and the potential gaps they may leave in the AI context.[152] There are other types of policies that were excluded from the below review, such as terrorism and kidnap & ransom policies,[153] that might still be proven relevant in the future but currently hold less of a stake in the AI context.

1. Cyber Insurance

Currently, the combination of cyber insurance and the below policy, Tech E&O, seems to be the main avenue for obtaining coverage for AI-related activities and risks, focusing on harms such as network security breaches, ransomware attacks, and data privacy violations. When AI exploits software vulnerabilities, cyber insurance is the appropriate product on the defenders' side

149. Zoom Interview with Lauren Finnis, head of Commercial Lines Insurance Consulting & Technology, WTW (Jul. 25, 2024).

150. *Id.*

151. Sonar, *supra* note 126 ("It is unlikely that a single insurance policy will cover all potential risks that AI presents. As of today, AI risks are neither explicitly mentioned, limited nor excluded in policy language, and different exposures may be covered by different policies already in existence.").

152. Jonathan D. Bick, *Improving Solutions to AI-Related Difficulties*, 50 RUTGERS COMPUT. & TECH. L.J. 159, 198–200 (2024) ("Business solutions to resolve Al difficulties eliminate or ameliorate adverse outcomes by providing for compensation from third parties. One such solution is insurance." *Id*. at 198).

153. *See, e.g.*, Michelle E. Boardman, *Known Unknowns: The Illusion of Terrorism Insurance*, 93 GEO. L.J. 783 (2005); Sheri Merkling & Elaine Davis, *Kidnap & Ransom Insurance: A Rapidly Growing Benefit*, COMP. & BENEFITS REV., Nov.–Dec. 2001.

to cover the costs of breach notifications, credit monitoring, and legal fees associated with managing these incidents. This policy could be relevant if AI results in privacy breaches or digital threats. There could still be gaps in this policy in scenarios involving AI. Munich Re provides an example in their whitepaper stating that this policy usually requires "failure of a technology product or service."[154] If the product or service is facing systematic AI failures, fulfilling this requirement and receiving coverage would be rather straightforward. However, a one-off incident that does not amount to a "failure" in the tech itself could lead to uncovered economic loss under this policy.[155]

Issues of data privacy and leakage have slightly morphed in scope and nature, given the high usage of GenAI by commercial businesses. A long line of companies in the US have banned their employees from using ChatGPT within the scope of their employment and are currently opting to use in-house GenAI tools tailored to their needs.[156] A good case in point is the Samsung leak in April 2023, where an employee uploaded sensitive source code into ChatGPT seeking solutions to an operational problem.[157] Given the open nature of OpenAI's platform, which runs ChatGPT, the sensitive code was discoverable to anyone else who used this platform.[158] This is one example of various Samsung-related incidents in which employees unknowingly leaked trade secrets, presenting the wide scope of AI risk exposure when employees are unaware of the potential harm of their actions.[159]

A traditional cyber policy provides data privacy coverage for third parties who are harmed by the leakage, such as customers. If a customer sues the policyholder for an unauthorized disclosure of personally identifiable

154. Devriese & Crowl, *supra note* 128, at 17.

155. *Id.*

156. *E.g.,* Siladitya Ray, Samsung *Bans ChatGPT Among Employees After Sensitive Code Leak*, FORBES (May 2, 2023), www.forbes.com/sites/siladityaray/2023/05/02/samsung-bans-chatgpt-and-other-chatbots-for-employees-after-sensitive-code-leak/?sh=6630d5f36078.

157. Joe Quinn, *Emergent AI and Potential Implications for Cyber, Tech & Media Coverages*, WTW (Nov. 9, 2023), https://www.wtwco.com/en-us/insights/2023/11/emergent-ai-and-potential-implications-for-cyber-tech-and-media-coverages.

158. *Id.*

159. Cecily Mauran, *Whoops, Samsung Workers Accidentally Leaked Trade Secrets Via ChatGPT,* MASHABLE (Apr. 6, 2023), mashable.com/article/samsung-chatgpt-leak-details ("three separate instances of Samsung employees unintentionally leaking sensitive information to ChatGPT. In one instance, an employee pasted confidential source code into the chat to check for errors. Another employee shared code with ChatGPT and 'requested code optimization.' A third, shared a recording of a meeting to convert into notes for a presentation. That information is now out in the wild for ChatGPT to feed on.").

information, the policy will indemnify the policyholder. The Samsung cases are a bit more complex as traditional cyber policies do not usually provide first-party coverage. Here, the insured, Samsung, is responsible for the unauthorized disclosure of its own proprietary data, and a traditional cyber policy may be inadequate to make Samsung whole again.[160] This gap seems relatively straightforward to resolve via tweaks to the current language of traditional cyber policies, enabling them to cover these types of events. Thus, it is not clear that an entirely new policy would be needed to address these concerns.

Cyber policies also cover "first-party incident response costs incurred to investigate a cyber-attack, accomplish digital asset restoration, and take proactive measures such as required notifications."[161] This coverage should be invaluable when AI is involved to better understand the circumstances leading to the incident and slowly de-mystify AI's vulnerabilities. Cyber focuses on software and AI is considered software for the time being.[162] As such, it seems AI's involvement in an event triggering a traditional cyber policy will not render it uncovered.[163] Nonetheless, there is a growing consensus among stakeholders in the insurance industry that cyber insurance on its own might not be enough for protection against AI risks,[164] and indeed that, "standalone AI insurance products will be fundamentally different from cybersecurity coverage"[165] and should provide a warranty for the performance of AI that doesn't exist in current cyber policies.[166] As such, whether cyber

160. *Id*.

161. Allison R. Burke & William R. Reed, *AI Risks: Are You Covered?*, TAFT LAW (Nov. 6, 2024), https://www.taftlaw.com/news-events/law-bulletins/ai-risks-are-you-covered-2/.

162. Christine Lai & Jonathan Spring, *Software Must Be Secure by Design, and Artificial Intelligence Is No Exception*, CYBERSECURITY & INFRASTRUCTURE SEC. AGENCY (Aug. 18, 2023), https://www.cisa.gov/news-events/news/software-must-be-secure-design-and-artificial-intelligence-no-exception.

163. Some companies have even expanded their cyber policies to better tackle AI risks. *See, e.g.*, Clara Goh, *WTW Launches CyCore Asia, A New Primary Cyber Insurance Solution for Businesses in Singapore and Hong Kong*, WTW (Jan. 13, 2025), www.wtwco.com/en-ph/news/2025/01/wtw-launches-cycore-asia-a-new-primary-cyber-insurance-solution-for-businesses-in-singapore.

164. Ins. Bus. Can., *Insuring against the Threats of Artificial Intelligence*, INS. BUS. (Jan. 7, 2025), www.insurancebusinessmag.com/ca/news/cyber/insuring-against-the-threats-of-artificial-intelligence-519528.aspx.

165. Gia Snape, *Brokers Must 'Ask Hard Questions' About AI Coverage*, INS. BUS. (Feb. 3, 2025), https://www.insurancebusinessmag.com/us/news/cyber/brokers-must-ask-hard-questions-about-ai-coverage-523132.aspx.

166. Gia Snape, *Specialized AI Insurance needed as Adoption Accelerates*, INS. BUS. (Jan. 29, 2025), https://www.insurancebusinessmag.com/us/news/technology/specialized-ai-insurance-needed-as-adoption-accelerates-522520.aspx.

insurance will be adjusted to accommodate these modified risks or a new AI line of products will be required is still debatable. It involves issues of economic incentives and business strategies on top of the "silent AI" issue the insurance industry faces.

2. Tech Errors & Omissions (E&O)

Tech E&O is a third-party policy protecting companies from harm caused to their customers given an error or omission carried on by the company, "in the provision of *technology services* and *technology products*."[167] It is considered an important policy that is essential in the current coverage of AI liability. An underwriter from a large cyber insurance company has suggested that this type of policy would be the place for AI liability coverage development.[168] This policy is a sub-evolution of the traditional Error and Omission policy companies purchase today to protect themselves in professional liability cases.[169]

The above cyber insurance policy protects against data leaks, breaches, and cyberattacks. Tech E&O, on the other hand, offers businesses coverage in cases of product failures, negligence, and mistakes related to the technology being used, making it extremely appealing in the AI context. While some argue that this will be the future hub for AI liability, others claim that because it is aimed at covering negligence, a negligent occurrence must be proven to trigger this policy. This implies that the policyholder should generally be aware that an issue, malfunction, or misalignment could happen. If they are not fully aware of the potential negligence event, as might be the case given the "black box" issue, it is unclear whether this policy will cover the associated risks.[170] This creates a grey area where Tech E&O could present a variety of challenges to both insurers and insureds.[171] The discussion of the applicability and suitability of a negligence regime for AI liability, given its unpredictability and the black-box issue, is still ongoing.[172] This can create a mismatch with the existing Tech E&O policy, which is oriented around negligent behavior leading to tech-related errors and omissions.

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167. Quinn, *supra* note 157.

168. Zoom: Interview with a Chief Underwriting Officer at a large insurance company (Jun. 20, 2024).

169. *See infra* Chapter V.3.

170. Zoom: Interview with Karthik Ramakrishnan, *supra* note 75.

171. Quinn, *supra* note 157 (referring to this policy as "a crude instrument when it comes to the nuances of AI risks.").

172. *See, e.g.*, Andrew D. Selbst, *Negligence and AI's Human Users*, 100 B.U. L. REV. 1315 (2020); Omri Rachum-Twaig, *Whose Robot Is It Anyway?: Liability for Artificial-Intelligence-Based Robots*, 2020 U. ILL. L. REV. 1141 (2020).

Another possibility brought up by Woods of Coalition is the emergence of AI E&O insurance, as AI firms buy traditional tech E&O policies.[173] This would entail specialist underwriters who have a deep understanding of this technology and who only underwrite AI tech providers. This type of policy should be viewed as part of the E&O line of policies, just with a deeper expertise in the AI context. In other words, this policy will be similar to E&O and D&O policies, only applied in a specific setting of AI technology providers.

On the other hand, the Head of North America Cyber and E&O at WTW doubled down on the utility of Tech E&O policies in the AI context while echoing the sentiments of other participants from the cyber market. They said we probably will not see a designated AI policy "for years to come."[174] "The tech E&O part," they continue, "covers your hardware and software and the failures of these services to protect you from liability versus a third party."[175] They said that the claims will first have to play out for the language policy to be developed, which will take time.[176] In the cyber insurance market, there does not seem to be a need for language tweaking or creating a whole new policy, "because of how these policies are defined."[177] Even without a declaration of affirmative coverage, these policies cover AI within the gambit of data protection. Hence, the combination of both policies should be sufficient in their opinion.[178] They do predict that more AI questions will be incorporated into the underwriting process of cyber insurance and Tech E&O policies in response to the current concerns of insureds.[179] Still, at this point, "that is all it will be."[180]

3. Employment Practices Liability Insurance (EPLI)

EPLI is significant in the AI context and is vastly underexplored from a technological point of view. EPLI is a third-party policy that "covers businesses against claims by workers that their legal rights as employees of the

173. Zoom interview with Daniel Woods, *supra* note 80. This might be seen as similar in substance to what Vouch is currently offering. *See* Willard, *supra* note 82 and accompanying text.

174. Zoom interview with Head of North America Cyber and E&O, *supra* note 144.

175. *Id.*

176. *Id.*

177. *Id.*

178. *Id.*

179. *Id.*

180. *Id.*

company have been violated."[181] These include, among many others, harassment, discrimination, wrongful termination, and failure to employ or promote.[182] The probability of these trigger events occurring has increased significantly since the adoption of AI, and especially GenAI. As AI can be considered more of an "active agent" rather than a passive tool employees use, EPLI will likely be triggered when things go wrong.[183] For example, using AI for hiring, evaluating, and employment termination purposes, which is prevalent around the business market today,[184] could trigger this policy, especially when discrimination arises.

EPLI covers claims of discrimination and harassment, which is unique to this policy and of added value given the known bias and discrimination embedded into AI algorithms.[185] It also covers these claims when they are made by non-employees against a company, such as customers or job applicants, even if these allegations, "are not directly related to employment within the firm."[186] This makes EPLI essential in cases where AI causes discriminatory harm.[187] For example, if a company uses GenAI chatbots while

181. *What is Employment Practices Liability Insurance (EPLI)?*, INS. INFO. INST., www.iii.org/article/what-employment-practices-liability-insurance-epli.

182. *Id.*

183. David Agnew, *Highlighting the Urgent Need for Updated D&O and EPLI Policies Amid AI Innovations*, RISK & INS. (Nov. 1, 2024), riskandinsurance.com/highlighting-the-urgent-need-for-updated-do-and-epli-policies-amid-ai-innovations/.

184. Lee Rainie, Monica Anderson, Colleen McClain, Emily A. Vogels & Risa Gelles-Watnick, *AI in Hiring and Evaluating Workers: What Americans Think*, PEW RSCH. CTR. (Apr. 20, 2023), www.pewresearch.org/internet/2023/04/20/ai-in-hiring-and-evaluating-workers-what-americans-think/; Jack Kelly, *How Companies Are Hiring And Reportedly Firing With AI*, FORBES (Nov. 4, 2023), https://www.forbes.com/sites/jackkelly/2023/11/04/how-companies-are-hiring-and-firing-with-ai/.

185. *See, e.g.*, Solon Barocas & Andrew D. Selbst, *Big Data's Disparate Impact*, 104 CALIF. L. REV. 671 (2016); Batya Friedman & Helen Nissenbaum, *Bias in Computer Systems*, 14 ACM TRANSACTIONS ON INFO. SYS. 330 (1996); Anupam Chander, *The Racist Algorithm?*, 115 MICH. L. REV. 1023 (2017); Anya E.R. Prince & Daniel Schwarcz, *Proxy Discrimination in the Age of Artificial Intelligence and Big Data*, 105 IOWA L. REV. 1257 (2020); Kate Crawford, *The Hidden Biases of Big Data*, HARV. BUS. REV. (Apr. 1, 2013), https://hbr.org/2013/04/the-hidden-biases-in-big-data; Joy Buolamwini & Timnit Gebru, *Gender Shades: Intersectional Accuracy Disparities in Commercial Gender Classification* (2018).

186. Anthony Rapa, *A Perfect Fit: Generative Artificial Intelligence & Corporate Insurance*, WTW (Jul. 3, 2024), www.wtwco.com/en-us/insights/2024/07/a-perfect-fit-generative-artificial-intelligence-and-corporate-insurance.

187. *Id*.

communicating with its clients, as many currently do,[188] and that chatbot displays bias against a protected class, which happens more than it should,[189] the company could face allegations of third-party discrimination. These allegations would be covered by an EPLI policy, including legal and settlement costs.

Currently, there are no other policies that cover harm caused by discrimination (excluding Relm's new AI products), making EPLI an interesting case study for lawsuits involving AI bias. EPLI underwriters might opt to exclude AI usage regarding discrimination claims, but that will depend on the volume and costs associated with such claims in upcoming years. Cases are already being brought against companies using AI software to make employment decisions. One recent example is the class action filed against Workday in California, claiming that their AI screening software is biased.[190] These types of cases will decide the future of EPLI coverage when employers use AI.

4. Professional Indemnity (PI) & Traditional Errors & Omissions (E&O)

This form of policy goes by various names depending on the relevant industry. Other than PI and E&O (traditionally in the real estate industry), this policy is also referred to as professional liability insurance (PLI) in construction or malpractice insurance in the medical and legal fields.[191]

All of these professions require some sort of coverage when liability arises, especially when AI and GenAI are involved. Professionals recklessly relying on AI chatbots can lead to inaccurate advice and other wrongful

188. Maryna Bilan*, Generative AI Chatbots in eCommerce: Use Cases, Benefits, and Statistics Behind*, MASTER.OF.CODE (Nov. 14, 2024), master-ofcode.com/blog/generative-ai-chatbot-in-ecommerce-use-cases-benefits-statistics ("80% of retail and eCommerce businesses are currently using or planning to use AI bots in the near future.").

189. *See, e.g.*, *The Americans with Disabilities Act and the Use of Software, Algorithms, and Artificial Intelligence to Assess Job Applicants and Employees*, EEOC (May 12, 2022), https://www.jacksonlewis.com/sites/default/files/docs/EEOC-TechnicalAssistanceADA-AI.pdf.; Jeremy Hsu, *AI Chatbots Use Racist Stereotypes Even After Anti-Racism Training*, NEWSCIENTIST (Mar. 7, 2024), www.newscientist.com/article/2421067-ai-chatbots-use-racist-stereotypes-even-after-anti-racism-training/.

190. Mobley v. Workday, Inc., No. 23-cv-00770-RFL, 2024 U.S. Dist. LEXIS 11573 (N.D. Cal. Jan. 19, 2024).

191. Mark Rosanes, *Professional Indemnity Insurance: What is it and How Does it Work?*, INS. BUS. (Jan. 18, 2023), www.insurancebusinessmag.com/us/guides/professional-indemnity-insurance-what-is-it-and-how-does-it-work-433113.aspx.

acts.[192] A well-known example in the legal realm is lawyers in the United States using GenAI to establish inaccurate or false legal precedents without performing due diligence.[193]

Companies offering professional services that are covered by PI policies might encounter a new set of issues because of the rapid adoption of AI into their practices. With respect to GenAI, there is a real overreliance concern by the professionals on the algorithm to a point where AI operates independently. To reach its full potential, GenAI usually operates with minimal human oversight.[194] However, completely removing the human from the loop changes the current risk landscape covered by traditional PI policies.[195] This would lead to faster and more widespread claims of professional malpractice.[196] Furthermore, this overreliance might prevent adequate oversight and necessary checks, resulting in avoidable risks that are not thoroughly considered in current PI policies. This might lead to, among other things, "poor performance, financial losses for clients, and subsequent legal and regulatory actions."[197]

Nonetheless, some still view this line of policies as an important tool covering AI used by professionals: "professional liability insurance will be a vital tool to protect against unforeseen liabilities arising out of the rapid adoption of AI by service providers."[198] As will be discussed below, this remains to be seen as removing the human out of the AI loop might lead some insurers to exclude AI from their traditional coverage while making room and creating

192. Joanne Cracknell & Roberto Felipe, *Navigating AI risks in Professional Liability*, WTW (Oct. 12, 2023), www.wtwco.com/en-us/insights/2023/10/navigating-ai-risks-in-professional-liability.

193. Kathryn Armstrong, *ChatGPT: US Lawyer Admits Using AI for Case Research*, BBC (May 27, 2023), www.bbc.com/news/world-us-canada-65735769; Sara Merken, *New York Lawyers Sanctioned for Using Fake ChatGPT Cases in Legal Brief*, REUTERS (Jun. 26, 2023), https://www.reuters.com/legal/new-york-lawyers-sanctioned-using-fake-chatgpt-cases-legal-brief-2023-06-22/.

194. Steven Mills, Noah Broestl, & Anne Kleppe, *You Won't Get GenAI Right If You Get Human Oversight Wrong*, BOS. CONSULTING GRP. (Mar. 27, 2025), https://www.bcg.com/publications/2025/wont-get-gen-ai-right-if-human-oversight-wrong.

195. Deepak Maheshwari, *The Future of AI: Is Human Oversight Always Necessary?*, MEDIUM (Sept. 29, 2024), https://maheshwari-bittu.medium.com/the-future-of-ai-is-human-oversight-always-necessary-3d9f427c43ae.

196. Rapa, *supra* note 186.

197. *Id.*

198. Evan Knott, Adrienne Kitchen & J. Andrew Moss, *Insurance Coverage Issues, Artificial Intelligence and Deepfakes*, REUTERS (Oct. 14, 2024), https://www.reuters.com/legal/legalindustry/insurance-coverage-issues-artificial-intelligence-deepfakes-2024-10-14/.

a demand for innovative policies focusing on AI. [199] The PI realm is of heightened interest, given that many professionals have been quick to adopt AI technologies into their practice.[200] Though currently, insurance companies have yet to exclude AI as a whole, it is bound to have an effect on the language of PI policies in the near term.

5. Casualty Insurance (GL & CGL)

Casualty insurance, also known as a General Liability (GL) or Commercial General Liability (CGL), is an umbrella type of coverage protecting businesses from common risks associated with their activities.[201] These include property damages, bodily injuries, product liability, contractual liability, premises liability, and non-bodily injuries such as advertising injuries, slander, and libel.[202]

This type of policy is the backbone of commercial coverage for businesses, given its broad scope.[203] Thus, prima facia, if services or products using AI result in injury to others or damages to property, CGL policies could be triggered. More specifically, advertising injury, covered by CGL, includes claims for "copyright infringement, trade dress infringement, slogan infringement, and misappropriation of advertising ideas."[204] In the context of GenAI, a CGL policy could be highly relevant when GenAI applications lead to these types of violations, including slander and libel.[205]

Given the broad scope of this policy and its inherent intention to protect commercial enterprises from risks associated with their day-to-day activities, there is a good chance that CGL will absorb AI as just another element of doing business in the modern world.[206] Nonetheless, similar to cyber harms, there is a possibility that the underwriters of these policies will consider AI as something that exceeds the scope of the policy, given its potential volume of harm and its high frequency, leaving policyholders exposed and in need of additional coverage. These gaps might be covered by cyber insurance

199. *See infra* Chapter VI.

200. Knott, et al., *supra* note 198.

201. *See, e.g.*, *Commercial General Liability Insurance*, THE HARTFORD, www.thehartford.com/general-liability-insurance. (last updated Nov. 20, 2023).

202. *E.g.*, *id*. ("These general policies offer a critical safety net for small businesses that might face liability claims.").

203. *Commercial General Liability Insurance*, INS. INFO. INST., www.iii.org/article/commercial-general-liability-insurance (last visited Mar. 12, 2025).

204. Burke & Reed, *supra* note 161.

205. Rapa, *supra* note 186; *Id*.

206. *See, e.g.*, Evan Knott et al., *supra* note 198 (In the context of deepfakes).

and Tech E&O for now, but if an exclusion trend expands, there will be no other option but to seek AI-specific policies.

6. Workers' Compensation

Workers' compensation policies provide coverage to employees who were injured or became ill at work. Thus, work-related injuries are the trigger for these policies.[207] They are required by law in most states in the United States.[208] These policies include coverage of medical expenses, lost wages, rehabilitation, short or long-term disability benefits, and death benefits.[209]

In the AI context, "if an AI-controlled industrial robot injures an employee, workers' compensation policies could be triggered."[210] Thus, similar to the above GL policies, workers' compensation should apply to work-related accidents even if caused by AI (unless those will be explicitly excluded by the insurance provider). The traditional workers' compensation policy should be indifferent to the cause of the accident as long as it was indeed an accident (i.e., not intentional, and part of a work-related event).

Nonetheless, adopting AI into businesses is changing the risk landscape of workplace injuries. This could be viewed as a "shift in the types of injuries employees may experience."[211] On top of physical injuries, malfunctions and programming errors could lead to work accidents as well as psychological effects of working with AI that might cause harm to employees. Introducing AI into the workplace raises several challenges to the existing workers' compensation models.[212] These include the difficulty in determining liability for compensation purposes, the need to update safety standards when

207. Julia Kagan, *Workers' Compensation: What It Is, How It Works, and Who Pays*, INVESTOPEDIA (Jul. 31, 2024), www.investopedia.com/terms/w/workers-compensation.asp.

208. *E.g., Purchasing Workers' Compensation Insurance*, COMMONWEALTH OF PA., www.pa.gov/agencies/dli/resources/for-claimants-workers/workers—compensation-insurance-search-form-/purchasing-workers-compensation-insurance.html ("If you employ workers in Pennsylvania, you must have workers' compensation insurance – it's the law.").

209. *Id.*

210. Devriese & Crowl, *supra* note 128, at 15.

211. *See How AI Alters Workplace Risks and Workers' Comp Needs,* FULLER INS. AGENCY, (Feb. 19, 2025) https://www.fullerins.com/blog/how-ai-alters-workplace-risks-and-workers-comp-needs. (stating how AI transforms workplaces across industries and how it has brought about new risks that businesses must manage).

212. *Id.*

AI is involved, and perhaps recognizing new categories of harm, such as psychological or emotional harm resulting from interactions with AI.[213]

Thus, several changes might be needed to adjust workers' compensation to the AI age. These might include expanding existing coverage, by law or need, to include injuries directly related to AI, gaining clarity regarding the applicable liability regime when AI is involved and updating safety regulations via workplace policies to ensure safer work environments. The latter may include guidelines for the safe deployment and operation of AI-powered software, as well as adequate training for the employees.[214] If underwriters of workers' compensation decide not to adjust the policy in light of AI, there will again be a new exposure that could be resolved primarily by purchasing a designated AI policy to cover this gap.

7. Intellectual Property (IP)

IP policies cover companies against IP infringement claims when they are allegedly infringing upon others' IP and the costs associated with defending their own IP right if a company believes it has been infringed upon. Some insurers offer these as a standalone policy, though they are usually combined with other policies, such as the media liability policy detailed below.[215] As such, IP policies are twofold: first, they protect against allegations that a company infringed IP because of their AI-generated content; and second, they apply when GenAI is allegedly infringing upon a company's own IP.

IP litigation insurance, a specific type of IP policy, aims to protect companies against allegations of IP infringement "in ways that General Liability or Professional Liability might not."[216] Thus, new companies who have not considered purchasing this type of policy in the past, such as financial institutions or cyber companies, are now seeing the appeal of this policy with the wide adoption of GenAI.[217]

The issue of intellectual property infringement has made headlines since the entrance of GenAI into our lives, followed by several notable lawsuits.[218] This is also amplified by the fact that OpenAI, the developer and

213. Catherine K Ettman & Sandro Galea, *The Potential Influence of AI on Population Mental Health*, 10 JMIR MENT HEALTH (2023), https://mental.jmir.org/2023/1/e49936.

214. Nada R. Sanders & John D. Wood, *The Skills Your Employees Need to Work Effectively with AI*, HARV. BUS. REV. (Nov. 3, 2023), hbr.org/2023/11/the-skills-your-employees-need-to-work-effectively-with-ai.

215. *See infra* Chapter V.12.

216. Rapa, *supra* note 186.

217. *Id.*

218. *E.g., Case Tracker: Artificial Intelligence, Copyrights and Class Actions*, BAKERHOSTETLER, www.bakerlaw.com/services/artificial-intelligence-ai/case-

provider of ChatGPT, has publicly committed to protecting its users against copyright infringement allegations.[219] It is highly unlikely that this statement is backed up by an insurer, given the high probability and volume of damages that might occur. Rather, OpenAI, given its size and net worth of approximately $157 billion,[220] is well positioned to self-insure and assure its users that its products are trustworthy.

A recent example from Germany presents the increasing scope of IP violations using GenAI, with little understanding of the possible consequences and harms. Die Aktuelle, a German magazine, published an AI-generated interview that included AI-generated "quotes" from Michael Schumacher, the seven-time Formula 1 world champion.[221] Schumacher had a severe skiing accident in 2013 and he has not been interviewed since, leading Die Aktuelle to claim this is his "first interview" since his accident.[222] Schumacher's family filed a lawsuit against the magazine and won, receiving reportedly €200,000 in compensation.[223] This claim should also be covered by a media liability policy, discussed below, given the context of its publication in a magazine.

IP policies are predicted to be a vital part of companies' risk mitigation strategies, given the high risk of IP infringement associated with GenAI. It is highly plausible that this will be one of the first policies to exclude AI, given its high probability of causing damages and the high costs associated with it, including litigation and possible settlements. This will most likely create an immediate need for a specific IP policy in the context of AI, which the insurance market should eventually deliver.

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tracker-artificial-intelligence-copyrights-and-class-actions/ (last visited Apr. 10, 2025); Gil Appel, Juliana Neelbauer & David A. Schweidel, *Generative AI Has an Intellectual Property Problem*, HARV. BUS. REV. (Apr. 7, 2023), hbr.org/2023/04/generative-ai-has-an-intellectual-property-problem.

219. Blake Montgomery, *OpenAI Offers to Pay for ChatGPT Customers' Copyright Lawsuits*, THE GUARDIAN (Nov. 6, 2023), www.theguardian.com/technology/2023/nov/06/openai-chatgpt-customers-copyright-lawsuits.

220. Antonio Pequeño IV, *OpenAI Valued At $157 Billion After Closing $6.6 Billion Funding Round*, FORBES (Oct. 2, 2024), https://www.forbes.com/sites/antoniopequenoiv/2024/10/02/openai-valued-at-157-billion-after-closing-66-billion-funding-round/.

221. *German Magazine Fires Editor over AI 'Interview' with Michael Schumacher*, REUTERS (Apr. 22, 2023, 2:05 PM), https://www.reuters.com/sports/motorsports/german-magazine-apologises-schumacher-family-sacks-editor-2023-04-22/.

222. *Id*.

223. *Michael Schumacher's Family Win Case Against Publisher Over Fake AI Interview*, ASSOCIATED PRESS (May 23, 2024), https://apnews.com/article/schumacher-ai-fake-interview-35bd73e6cd4aecfa3bfb46339d3f2376.

8. Property Insurance

These first-party policies usually protect businesses' physical property and the costs associated with business interruption once a company's physical property is damaged or destroyed.[224] "If AI causes physical harm to a person or property, most underwriters will consider this a loss that would be covered by property insurance."[225] A second option is general liability insurance, and it is important to note that for "a single AI-driven entity, the limits of multiple policies could be stacked."[226] This means that if the limit of the first policy (e.g., a GCL policy) is reached, the policyholder can benefit from its second policy (e.g., a property policy) and its limit.[227]

Examples of the need for property insurance in the AI context include coverage for loss or damage to corporations' physical assets when their AI software is hacked, causing physical damage. For example, if the company's "industrial control systems are manipulated to cause physical damage,"[228] if a company's facilities used to store AI software, such as data centers, are damaged, or if business income is lost due to interruptions resulting from said physical damage to physical AI assets.[229] Furthermore, this type of policy might be of high value for companies that are "building or expanding the physical infrastructure necessary to support large databases of customer or other data" used to power AI software.[230]

AI could also change the way "business interruption" is evaluated for purposes of property loss. Before the AI age, business interruption covered by a traditional property policy covered lost income and operational expenses resulting from a property loss. However, in the AI age, once a data center or other physical infrastructure is down, it could lead to more complex results with much broader effects. A recent example is the Microsoft global software malfunction due to a problematic CrowdStrike Incident in July 2024,[231]

224. Burke & Reed, *supra* note 161.

225. *Id.*

226. Devriese & Crowl, *supra* note 128, at 19.

227. Stacking, LSD, www.lsd.law/define/stacking.

228. Burke & Reed, *supra* note 161.

229. *Id.*

230. Rapa, *supra* note 186 ("As institutions invest in data centers and other physical assets, property insurance becomes crucial for protecting these investments against physical damage and loss.").

231. *See infra* note 353 and accompanying text. *See also*, Jerry Gupta, *CrowdStrike Incident: A Wake Up Call for Insurance of Digital – and AI – Risk*, ARMILLA AI (Jul. 22, 2024), www.armilla.ai/resources/crowdstrike-incident-a-wake-up-call-for-insurance-of-digital—-and-ai—-risk.

estimated to cause worldwide financial damage of $10 billion.[232] A recent report stated that, "roughly 25% of Fortune 500 companies experienced disruptions due to the incident, the most heavily affected industries, financially, being healthcare ($1.94 billion in estimated losses) and banking ($1.15 billion). In addition, a shocking 100% of the transportation and airlines sector was affected, and the group will rack up an estimated $0.86 billion in losses, according to the forecast."[233] Though cyber insurance was the main policy triggered by this incident, property insurance could also be relevant to these types of incidents once physical assets are harmed and businesses are interrupted. Although at first glance a property policy seems less relevant to the age of AI, it could have significant implications as AI continues to progress and physical damage might ensue.

9. Fidelity / Bond / Crime Insurance

This first-party coverage is aimed to protect companies against loss as a result of employee "theft, fraud, and computer crime."[234] The coverage applies to loss resulting from dishonesty, embezzlement, theft of property and money, and computer fraud from both employees and non-employee third parties.[235] These policies also cover "social engineering" risks caused by deceit or impersonation, but these are usually subject to a low limit of $1 million.[236]

It is highly likely that adopting AI, specifically GenAI, will influence this type of policy as AI creates "new attack vectors that bad actors can exploit."[237] A prominent example that has caught the eyes of the legislature[238] is using AI to create deepfake video calls that can deceive employees and result in company losses.[239] On the other hand, it is important to note that AI

232. Lian Kit Wee, *Here Comes the Wave of Insurance Claims for the CrowdStrike Outage*, BUS. INSIDER (Jul. 22, 2024), www.businessinsider.com/businesses-claiming-losses-crowdstrike-outage-insurance-billions-losses-cyber-policies-2024-7.

233. Dark Reading Staff, *CrowdStrike Outage Losses Estimated at a Staggering $5.4B*, DARK READING (Jul. 26, 2024), www.darkreading.com/cybersecurity-operations/crowdstrike-outage-losses-estimated-staggering-54b.

234. Rapa, *supra* note 186.

235. Burke & Reed, *supra* note 161.

236. *Id.*

237. Rapa, *supra* note 186.

238. *Deceptive Audio or Visual Media ('Deepfakes') 2024 Legislation*, NCSL (Nov. 22, 2024), www.ncsl.org/technology-and-communication/deceptive-audio-or-visual-media-deepfakes-2024-legislation.

239. Bethan Moorcraft, *What Are Deepfakes – And How Does Insurance Respond?*, INS. BUS. (Mar. 23, 2020),

can also provide beneficial methods for companies to protect their systems from internal threats covered by this policy.[240]

At their essence crime policies were created to address crimes, regardless of their origin. Cyber insurance has helped cover some exposure left by crime insurance policies, given their low limit. It is likely that the same will happen with AI, given the expected scope and probability of these criminal attacks happening in light of the ease of using this technology for nefarious purposes.[241]

10. Directors & Officers (D&O)

D&O policies usually offer coverage for costs associated with claims made against "a company or its directors, officers, managers and board members arising out of their decisions or actions,"[242] in other words, the companies' leadership. Essentially, the policy protects the stakeholders mentioned above from "personal liability for decisions made in their official capacities, including those related to the oversight of AI initiatives."[243]

The increasing use of AI by boards and directors of companies to make business decisions to boost their future gains, as well as adopting and implementing an AI strategy, is alarming to those underwriting D&O policies.[244] Securities class actions are already happening when companies use AI, and it is unclear how D&O might change as a result.[245]

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www.insurancebusinessmag.com/uk/news/cyber/what-are-deepfakes—and-how-does-insurance-respond-217669.aspx.

240. Rapa, *supra* note 186 ("Advanced AI systems can monitor transactions and employee behavior for signs of fraudulent activity, offering a proactive approach to preventing theft and fraud.").

241. Daniel Oberhaus, *Prepare for AI Hackers*, HARV. MAG. (Mar.-Apr., 2023), www.harvardmagazine.com/2023/02/right-now-ai-hacking; Scott Shapiro, *Staying One Step Ahead of Hackers When It Comes to AI*, WIRED (Jan. 8, 2024), www.wired.com/story/staying-one-step-ahead-of-hackers-when-it-comes-to-ai/.

242. Burke & Reed, *supra* note 161.

243. *Navigating AI Risks. Part III: Leveraging Insurance to Mitigate AI Risks*, MMMLAW (Nov. 6, 2024), www.mmmlaw.com/news-resources/102jmym-navigating-ai-risks-part-iii-leveraging-insurance-to-mitigate-ai-risks/.

244. Agnew, *supra* note 183.

245. *Id*. ("While the triggers may be novel, the liabilities themselves are not, and existing policies may be up to the challenge of securing their risks."). *See also*, John M. Orr & Lawrence Fine, *Directors and officers (D&O) Liability: A Look Ahead to 2025*, WTW (Jan. 29, 2025), www.wtwco.com/en-us/insights/2025/01/directors-and-officers-d-and-o-liability-a-look-ahead-to-2025.

This policy should also cover AI washing: when a company's representations regarding its AI capabilities are false,[246] as well as shareholder and derivative actions concerning the company misuse of AI in employment (also relevant for EPLI) and data privacy (also relevant for cyber policies).[247] D&O policies also offer protection from reputational harm. If AI incidents tarnish a company's reputation, leading to a decline in its shareholder value, this policy can protect its directors from allegations that "they mismanaged AI risks," thus reducing the company's value and reputation.[248]

Furthermore, more companies are creating new corporate leadership roles focused on AI governance, also known as the Chief AI Officer (CAIO).[249] These new officers may be especially vulnerable to liability and regulatory scrutiny, given the uncertainty associated with AI development and implementation. This policy holds an imperative role in protecting these new positions and thus supporting in-house innovation and better oversight over AI implementation in companies.[250]

D&O policies are yet another example of a valuable policy in the AI context that is currently being overlooked, given other traditional policies and the development of new AI-specific policies. Nonetheless, as described above, the trajectory of AI in the D&O realm depends on ongoing exclusions that might occur if AI is proven to be too high-risk for this policy.

11. Product Liability

This policy covers bodily or property harms caused under the theory of product liability in torts when a manufacturing, design, or failure to warn defect is discovered in the product, as well as the litigation costs and any

246. A growing topic in the corporation world, *see e.g.*, *SEC Charges Two Investment Advisers with Making False and Misleading Statements About Their Use of Artificial Intelligence*, U.S. SECURITIES AND EXCHANGE COMMISSION (Mar. 18, 2024), www.sec.gov/newsroom/press-releases/2024-36; Marc Galindo, *How AI Washing is Impacting D&O Insurance: A Growing Risk for Companies and Their Leadership*, FLOW (Feb. 12, 2025), www.flowspecialty.com/blog-post/how-ai-washing-is-impacting-d-o-insurance-a-growing-risk-for-companies-and-their-leadership.

247. Burke & Reed, *supra* note 161.

248. *Navigating AI Risks. Part III*, *supra* note 243.

249. Cole Stryker, *What Is a Chief AI Officer?*, IBM (May 29, 2024), www.ibm.com/think/topics/chief-ai-officer.

250. Rapa, *supra* note 186 ("safeguarding against potential legal actions and ensuring that leadership can navigate the complexities of Gen AI adoption with confidence.").

compensation owed to affected parties.[251] Product liability also covers situations where the products do not comply with regulatory standards, legal fees, and settlements related to non-compliance issues.[252]

To those who view AI as nothing more than a product,[253] this policy should cover AI software rather easily and be an integral part of the risk management strategy when it comes to AI.[254] Indeed, Catherine M. Sharkey, in her article on AI, has claimed that a product liability framework for AI is the best approach to incentivize AI developers to mitigate potential risks proactively by manufacturing and designing safer AI products before releasing them to the market.[255] However, some stakeholders view AI as something more than just a product, given its unique features and the black-box issue, thus challenging the application of this traditional policy in its current format.[256] If we consider AI to be more than a product, as many scholars and regulators do, then the applicability of a product liability policy could be extremely limited when AI causes harm.[257]

The revised Product Liability Directive (PLD) in the EU will have significant implications for traditional product liability policies worldwide.[258] The revised PLD explicitly applies a strict liability regime to AI software, which it considers to be a product.[259] The new Directive defines products to

251. *Facts + Statistics: Product liability*, INS. INFO. INST., www.iii.org/fact-statistic/facts-statistics-product-liability.

252. *Navigating AI Risks. Part III*, *supra* note 243.

253. Anat Lior, *AI Entities as AI Agents: Artificial Intelligence Liability and the AI Respondeat Superior Analogy*, 46 MITCHELL HAMLINE L. REV. 1043, 1056 (2020).

254. Jonathan Selby, *Safeguard Your AI: Essential Insurance for Generative Businesses*, FOUNDERSHEILD (Dec. 19, 2024), https://foundershield.com/blog/insurance-for-generative-ai-businesses/. ("Product liability insurance covers companies in case their product causes bodily injury or property damage. As more and more companies leverage generative AI to design their products, product liability will take center stage to cover accidents stemming from the technology.").

255. Catherine M. Sharkey, *A Products Liability Framework for AI*, 25 COLUM. SCI. & TECH. L. REV. 240, 258 (2024).

256. Devriese & Crowl, *supra* note 128, at 17 ("Product liability policies could also be impacted and could offer protection against AI failures. However, for AI to fall within the insuring agreement, AI would need to be considered a product (as opposed to a service), an important question that has not yet been decided upon.").

257. *Id.*

258. Council Directive 85/374/EEC of 25 July 1985 on the approximation of the laws, regulations and administrative provisions of the Member States concerning liability for defective products, O.J. (L 210) 29.

259. STEFANO DE LUCA, NEW PRODUCT LIABILITY DIRECTIVE, EUR. PARLIAMENTARY RSCH. SERV. (Dec. 2023), www.europarl.europa.eu/RegData/etudes/BRIE/2023/739341/EPRS_BRI(2023)739341_EN.pdf.

include AI systems.[260] It expands the covered harms to include "medically recognised psychological harm" and "loss or corruption of data that is not used exclusively for professional purposes."[261] It also expands liability to defects that happened after the product had already left the entity manufacturing it, such as harms resulting from software updates and machine learning.[262]

From an insurance perspective, the revised PLD will probably make it much easier for claimants to submit a successful claim under a product liability policy once AI causes harm, given the expansion in product definition and the types of damages.[263] The revised PLD could also create new opportunities for insurers, leading to higher demand for product liability coverage.[264] Either way, this type of regulation, as well as further discussion of AI as a product in the US and the UK, will have a significant effect on the development and relevance of a traditional product liability policy.

12. Media Liability

Media liability covers "claims for 'media' or 'multimedia wrongful acts' alleging copyright or trademark infringement, misappropriation, plagiarism, or invasion of the right of privacy or publicity in connection with the production, publication or dissemination of media (such as sounds, images, or advertisements) in electronic or print media."[265] Though the subject matter overlaps with the above IP policy, media liability policies are narrower and focus on media companies and the content they create and distribute via publication or broadcasting.

Some carriers bundle media liability as part of a cyber policy or add it as a separate endorsement.[266] A media policy is extremely appealing to all companies and vendors who might be accused of and sued for copyright

260. *Id*. at 1 ("The proposal introduces new provisions to address liability for products such as software (including artificial intelligence systems) and digital services that affect how the product works (e.g. navigation services in autonomous vehicles)").

261. *Id*. at 5–6.

262. *Id*. at 6.

263. As well as other elements set in this legislation. *Id*.

264. Ina Ebert, *Product Liability 2.0: What Insurers Should Know about the New EU Directive*, THE INSURER (Dec. 31, 2024), www.theinsurer.com/ti/viewpoint/product-liability-20-what-insurers-should-know-about-the-new-eu-directive-2024-12-31/. *See also*, Stuart Collins, *AI Regulation to Shake Up Liability Insurance*, COM. RISK (Mar. 13, 2024), www.commercialriskonline.com/ai-regulation-to-shake-up-liability-insurance/

265. Knott, *supra* note 198.

266. Peter M. Gillon & Tamara D. Bruno, *Generative AI Creates New Insurance Risks for Corporations*, CORP. COUNS. ONLINE (Aug. 16, 2023).

infringement, which is a major concern associated with AI development and usage by both companies and individuals.[267] Providers of media liability are emphasizing the need to educate users of AI, especially GenAI, that utilizing this technology could lead to IP infringement claims, even if the output was solely created by AI.[268]

Traditional media policies usually provide some defense and indemnity for copyright infringements. Thus, AI vendors are encouraged to purchase said policies if they need to train their model on data that might amount to copyright infringement.[269]

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Head of North America Cyber and E&O at WTW stated that other liabilities that might emerge from AI usage would be rolled up to other areas for example, discrimination, IP infringement, media, regulatory fines and penalties, and data privacy.[270] In light of this, it is mostly about how a policyholder uses the AI, not the mere fact that it is an AI algorithm or product. In their words, "your liability is the same at the end of the day, whether you have a person doing it or your AI."[271] Thus, there is a genuinely strong case for sticking to traditional policies given *what* they cover (the content and context) and not *who* they cover.

A different but parallel approach could be combining separate lines of insurance, e.g., cyber, tech E&O, and PI, into "one policy underwritten by a single insurer to address concerns over the proximate cause of loss and avoid arguments over which insurer is liable."[272] These could be marketed by vectors of the AI application in a given industry, such as healthcare services, banking, etc.

In a recent publication focusing on GenAI and corporate insurance,[273] it was stated that "managing the risks associated with GenAI is like solving a

267. *See, e.g.*, Matthew Sag, *Copyright Safety for Generative AI*, 61 HOUSTON L. REV. 295 (2023); Sofia Vescovo, *Rise of the Machines: The Future of Intellectual Property Rights in the Age of Artificial Intelligence*, 89 BROOK. L. REV. 221 (2023); Jane C. Ginsburg & Luke Ali Budiardjo, *Authors and Machines*, 34 BERKELEY TECH. L.J. 343 (2019).

268. Olivia Overman, *How AI is Changing the Need for Media Liability Coverage*, INDEPENDENT AGENT (Jun. 24, 2024), www.iamagazine.com/markets/how-ai-is-changing-the-need-for-media-liability-coverage.

269. Quinn, *supra* note 157.

270. Zoom interview with Head of North America Cyber and E&O, *supra* note 144.

271. *Id.*

272. Phillips, *supra* note 33.

273. Rapa, *supra* note 186.

complex puzzle—no single insurance policy covers all potential exposures. Instead, a comprehensive risk management strategy must be pieced together using various policies from your insurance portfolio." In its conclusion, the piece calls on financial institutions to take a proactive approach to "piece together a robust insurance strategy that addresses the multifaceted risks of GenAI," to ensure, "comprehensive and cohesive coverage." However, further analysis reveals that this is easier said than done.[274] This is due to "silent AI" challenges and the current, profound uncertainty regarding what is actually covered by these policies and what will require additional affirmative endorsement, perhaps in the form of a designated AI policy.

VI. UNDERWRITING PRACTICES AND RISK ASSESSMENT

Even the companies already operating in this field aiming at offering coverage for AI risks are struggling to articulate the appropriate underwriting process and the overall risk perception associated with this technology. The data simply is not there yet. This does not mean insurance companies are unwilling to underwrite policies covering these risks. On the contrary, "this is the main purpose of the insurance industry," states an underwriter working at a large cyber insurance company, and this embodies the essence of insurance – "we price for uncertainty."[275]

1. Issues and Challenges to AI Coverage

Most insurance companies in this field hope to build historical data loss sets in the upcoming years. They plan to develop their underwriting process upon these data loss sets to reach more accurate premiums reflecting, to the best of their ability, the actual risks associated with AI. This process takes time and resources. Conal McCurry, a senior cyber broker, specifically referred to setting premiums for AI risks as a major challenge. Interestingly, he connected the determination of AI liability premiums with the exponential costs lawyers will charge initially, given the profound uncertainty surrounding the legal outcomes of AI violations.[276] He stated that because the next wave of AI-associated claims will be detrimental to the development of AI coverage, law firms are expected to set very high rates given the high publicity these incidents get, along with the fact that they are setting new precedents.

274. *See also* Levine & Pappas, *supra* note 143 ("Of course, not all AI risks may be covered by standard legacy insurance products. For instance, AI models that underperform could lead to uncovered financial losses.").

275. Zoom interview with a Chief Underwriting Officer, *supra* note 168.

276. Zoom interview with Conal McCurry, Senior Cyber Broker at WTW (Sep. 5, 2024).

All of these, he claimed, are bound to have a direct impact on policy premiums.[277]

Big insurance companies can afford to delve into this market early and develop the required expertise to brand themselves as experts in this field for the years to come, even if it reduces their bottom line. Other, more conservative insurers will probably operate in this field later on as they feel more comfortable offering policies to cover AI.[278] Some, however, are diverging from this traditional play set. For example, CoverYourAI does not aim to write its policies based on historical loss data of AI but, instead, based on prediction models, revolutionizing the traditional way policies are underwritten in this industry.[279]

Armilla AI employs a model that strives to deeply understand the specific AI technology before underwriting a policy for it. They test 10-12 product dimensions, each with 10-15 tests to run. The tests are specific to the types of usage of the AI product, focusing on gathering information regarding the efficacy of the technology. Different factors, such as target audience, regulated environment, etc., determine the coverage, enabling Armilla to price and set the policy terms. Currently, as stated above, Armilla is focused on a product guarantee policy, providing a warranty that speaks to the performance of the AI technology.[280]

Claire of Relm Insurance agrees that there is limited historical data concerning AI specifically, but relying on previous data is sometimes counterintuitive to pricing emerging risks. Furthermore, analogous risks are available to insurance companies.[281] She gives the example of the General Data Protection Regulation (GDPR), a European Union regulation that sets guidelines for the collection and processing of personal information.[282] The GDPR explicitly provided information about fines and penalties giving insurance companies some clarity regarding their clients' potential exposure.[283] A similar path could be taken when discussing the EU AI Act as it also provides explicit

277. *Id*.

278. For example, QBE insurance company in North America only launched its cyber insurance line in July 2023, much later than other more innovative companies started to operate in this field. *QBE North America Launches New Cyber Insurance Program with Converge*, QBE (Jul. 27, 2023), www.qbe.com/us/newsroom/press-releases/qbe-north-america-launches-new-cyber-insurance-program-with-converge.

279. Zoom interview with Josh Fourie, *supra* note 90.

280. Zoom Interview with Karthik Ramakrishnan, *supra* note 75.

281. Zoom Interview with Claire Davey, *supra* note 101.

282. *General Data Protection Regulation*, INTERSOFT CONSULTING, https://gdpr-info.eu/ (last visited Apr. 17, 2025).

283. Commission Regulation 2016/679, art. 84, 2016 O.J. (L 119).

information regarding fines and penalties.[284] Previous emerging technologies have shown us that the core way of underwriting technology is very similar, whether that technology is AI or something else. In that sense, the lack of historical data should not prevent companies from offering policies, especially if they aim to support emerging tech that, by definition, has no historical data.[285]

In discussing the overall approach of underwriting policies covering AI technologies Lauren Finnis of WTW encourages companies working with AI to better understand which risks are covered and which are not, assuming the risks on their own.[286] She calls for AI and GenAI risks to be treated similarly to other risks. First, the technology needs to be assessed and identified. Once that happens, "the next step is to analyze the potential impact, determine risk tolerance, and explore mitigation strategies."[287] This approach includes mitigating "the severity and occurrence of rations and implementing monitoring systems."[288] This is a traditional approach to handling and managing new risks presented by new technologies. Furthermore, Finnis described education as one of the major challenges of underwriting and offering coverage for AI.[289] Thus, basic education and understanding of the technology by both sides is essential to ensure providers' ability to offer better coverage.

Another important consideration in the underwriting process is the "human in the loop" issue.[290] This refers to having a human within the AI's decision-making process, whether at the end authorizing its recommendation or decision, or in any other part of this pipeline. Having a human in the loop has been referred to as a human "liability sponge," where said human essentially absorbs "the legal and moral liability around a negative incident, including bearing the weight of tort liability, professional sanctions, or other opprobria."[291] This might very well include the "absorption" of payment via a new or an existing liability policy. Some underwriters from the cyber insurance sector stated that once there is no human in the loop, there is an assumption that offensive cyber operations utilizing AI will escalate. This means that if we have an anonymous "human in the loop" or no human at all, more cyber operations will be powered by AI, raising concerns within the insurance sector

284. Commission Regulation 2024/1689, art. 99, 2024 O.J. L.

285. *Id*.

286. R&I Editoral Team, *supra* note 81.

287. Zoom Interview with Lauren Finnis, *supra* note 149.

288. *Id.*

289. *Id*.

290. Rebecca Crootof, Margot E. Kaminski & W. Nicholson Price II, *Human in the Loop*, 76 VAND. L. REV. 429 (2023).

291. *Id*. at 483.

about compatible coverage.[292] On the other hand, Testudo's co-founders stated that, "insurance can take humans out of the loop as a solution" for the liability concerns associated with AI.[293] "You no longer need a human because the insurance products will bear the weight, insuring those who develop and hold up to safety standards to avoid moral hazard issues."[294] These very different approaches to having a human in the decision-making process will evolve as more AI-based products and services change, or even eliminate, the concept of having a human in the loop. The insurance industry will have to grapple with what this means for its new or existing policies. As of now, it seems that new companies in this field are optimistic about their ability to provide policies, even when the operation is completely isolated from human intervention.

Finnis of WTW also addressed this issue as she stated that eventually, even if there is no physical human in the loop, there is a human in the background that should be held liable for the end harm. Not having a human in the loop does not mean no one should pay or be held responsible.[295] An underwriter from the cyber industry expressed a similar thought by saying that blaming the computer is a policyholder's "first mistake."[296] There is always a human in the process, and ignoring it creates a broader fallacy that should be eliminated from current discussions as soon as possible.

Risk assessment is a critical factor in an insurance carriers' ability to operate in this field successfully.[297] Many participants expressed that neither consumers nor AI developers have the tools or data to assess their potential AI risk exposure accurately. There seems to be a general tendency to overestimate the risk regarding AI.[298] Currently, insurers are driven by the claims

292. Zoom interview with a Chief Underwriting Officer, *supra* note 168.

293. Zoom interview with George Lewin-Smith & Mark Titmarsh, *supra* note 17.

294. Lewin-Smith and Titmarsh clarified in this context that even though insurance financially protects businesses from liability risks arising from damages caused by a company's AI system, "insurance is a risk management tool that complements robust governance, controls, and regulatory standards and should not be seen as a panacea for all AI risks." *Id*.

295. Zoom Interview with Lauren Finnis, *supra* note 149.

296. Zoom interview with an Underwriting Manager Cyber Lead at a large cyber insurance company (Jun. 20, 2024).

297. Sheldon H. Jacobson, *The Rewards of AI Are Huge, But So are the Risks — Enter AI Insurance*, THE HILL (Jul. 15, 2024), thehill.com/opinion/technology/4771607-artificial-intelligence-liability-insurance/.

298. NEERAJ SARNA, MUNICH RE, DE-RISKING AI VENTURES: HOW MUNICH RE ASSESSES AI PERFORMANCE RISKS – INSIGHTS INTO OUR DUE DILIGENCE PROCESS 3 (2023), https://www.munichre.com/content/dam/munichre/contentlounge/website-pieces/documents/MunichRe-De-Risking-AI-Ventures-Whitepaper.pdf/_jcr_content/renditions/original./MunichRe-De-Risking-AI-

they receive and see. The claims departments of insurance companies identify the claims related to AI and advise on how to pivot and underwrite them. Big cyber insurance companies state that they currently do not see enough explicit AI claims to make any decisions about their future trajectory in this field.[299] Nonetheless, the designated AI insurance companies described above have a very different approach to this AI question. They are honing in on these risks using existing data loss information gathered from both legal and non-legal databases.[300] This proactive approach, building an AI database rather than waiting for AI claims to enter their network, significantly differentiates them from companies that are still contemplating how to operate in this area.

In a recent interview, Christian Westermann, Group Head of AI's Zurich Insurance, stated two significant challenges to coverage for GenAI.[301] First, he started by stating that "very little has changed with basic AI-related risks: you must ensure that your models are reliable, that you address bias, that your solution is robust and explainable, and that you are transparent and accountable when using AI." He continued to say that GenAI, "introduces new risks, such as misinformation and deep fakes, leading to an increase in the professionalism of fraud and the sophistication of cyberattacks, wherein AI probes weaknesses in a network and finds a strategy to penetrate it." Many would disagree with the classification of these risks as "new" but rather as risks with a larger scope of harm. Second, he mentioned the risk accumulation issue; "we tend to all rely on the same suppliers, so there's a concentration and a lock-in risk. If we are all based on the same third-party models, we all have the same dependency on those vendors." This dependency could lead to a complete shutdown of a specific industry, given that all applications run on the same supplier, and if that supplier falls, a domino effect ensues. This is also evident in the cyber insurance industry, such as the CrowdStrike

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Ventures-Whitepaper.pdf ("In short, it will transform our lives. However, the lack of trust hinders positive change and means that innovative start-ups are having a hard time convincing their future customers to adopt AI-based technologies.").

299. Zoom interview with a Chief Underwriting Officer, *supra* note 168; Zoom interview with Conal McCurry, *supra* note 276; Zoom interview with an Underwriting Manager Cyber Lead, *supra* note 296; Zoom Interview with a Senior Broker at a Large Insurance Company (Aug. 9, 2024).

300. For a legal database, see *DAIL – the Database of AI Litigation*, THE GEORGE WASH. U., blogs.gwu.edu/law-eti/ai-litigation-database/. For non-legal databases, see *AI Incident Database*, AIID, incidentdatabase.ai/; *AI, Algorithmic and Automation Incidents and Issues*, AIAAIC REPOSITORY, www.aiaaic.org/aiaaic-repository/ai-algorithmic-and-automation-incidents.

301. Tanja Brettel, *Scaling AI in Insurance: A Conversation with Zurich's Christian Westermann*, BAIN & CO. (Jul. 30, 2024), www.bain.com/insights/interview-scaling-ai-in-insurance-a-conversation-with-zurichs-christian-westermann/.

incident,[302] but might lead to higher volumes of damages in the GenAI realm, given its widespread accessibility via a very limited number of suppliers.[303] These two challenges will likely present an ongoing issue to insurance companies working in the AI sector.

Honing more specifically on GenAI, there seem to be a few major risks associated with this specific type of AI technology. These risks obviously exist across the board regarding AI but present a more salient challenge in the context of GenAI. These risks are false information (commonly referred to as hallucinations),[304] bias, privacy violations, intellectual property violations, offensive context, and environmental risks. Aside from IP risks, which are more prevalent in the context of GenAI,[305] it seems that the other risks listed above pose no unique challenge in the AI context. Participants in the research did not indicate any particular significance to GenAI compared to other AI technologies. They did refer to the heightened IP risks created by GenAI and the lack of insurance companies willing to underwrite these risks for AI companies.[306] In a recent interview, Michael Brunero from CFC (a specialist insurance provider) stated in the context of IP coverage, "from an insurance perspective, we tend to be concerned about worst-case scenarios, but these are issues we've dealt with before, albeit on a different scale. The discovery element is more challenging, but it's a question of the scale of the problem increasing rather than being an entirely new problem."[307] This reinforces the overall notion reflected in this paper that it is not the problem that is new but rather the scale of it that is challenging.

Other than heightened IP concerns, for the most part, participants did not believe GenAI should receive different treatment regarding insurance coverage. It presents similar risks when it comes to "silent AI" coverage and potential gap exposures that the industry should work out as soon as possible.

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302. *See infra* note 353 and accompanying text.

303. *See* IOT ANALYTICS, THE LEADING GENERATIVE AI COMPANIES (Dec. 14, 2023), https://iot-analytics.com/wp/wp-content/uploads/2023/12/INSIGHTS-RELEASE-The-leading-generative-AI-companies.pdf.

304. *What are AI Hallucinations?*, IBM, www.ibm.com/topics/ai-hallucinations.

305. *See, e.g.*, Lisa Morgan, *The Intellectual Property Risks of GenAI*, INFO. WEEK (Nov. 1, 2024), https://www.informationweek.com/machine-learning-ai/the-intellectual-property-risks-of-genai; Appel et al., *supra* note 218.

306. Insurers have data to suggest that there are vast differences in the risks between different types of deployments, models, functional domains, and use cases. It is important to note that this is a very narrative-driven assumption by the market rather than based on data and facts. Zoom interview with George Lewin-Smith & Mark Titmarsh, *supra* note 17.

307. David Agnew, *CFC's Michael Brunero on the Legal Landscape Surrounding AI, IP, PII and More*, RISK & INS. (Aug. 7, 2024), riskandinsurance.com/cfc-michael-brunero-artificial-intelligence-intellectual-property/.

GenAI might have accelerated the development of this new evolving market, given its widespread and extensive media coverage. Still, when it comes to its risk landscape, it is not significantly different from other AI branches that are currently being developed and used.

From a client's perspective, there seems to be less of an urge to create and secure a designated AI liability policy. However, "improved wording on current Cyber/ Tech E&O products to better address clients' coverage needs in the AI space and remove any grey areas in terms of coverage would be welcomed"[308] stated Alexandru Lascu, Risk & Insurance Director at UiPath, a global software company that makes robotic process automation software.[309] He also stated that he currently does not see any AI-related exclusions in their liability policies, "but also not explicit coverage, so basically silent coverage, which also comes with grey areas." He believes that if a company sells AI or has AI embedded into their service, "specific client needs could be addressed through endorsements or other amendments on a cyber/ Tech E&O program" to cover any faulty AI accidents. He continued by stating that it is probably too early to purchase a stand-alone AI policy as the data regarding its severity and frequency of risks is lacking. He stated that it would be nice to have explicit coverage, but it depends on the premiums and exclusions of a policy. He currently does not see the added value of purchasing additional policies and coverages, while the traditional ones offered in the market do not have AI exclusions.[310]

A recent article discussing insurance and AI presented a similar line of thought.[311] The article stated, "commercial insurance claims for losses related to the emerging technology have yet to reach the critical mass necessary to spur insurers to adjust policy language or issue widespread exclusions."[312] It adds that we are seeing a couple of insurers that are either explicitly excluding AI coverage or affirmatively covering it by adding it to the language of the policy. A good example of the latter is "Coalition Inc., which in March [2024] introduced an artificial intelligence affirmative endorsement to clarify what is covered by its U.S. surplus lines and Canadian cyber insurance

308. Zoom Interview with Alexandru Lascu, Risk & Insurance Director, UiPath (Jul. 24, 2024).

309. UiPath, www.uipath.com/ (last visited Mar. 12, 2025).

310. Zoom Interview with Alexandru Lascu, *supra* note 308.

311. Matthew Lerner, *Insurers Seek to Keep Pace with Explosive use of AI*, BUS. INS. (May 1, 2024), www.businessinsurance.com/Insurers-seek-to-keep-pace-with-explosive-use-of-AI/.

312. *Id*.

policies."[313] This endorsement was added because Coalition saw, "a rising influence of AI in some of its claims reviews of cyber incidents."[314]

In a formal reply by Coalition to an inquiry whether they believe this path will be the trajectory of AI coverage or an independent AI policy will be developed, they replied, "a cyber insurance policy should give policyholders confidence they have coverage when a malicious actor exploits their digital systems, independent of which specific technical exploit was used. Insurers need to understand how cyber risk develops to provide policyholders with that confidence. For these reasons, we believe cyber insurance policies will absorb the risk of attackers using AI systems."[315] Furthermore, they, "expect Technology Errors & Omissions (Tech E&O) policies to cover the risk defenders take by using AI systems." Lastly, when asked about the greatest challenges of offering AI coverage, Coalition stated, "risk isn't created by the success of AI but by the failures of AI safety. The tech industry has tried and failed to secure much simpler non-AI software systems, so it's unlikely that AI safety will be solved anytime soon. AI has evolved so much in recent months that coverage will have to evolve with it to ensure policyholders stay protected."[316] They flag AI privacy as a major concern; "certain AI use cases may operate without express consumer consent, and others may identify personal traits or interests that impact the consumer. Companies may also open themselves to legal and regulatory risks by using programs not compliant with federal or local guidelines. To help avoid some of these exposures, Coalition recommends creating a company AI Use policy that can help organizations prevent employees from opening their employers up to further risks."[317]

In October 2024, AXA XL, a global insurance and reinsurance company,[318] added a GenAI endorsement to its cyber policy.[319] Limitations for said coverage will be determined, "on a risk-by-risk basis." The endorsement is said to cover "data poisoning, where hackers manipulate or contaminate data used to develop machine learning models; usage rights infringement, where companies do not have appropriate permissions to use copyrighted or

313. *Id. See also*, *Coalition Adds New Affirmative Artificial Intelligence Endorsement to Cyber Insurance Policies*, COALITION (Mar. 26, 2024), www.coalitioninc.com/en-gb/announcements/coalition-adds-new-affirmative-ai-endorsement-to-cyber-policies.

314. Lerner, *supra* note 311.

315. Email from Communications Manager, Coalition, to author (Aug. 22, 2024) (on file with author).

316. *Id.*

317. *Id.*

318. *See* AXA XL, axaxl.com/ (last visited Apr. 17, 2025).

319. Gavin Souter, *Axa XL Adds Generative AI Endorsement to Cyber Policy*, BUS. INS. (Oct. 21, 2024), www.businessinsurance.com/axa-xl-adds-generative-ai-endorsement-to-cyber-policy/.

licensed data; and regulatory violations, such as liabilities resulting from the European Union's AI Act, which provided a legal framework for the use of AI."[320] These endorsements might become a common feature as more companies rely on AI in general and GenAI specifically.

A broker from a large insurance brokerage company also stated that, currently, they do not yet see a need in the market to create an AI Technology policy, given existing Technology E&O policies and their broad coverage. The Cyber, Technology E&O, and Media policies they currently place are broad and typically do not exclude AI. Thus, they believe these policies will remain broad until new claims activity leads insurance companies to rectify and restrict coverage.[321] However, they give an example of some carriers that are clarifying the definition of a security failure and data breach to encompass AI-related security incidents while also extending the criteria for a funds transfer fraud event to include fraudulent instructions delivered via deepfakes or other artificial intelligence technologies.[322] These "coverage innovations"[323] will probably continue to unfold until a good enough reason emerges to exclude them from existing policies. They conclude that "AI is a form of software," and as such, we already have the policies to address it and can tailor it for certain exposures if they arise.[324]

2. "Hyper Scalers" and AI Coverage

The overall approach of opting for existing policies over creating a designated AI policy is also shared with Amazon. Matt Gaschel, Senior Manager of Corporate Risk & Insurance at Amazon,[325] stated that they purchase their cyber insurance policies externally and have not yet faced any significant exclusions for their policies in the AI context. Thus, he concluded that "silent AI" coverage is sufficient at the moment. Amazon presents a unique case study compared to other small to mid-size businesses working with AI, given that it is a "hyper scaler," similar to Google and Microsoft. Their balance sheet enables them to think differently about insurance and leverage alternative risk transfer methods and markets, such as debt and bonds markets, and their own captive insurance company, which Gaschel called a "business enablement

320. *Id.*

321. Zoom Interview with a Senior Broker, *supra* note 299.

322. *See, e.g.*, David Ledet & Evan Knott, *Real Insurance Coverage for Increasing AI Deepfake Risks*, REUTERS (Apr. 11, 2024, 10:00 AM), www.reuters.com/legal/legalindustry/real-insurance-coverage-increasing-ai-deepfake-risks-2024-04-11/.

323. Zoom Interview with a Senior Broker, *supra* note 299.

324. *Id.*

325. Zoom interview with Matt Gaschel, Senior Manager of Corporate Risk & Insurance, Amazon (Jul. 24, 2024).

tool."[326] Traditional insurance markets view them as having increased "concentration and accumulation risks," as insurers view themselves as offering coverage for both the company and its billions of customers. There is a good chance that these "hyper-scalers" will eventually outgrow the traditional insurance market, having no other option but to seek recourse with alternative risk transfer markets or at least a mixture of both.

Furthermore, given that these "hyper-scalers" companies are highly susceptible to GDPR fines, and presumably the EU AI Act fines, they are exposed to a different scale and level of regulatory liability. This is because they are the source who usually provides the infrastructure for AI development (e.g., via bedrock API)[327] but do not have any control over how they are trained and applied by the end users.

Gaschel agreed that, "at face value, there is value in having a standalone AI policy."[328] Still, different types of exclusions and pricing will apply to big companies like Amazon, so it is not clear what the policy will cover or what the coverage actually provides for these policyholders. From his experience, cyber insurance carriers are unsure what AI-related risks they cover in their current policies. Thus, a "wait and see" approach seems like the appropriate path for the near future as to how AI coverage will evolve. It depends on a company's "risk appetite and tolerance; it is not worth the price for what we get."[329] He predicted that in the future, Amazon will only have coverage for their contractual minimal obligations and will not purchase any additional coverage beyond that, as it will simply not be worth it. A broker from a large insurance company echoed this perspective, stating that "insurance is always a 'wait-and-see' approach."[330] Others in the market also predict that "most insurers are expected to follow a 'wait-and-watch' approach, looking at large global carriers as they establish some pricing and loss history."[331]

The designated AI insurance companies mentioned above know the challenges associated with large tech companies. They explicitly acknowledge that these are not their target audience but rather small to medium-sized companies, as well as users, who could more easily benefit from how the traditional insurance market operates. AI insurance companies are better positioned to offer meaningful coverage to these companies, given the

326. For more on Captives, see *infra* Chapter VII.a.

327. *Amazon Bedrock: The Easiest Way to Build and Scale Generative AI Applications with Foundation Models*, AWS, aws.amazon.com/bedrock/.

328. Zoom interview with Matt Gaschel, *supra* note 325.

329. *Id.*

330. Zoom interview with a senior broker, *supra* note 299.

331. Sandee Suhrada, Dishank Jain & Kate Schmidt, *Providing Coverage for AI May Be Huge Opportunity*, INS. THOUGHT LEADERSHIP (Jul. 8, 2024), www.insurancethoughtleadership.com/ai-machine-learning/providing-coverage-ai-may-be-huge-opportunity.

somewhat limited scope and severity of their exposure, unlike "hyper-scalers." The latter companies are significant and vital to the development of the AI industry but might lay outside of the capabilities of the traditional insurance industry as it operates today.

3. The Broker

It is important to briefly note the important yet underexplored role that brokers play in supporting or inhibiting the development of new tech-oriented policies. As the middlemen, brokers, also known as insurance intermediaries, have an essential part and underappreciated power within the insurance industry.[332] They are effectively the gatekeepers of policies, connecting insurance companies and potential clients and providing relevant information to them. However, one participant pointed out that this power could be misused when it comes to the offering and development of new policies.[333] Currently, it seems that most brokers do not see a need to create a new AI-designated policy for their clients. Thus, they are confident in telling their customers that the current policies they have already cover possible AI harm via "silent AI," and they do not need supplemental coverage. Nonetheless, as we have seen above, this is not necessarily true, as traditional policies might expose policyholders to uncovered risks.

Only when more claims arise and insurance companies change the language of their policies, explicitly excluding AI activities from traditional coverage, is it predicted that brokers will shift their position and recommend their clients to shop for AI-tailored policies to get holistic coverage for their activities. They will probably not be incentivized to recommend otherwise until the very last minute, and in most cases, that might be too late as policyholders will have to bear their own risk without the benefits of an insurance policy. Thus, brokers might inhibit the progress of developing new avenues for coverage.[334] The power held by brokerage companies as the connectors of policies' demand and supply could essentially influence the adoption and development of new policies. As a result, the participant points out that brokers might have other incentives that could influence their opinion about the need for a specific AI policy. Chiefly, their desire to cement their power in the

332. Neil A. Doherty & Alexander Muermann, *On the Role of Insurance Brokers in Resolving the Known, the Unknown, and the Unknowable*, *in* THE KNOWN, THE UNKNOWN, AND THE UNKNOWABLE IN FINANCIAL RISK MANAGEMENT 194 (2010); Neil A. Doherty & Alexander Muermann, *Insuring the Uninsurable: Brokers and Incomplete Insurance Contracts* (CFS, WORKING PAPER, NO. 2005/24, 2005), www.econstor.eu/bitstream/10419/25461/1/515325678.PDF.

333. Zoom interview with an anonymous participant (Nov. 26, 2024).

334. *Id.*

insurance industry over insurance companies that want to provide new types of policies to brokers' clients.[335]

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There seems to be an overall consensus among brokers, traditional (non-AI specific) insurance companies, and policyholders that we are not yet in the era of an AI stand-alone policy. A "wait-and-see" approach was repeated throughout the interviews as the best course to take. Companies working on developing AI-designed policies strongly disagree with this assertion. Their existence, ongoing development, and overall growing demand puts a significant dent in this approach. They prove that the industry is slowly shifting into a potentially new and exciting market that will not appeal to all but will be a game changer for some, especially small to medium businesses.

VII. MARKET DYNAMICS & REGULATORY LANDSCAPE

At the intersection of insurance and legislation, three different, yet significant, perspectives emerged from the interviews. The first and most intuitive is particular legislation, known as insurance law, aimed at the insurance market. These are legal obligations and guidelines the legislators set that apply to insurance companies to regulate this market. Second, the role insurers take upon themselves as quasi-regulator entities to nudge and manage the behavior of their policyholders via, among others, the policy terms, claims management, and underwriting process.[336] A vast amount of literature has discussed how insurance can proactively direct the activities of its policyholders in a manner that can mitigate and reduce risks associated with activities covered by the policy.[337] Third, and least intuitive, any rules regulating a

335. *Id.* This is a fascinating topic that merits further empirical research. For more on brokers in a legal context, see, e.g., J. David Cummins & Neil A. Doherty, *The Economics of Insurance Intermediaries*, 73 J. OF RISK & INS. 359 (2006); Hazel Beh & Amanda M. Willis, *Insurance Intermediaries*, 15 CONN. INS. L.J. 571 (2009).

336. *See, e.g.*, Omri Ben-Shahar & Kyle D. Logue, *Outsourcing Regulation: How Insurance Reduces Moral Hazard*, 111 MICH. L. REV. 197 (2012).

337. *See, e.g.*, Angela N. Aneiros, *The Unlikely Pressure for Accountability: The Insurance Industry's Role in Social Change*, 27 TEXAS J. CIV. LIBERTIES & CIV. RTS. 140 (2022); Troy Herr, *Cyber Insurance And Private Governance: The Enforcement Power Of Markets*, 15 REGUL. AND GOVERNANCE 98 (2021); ANJA SHORTLAND, KIDNAP: INSIDE THE RANSOM BUSINESS (2019); Deborah Ramirez et al., *Policing the Police: Could Mandatory Professional Liability Insurance for Officers Provide a New Accountability Model?*, 45 AM. J. OF CRIM. L. 407 (2019); Anat Lior, *Insuring AI: The Role of Insurance in Artificial Intelligence Regulation*, 35 HARV. J. LAW & TECH. 468 (2022); Alexander B. Lemann, *Coercive Insurance and the Soul of Tort Law*, 105 GEO. L.J. 55 (2016); John Rappaport, *How Private*

specific set of activities or risks covered by insurance policies influences how insurance carriers offer (or do not offer) these policies. Regulatory interventions that set, change, or adjust the obligations and liabilities of individuals and companies will consequently affect the insurance market and its products, even if they are not classified as 'insurance law' per se.

The interviews focused on the first and second aspects of insurance intersection with regulation. Still, the third type continued to be brought up by the interviewees as an important aspect of AI insurance, given ongoing regulation attempts worldwide focusing on AI and its ramifications in different disciplines. The section below elaborates on these three topics.

1. Insurance Law

An underwriting manager from a large cyber insurance company stated that, "in general, when it comes to insurance regulation for commercial insurance, a lot of the regulation actions are well-intentioned, but they miss the mark and end up hurting small businesses, especially because they limit the ability of insurance companies to innovate."[338] Rigid requirements set by the legislature might prevent insurance companies from doing better for their policyholders because they have many obligations, such as filings and rate justification, that make their endeavours not commercially viable. In some cases insurance companies see a need, but the regulation states that they cannot offer coverage. This can be restrictive and detrimental to all parties involved, especially consumers.[339]

A different underwriter from a large cyber insurance company stated that the legislator's focus should be on the AI companies and ensuring they have good control over their products and services; hence, setting clear guidelines and guardrails should be the basis of cyber and AI security.[340] Encouraging specific AI policies, they continue, overlooks what is already covered by existing policies and might lead to consumer confusion and lack of clarity in the liability policies market. Another approach for legislators in this area is to get involved when policies become unavailable and insurance companies

Insurers Regulate the Police, 130 HARV. L. REV. 1539 (2017); Peter Kochenburger, *Liability Insurance and Gun Violence*, 46 CONN. L. REV. 1265 (2014); TIMOTHY D. LYTTON, OUTBREAK: FOODBORNE ILLNESS AND THE STRUGGLE FOR FOOD SAFETY 149-52 (2019); Jan Martin Lemnitzer, *Why Cybersecurity Insurance Should Be Regulated And Compulsory*, 6 J. CYBER POLICY 118 (2021); Andrew Verstein, *Changing Guards: Improving Corporate Governance With D&O Insurer Rotations*, 108 VA. L. REV. 983, 984 (2022).

338. Zoom interview with an Underwriting Manager Cyber Lead, *supra* note 296.

339. *Id.*

340. Zoom interview with Chief Underwriting Officer, *supra* note 275.

do not have a financial incentive to offer them, similar to the unavailability of flood policies in certain locations.[341] Otherwise, their premature intervention might be viewed as counterproductive.

Yet another insurance consultant stated that the legislator could implement certain limitations that would allow AI companies to compete in the AI market without excessive costs.[342] He offers as an example, legislation that allows plaintiffs to sue in both federal and state courts. This results in high litigation expenses, which are covered by insurance policies. This practice might lead insurers to leave a specific market if the litigation costs are extremely high for them to transfer and distribute. In that sense, focusing on the federal courts, he believes, as the main avenue for litigation will drive overall efficiency and encourage insurance companies to provide policies for emerging technologies or, at the very least, not withdraw their existing coverage.[343]

As I have elaborated in previous scholarship,[344] there are several possible paths legislators can take in the realm of insurance law, and they move on a spectrum. The most invasive and proactive would be to set a mandatory insurance scheme similar to the current insurance infrastructure applicable to automobiles.[345] A big issue that will likely arise if legislators mandate enterprises to purchase insurance to cover their AI activities is the "silent AI" challenge. Insurance EU recently opposed mandatory AI insurance as it, "can only work for mature and homogenous markets, and this is not currently the case."[346] Setting a mandatory insurance scheme may lead to friction between the current system and the one we envision for AI-related activities. In most cases, neither the policyholder nor the policy provider knows exactly what is covered and what is not. Sorting this in advance can help the AI insurance

341. *See, e.g.*, Moriah Costa, *Lack of Flood Insurance in US Could Cost Trillions of Dollars*, GREEN CENT. BANKING (Oct. 31, 2024), greencentralbanking.com/2024/10/31/lack-of-flood-insurance-in-us-could-cost-trillions-of-dollars/.

342. Zoom Interview with Haim Levy, Insurance Consultant at HL Consultants Insurance and Risk Management (Feb. 11, 2025).

343. *Id.*

344. Anat Lior, George Lewin-Smith & Mark Titmarsh, *The Role for Insurance within AI Regulation*, TESTUDO (Jul. 17, 2024), https://www.testudo.co/insights/ai-regulation.

345. *See, e.g.,* ROBERT E. KEETON & JEFFERY O'CONNELL, BASIC PROTECTION FOR THE TRAFFIC VICTIM: A BLUEPRINT FOR REFORMING AUTOMOBILE INSURANCE (1965). Today, auto liability insurance is mandatory in 49 states and the District of Columbia. Ava Lynch, *Why is Car Insurance Mandatory?*, ZEBRA (July 6, 2022), www.thezebra.com/auto-insurance/policies/why-is-car-insurancemandatory.

346. Kassandra Jimenez-Sanchez, *Insurance Europe calls for European Commission to Scrap AI Liability Directive*, REINSURANCE NEWS (Nov. 8, 2024), www.reinsurancene.ws/insurance-europe-calls-for-european-commission-to-scrap-ai-liability-directive/.

industry progress more efficiently and learn from the mistakes made in the cyber insurance context.

This is the most potentially burdensome way the regulator could get involved regarding the intersection of insurance policies and AI, but it sets an important baseline for consumer protection. The social utility of AI must be extremely clear, similar to how we view automobiles as an essential aspect of our lives. Otherwise, it will be difficult to implement this path without social and political resistance. It will also require a rapid expansion in insurance markets dedicated to AI and commitments from insurers to provide this coverage, given a sharp increase in demand in light of the new regulation. Nonetheless, establishing this mandatory scheme will benefit all sides if such utility is established, focusing on specific sectors of AI development and usage that present more risks (e.g., medicine, banking, etc.). By focusing on mandating coverage in specific instances of AI usages that present broader risks but are still considered essential, the regulator can ensure that AI activities will continue with an added layer of protection.

A recent report examining the interaction between AI liability and insurance recommended "mandating insurance coverage for certain AI applications."[347] These applications focus on instances where AI might lead to catastrophic risks that are too high to be self-insured by big tech companies.[348] The major challenge with this suggestion is that the current insurance system is not up for this task, given the high amounts of damage associated with these catastrophic risks. If it is mandated, the legislature will have to provide some sort of backstop for insurance companies to allow them to offer substantial policies. Otherwise, the low caps that will be administrated will render this tool less effective.

A slightly less intrusive approach will be to set up a reimbursement cap from which the government will compensate policyholders if a correlated event involving AI occurs and multiple policies are triggered simultaneously. This would be similar to the structure set in the Terrorism Risk Insurance Act (TRIA) following the 9/11 attacks.[349] The trigger for the TRIA mechanism is fulfilled once insurers pay losses of $200 million dollars following an act

347. GABRIEL WEIL, MATTEO PISTILLO, SUZANNE VAN ARSDALE, JUNICHI IKEGAMI, KENSUKE ONUMA, MEGUMI OKAWA & MICHAEL A. OSBORNE, OXFORD MARTIN SCH. INSURING EMERGING RISKS FROM AI 3 (Nov. 14, 2024), https://oms-www.files.svdcdn.com/production/downloads/Insuring%20emerging%20risks%20from%20AI%2014%20Nov%2024%20Final.pdf?dm=1732266323.

348. *See, e.g.*, Gabriel Weil, *Tort Law as a Tool for Mitigating Catastrophic Risk from Artificial Intelligence*, SSRN (2024), papers.ssrn.com/sol3/papers.cfm?abstract_id=4694006.

349. 15 U.S.C. § 6701; 28 U.S.C. § 1610; 12 U.S.C. § 248, § 6701; 28 U.S.C. § 1610; 12 U.S.C. § 248.

certified by the Secretary of State as a terror attack. In this case, eligible insurers can "recoup reinsurance for 80 percent of their payments beyond their deductible, which is calculated as 20 percent of the insurer's previous year's direct earned premiums."[350] The cap for aggregated government and private insurer payout for losses is $100 billion annually.[351] This type of mechanism in the AI context can help alleviate insurers' concerns about correlated/aggregated risks and diluted revenue and encourage them to minimize exclusions knowing this backup reserve exists. Conversely, AI risks, even existential ones, are not similar enough to risks posed by terrorism and other wide-scope risks generated by malicious third parties where the government is responsible for protecting its citizens. Thus, this path might suffer political and social resistance as well, with legislators opting to invest the funds into other, more pressing, matters. Still, given the national security significance of AI and the high cap that will be set, it still seems feasible to implement such a method as long as some bi-partisan support is established.[352]

Gaschel from Amazon cites an apt example of why this sort of mechanism may be necessary. Although he stated that the insurance market is unlikely to bear a 24–48-hour cloud outage, similar to the Microsoft global software malfunction due to a problematic CrowdStrike Incident in July 2024,[353] Gaschel predicts that insurers would be eliminated from the market if this were to happen, given the high costs associated with such a long outage.[354] In this sense, there is logic in having the legislator act as a backstop to the traditional insurance market and practice. However, this type of legislation is usually rear-facing after a catastrophic event has already happened, similar to the 9/11 attack that led to the legislation of TRIA. Thus, until such a catastrophic event happens, a legislative backstop is unlikely to be established.

Other possible paths, in order of ascending intrusiveness, include (1) setting up a general AI insurance risk framework to provide overall guidelines for insurers in the context of AI policies; (2) creating a compensation fund, general to AI or classified by AI sector and activity; and (3) offering limited

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350. Kenneth S. Abraham & Tom Baker, *What History Can Tell Us about the Future of Insurance and Litigation after COVID-19*, 71 DEPAUL L. REV. 169, 195–196 (2022).

351. 15 U.S.C. §6701(103)(e)(B)(2)(A).

352. *See, e.g.*, *Bipartisan House Task Force Report on Artificial Intelligence*, *supra* note 28.

353. Emily Atkinson, *Global IT Chaos Persists as Crowdstrike Boss Admits Outage Could Take Time to Fix*, BBC (Jul. 19, 2024), www.bbc.com/news/live/cnk4jdwp49et; Jerry Gupta, *CrowdStrike Incident: A Wake Up Call for Insurance of Digital – and AI – Risk*, ARMILLA AI (Jul. 22, 2024), www.armilla.ai/resources/crowdstrike-incident-a-wake-up-call-for-insurance-of-digital—-and-ai—-risk.

354. Zoom interview with Matt Gaschel, *supra* note 325.

liability where AI providers or users have obtained specific coverage and carry out specific safety measurements agreed upon by contract or policy.

First, a general AI insurance risk framework can follow suit of the 2021 New York Cyber Insurance Risk Framework.[355] This Framework identifies six priorities for best practice, including establishing cybersecurity expertise, educating policyholders, and evaluating systemic risk, all of which are also highly relevant in the AI context. This hands-off approach does not offer clear regulatory instructions but rather suggests general guidelines for insurance companies working in this field. It provides flexibility and a soft regulatory nudge in the form of standards and principles, enabling insurers to better understand what is expected of them and how they can offer improved services this early in the process of AI implementation into our commercial market. As such, it is a welcomed starting point in this novel field where regulatory sources are lacking.[356] Claire of Relm stated that an AI EU user's guide or framework would be helpful as parts of the Act are already in effect.[357] She stated that while big companies have the resources to navigate the EU AI regulation, small companies and entrepreneurs lack the bandwidth to understand their duties under the Act. This might stifle growth and development in this area. In that sense, a user framework guide could be of added value to the AI industry.[358]

Second, a dedicated AI compensation fund could be established by law. A similar proposition was made in 2017 by the European Parliament in its *Report with Recommendations to the Commission on Civil Law Rules on Robotics* with regard to all AI entities.[359] Section 59(d) of the resolution considers the creation of "a general fund for all smart autonomous robots" or "an individual fund for each and every robot category and whether a contribution should be paid as a one-off fee when placing the robot on the market or whether periodic contributions should be paid during the lifetime of the

355. Insurance Circular Letter No. 2 from Linda A. Lacewell, Superintendent, N.Y. Dep't Fin. Servs., to All Authorized Property/Casualty Insurers, N.Y. State Dep't of Fin. Serv. (Feb. 4, 2021), www.dfs.ny.gov/industry_guidance/circular_letters/cl2021_02.

356. New York has already published a circular letter concerning the usage of AI systems in the underwriting process. *See* Insurance Circular Letter No. 7 from N.Y. Dep't Fin. Servs., to All Insurers Authorized to Write Insurance in New York State (Jul. 11, 2024), www.dfs.ny.gov/industry-guidance/circular-letters/cl2024-07.

357. Zoom Interview with Claire Davey, *supra* note 101.

358. *Id.*

359. European Parliament Resolution of 16 February 2017 with Recommendations to the Commission on Civil Law Rules on Robotics, 2017 O.J. C. 252/250. Most of the attention was focused on Section 59(f) of this report, which suggested the creation of a new legal status of "electronic persons.". *Id.*

robot."[360] This discussion did not consider GenAI, as it was not publicly available yet and mostly focused on the physical manifestation of AI technologies. Nonetheless, the notion of setting up a fund and splitting the contribution between AI developers and users has been repeatedly brought up, especially in the context of autonomous vehicles.[361] This approach seems premature at the moment, given the state of the technology and the high burden it puts on developers and users of AI. It does provide a safety net in a field that is currently alarming society, but it is likely to do so in a non-structured way as no clear categorization of AI usage currently exists, especially given the ubiquity of GenAI.[362]

An interesting, related path is a group captive approach.[363] A captive insurance company is "an insurance subsidiary formed to provide risk mitigation services to its parent company."[364] In other words, instead of going to the insurance market and purchasing a commercial insurance policy, a parent company retains the cost of coverage via its captive. A group captive is usually founded by large corporations, such as Microsoft and Goldman Sachs. However, it can also appeal to mid-sized companies that want "to lower their insurance costs and control other aspects of their insurance program."[365] They could either establish a new group captive or join an existing one. These mid-sized and large companies could set up an inclusive "industry group captive" to manage AI-associated risks instead of purchasing an insurance policy from a traditional insurance provider. Indeed, Gaschel of Amazon mentioned this approach when discussing managing Amazon's overall risk landscape, given its size and cost-effectiveness in creating subsidiary insurance rather than

360. *Id.* at 18.

361. *See generally*, Kenneth S. Abraham & Robert L. Rabin, *Automated Vehicles and Manufacturer Responsibility for Accidents: A New Legal Regime for a New Era*, 105 VA. L. REV. 127 (2019); Carrie Schroll, *Splitting the Bill: Creating a National Car Insurance Fund to Pay for Accidents in Autonomous Vehicles*, 109 NW. U. L. REV. 803 (2015); Jin Yoshikawa, *Sharing the Costs of Artificial Intelligence: Universal No-Fault Social Insurance for Personal Injuries*, 21 VAND. J. ENT. & TECH. L. 1155 (2019).

362. *See, e.g.*, McKinsey & Company, *The State of AI in Early 2024: Gen AI Adoption Spikes and Starts to Generate Value*, MCKINSEY & CO. (May 30, 2024), www.mckinsey.com/capabilities/quantumblack/our-insights/the-state-of-ai.

363. Sean Flavin, *Group Captives 101: What is a Captive Insurance Company?*, CAPTIVE RES. (Jul. 30, 2021), www.captiveresources.com/insight/group-captives-101-what-is-a-captive-insurance-company/.

364. PATRICIA BORN & WILLIAM T. HOLD, INS. INFO. INST., A COMPREHENSIVE EVALUATION OF THE MEMBER-OWNED GROUP CAPTIVE OPTION 3 (April 2021), www.iii.org/sites/default/files/docs/pdf/captives_wp_04062021.pdf.

365. *Id.* at 2.

finding a policy on the open market.[366] This industry group-captive approach could benefit the entire industry, giving it a comprehensive and stable safety net, thus signaling to the regulators, users, and developers of AI the strength and potential growth of the field.[367]

Gaschel clarifies that, in his experience, using a captive in the cyber context is typically connected to companies' contractual minimum requirements set by a third party. For example, if a contract states that the captive parent company must carry a specific amount of money in cyber coverage to indemnify the customer if an accident happens. Those minimum thresholds are usually low (ranging between $10-$25 million). As such, "any captive would be challenged to provide coverage for any systematic cyber event that would quickly exhaust any surplus."[368] Gaschel views this as a "vehicle to take a primary layer and utilize the insurance market in an excess capacity or fill the gaps."[369] However, he continues, that would highly depend on the companies' level of risk tolerance and the health of the captive. This could also apply in the AI context, enabling the captive to act as an important first protection layer while still requiring other risk-managing mechanisms to handle any surplus.

Third, a possible middle approach would be mandating limited liability where AI providers or users have obtained specific coverage and consulting provided by risk management companies, including but not limited to insurers, attestation, and audit firms.[370] Combined with a compensation fund, section 59(c) of the EU resolution offers a similar line of thought: "the manufacturer, the programmer, the owner or the user to benefit from limited liability if they contribute to a compensation fund."[371] This approach incentivizes AI developers and users to purchase policies to benefit from limited liability under certain circumstances. By doing so, it increases the safety net insurance products offer. On the other hand, it is still difficult to decide which specific coverage or services should be mandated, given the novelty of AI and the lack of information surrounding its risk mitigation processes. As a result, this seems like an uncertain method to implement until more information is

366. Zoom interview with Matt Gaschel, *supra* note 325.

367. For more on group captive insurance, see Robert E. Bertucelli, *Captive Insurance Companies*, THE CPA J., Feb. 2011, at 60 dev.mesquitecaptive.com/wordpress/wp content/uploads/2015/02/Captive_Insurance_Companies.pdf.

368. Email correspondence with Matt Gaschel, Senior Manager of Corporate Risk & Insurance, Amazon, to author (Jan. 22, 2025) (on file with author).

369. *Id.*

370. *See, e.g.*, Schellman Inc., which offers an ISO certification designed for AI technologies. *ISO 42001 Certification*, SCHELLMAN, www.schellman.com/services/ai-services/iso-42001 (last visited Apr. 17, 2025).

371. European Parliament Resolution of 16 February 2017 with Recommendations to the Commission on Civil Law Rules on Robotics, 2017 O.J. 252/250.

gathered, and it becomes clearer what safety measurements could and should be mandated to benefit both policyholders and insurance carriers.

When presented with these different approaches, the interviewees generally emphasized that most types of legislative intervention, aside from providing general guidelines and some clarity regarding the "silent AI" issue, will probably do more harm than good. This is especially true early in the life cycle of AI and its risk management strategies. When asked if insurance companies' collaboration with policymakers and regulatory bodies would be beneficial in developing standardized AI liability insurance approaches, an experienced underwriter from a large cyber insurance company replied that insurance usually comes because of liability. They stated, – "we are oftentimes the tax due to lack of regulatory or risk management action."[372] This can possibly incentivize regulatory bodies to set rules for a more symbiotic relationship with insurance companies to encourage proactive actions to mitigate said cost.

Given the current trajectory of AI development, the lighter touch paths seem more appropriate to allow flexibility and enable innovation for all stakeholders. Insurance companies will be better positioned to leverage their data and risk-managing properties if the regulations give them a clearer starting point. Or as one participant framed it – "regulators should regulate to a certain extent. But that said, business has to flow freely."[373] Thus, even if we do opt for a "wait-and-see" approach, this does not mean the regulator should not proactively try to ensure that the creation and development of an AI policy is accessible and feasible for those who desire it.

2. Insurers as Quasi-Regulators and Consumer Education

Extensive literature exists within insurance law addressing the potential role of insurers as quasi-regulators. This work explores the insurer's role in influencing the risk appetite of its policyholders.[374] It discusses the insurance industry's different behavior channelling mechanisms utilized to educate its policyholders on, and spur them towards, safer conduct. These include risk-based pricing, insurance underwriting, contract design, claims management, loss prevention service, implementing private safety codes, research and education, and engagement with public regulation. Recently, this body of literature has been heavily criticized.[375] Its opponents claim that insurance carriers' ability to channel their policyholders' behavior in practice is

372. Zoom interview with a Chief Underwriting Officer, *supra* note 168.

373. Zoom interview with Head of North America Cyber and E&O, *supra* note 144.

374. *See, e.g.*, Ben-Shahar & Logue, *supra* note 336.

375. *See, e.g.*, Kenneth S. Abraham & Daniel Benjamin Schwarcz, *The Limits of Regulation by Insurance*, 98 IND. L.J. 215 (2022).

significantly more limited than hypothesized and, in some cases, non-existent. Nonetheless, policies covering innovation, especially AI, can benefit from the quasi-regulatory approach to fill the legislative void as we await meaningful AI regulation.

Insurance enables its policyholders to encourage innovation while also prompting them to implement safety measurements and providing remedies for when these protections are inadequate.[376] Even though the insurance industry is private and driven by profit, insurance carriers and policyholders have an alignment of interests. Insurance carriers have an incentive to mitigate and even eliminate harms caused to their policyholders as this means they will not have to reimburse them and get to profit from their premiums. Policyholders also have an incentive to reduce or prevent harm as risk-avoiders; the purpose for which they purchased a policy in the first place (assuming it was not mandated by law). This alignment of interests is crucial to understanding insurance's role and how governments should strive to ensure its availability to all who desire or are required to purchase it.

Some interviewees felt that the terminology of "quasi-regulator" does not hit the mark because the insurer does not "regulate" the policyholder in the traditional sense but advises them on safety measurements and appropriate education as part of their risk management services and toolkit. Regardless of the term used, which might be an appropriate topic for further research, individuals from the insurance industry who participated in the research were unequivocal about their important role in assisting policyholders in navigating these uncharted waters. They view it as part of their inherent duty towards their clients, such as HSB, which has signaled itself as a supporter of innovation since the 1800s.[377] Though in practice they might fall short of this target, this supportive agenda is clearly stated by these insurers as they continue to provide loss prevention services and education as part of their business obligations.

All participants put a big emphasis on the consumer education aspect of this emerging market by the insurers. Claire of Relm Insurance stated that, "insurance plays a key role in driving better industry standards,"[378] and that supporting startups in this context enables insurance companies to "make innovation resilient," which is one of Relm's explicit missions.[379] The Head of North America Cyber and E&O at WTW emphasized the need to encourage and provide best practices to their policyholders by educating and training personnel and increasing overall awareness of the perils AI presents. They

376. Lior, *supra* note 53.

377. Zoom Interview with Michael Crowl, AI product manager, HSB (Jul. 22, 2024).

378. Zoom Interview with Claire Davey, *supra* note 101.

379. *Id.*

referred to this awareness as the "most critical" aspect of covering AI risks today.[380] This could be done, for example, by incentivizing policyholders to have an in-house AI policy in place to have more clarity, certainty, and awareness when risks materialize; a practice companies are now starting to follow.[381]

Establishing in-house policies and procedures for AI-based applications for companies who are seeking coverage is an important element for insurers working in this area. Google recently changed its user policy, allowing customers to use its AI in 'high-risk' domains, such as healthcare and social welfare, as long as human supervision exists.[382] Underwriters stated that, currently, employees use AI in their scope of employment with no clear guidelines or understanding of the technology and its risks. Creating in-house policies in different sectors helps underwriters understand the predicted nature, scope, and risks involved with using AI within a potentially covered policyholder and adjust the terms and scope of the policy accordingly. It seems that given the lack of clarity regarding AI regulations in the US and elsewhere, including the way the EU AI Act will be enforced, setting up internal rules of usage is imperative for insurance to be able to offer coverage.

Trust and confidence in new technologies are essential for offering AI risk solutions. Insurance carriers play an immensely important role when offering policies to cover AI. In this way, they signal to potential consumers and the market overall that despite its inherent uncertainty, risks associated with AI can be priced and managed. For example, when discussing loss prevention services and other means of educating AI vendors, users, and developers about AI, virtually all interviewed from the insurance industry agreed that insurance companies have an important role in ensuring their clients educate themselves. Claire from Relm gave an example of partnering with an AI governance technology company that can help with auditing and managing daily AI-related governance risks.[383]

Insurance carriers play a significant role in risk reduction through policyholder education. Swiss Re, for example, launched Responsible Artificial Intelligence (RAI) "as a service solution, an innovative approach to provide assessments of AI, machine learning and analytics models for trustworthiness, robustness, accuracy, transparency, ethical use and governance of data and

380. Zoom interview with Head of North America Cyber and E&O, *supra* note 144.

381. Alaura Weaver, *Every Company Needs a Corporate AI Policy*, WRITER, writer.com/blog/corporate-ai-policy/.

382. Kyle Wiggers, *Google Says Customers Can Use its AI in 'High-Risk' Domains, So Long As There's Human Supervision*, TECHCRUNCH (Dec. 17, 2024), techcrunch.com/2024/12/17/google-says-customers-can-use-its-ai-in-high-risk-domains-so-long-as-theres-human-supervision/.

383. Zoom Interview with Claire Davey, *supra* note 101.

AI."[384] This enables insurance companies to offer accurate policies and instruct their current and potential policyholders on what they should change to reduce risks and, as a result, receive better coverage via their policies. Armilla AI, who is in collaboration with Swiss Re as part of their business model, stated that, indeed, the biggest challenge in the future will be ensuring sufficient education of the policyholders to understand their exposure to risks and act to mitigate them.[385]

Lauren Finnis of WTW stated that, "education is a vital component."[386] She gives the example of annual cyber assessments in the context of GenAI to help prevent risks in advance rather than just manage them once they occur. More specifically, she stated that this training, "should cover what should and should not be input into large language models, how to craft effective prompts, and how to leverage these tools in a lower-risk manner." Finnis refers to another important aspect of education: being "able to explain the black box." This does not necessarily mean you have to be able to replicate it, but you do need to be able to explain how it reached its harmful conclusion.[387]

From a client's perspective, when it comes to consumer education and providing loss prevention tools, it could be argued that it is too early for AI insurance companies to effectively provide loss mitigation services or similar services that could reduce losses at this point. We can also see this lack of efficiency in the cyber insurance context, where many claim that even when you collaborate with cyber security firms, they do not necessarily have accurate data to provide these mitigation services.[388] Alexandru Lascu at UiPath stated that companies could provide, as a loss control measure, "a white paper on the best practices of using AI tools and reducing your exposure to

384. Armilla AI Inc., *RAI Institute Partners with Armilla AI to Scale Adoption of its Responsible AI Assessments with Company's Performance Guarantee for AI Products*, PR NEWSWIRE (Dec. 13, 2023), www.prnewswire.com/news-releases/rai-institute-partners-with-armilla-ai-to-scale-adoption-of-its-responsible-ai-assessments-with-companys-performance-guarantee-for-ai-products-302014278.html.

385. Rayne Morgan, *Added Exposure Paves Way for Emerging AI Insurance Market, Expert Says*, INS. NEWSNET (Sep. 3, 2024), insurancenewsnet.com/innarticle/added-exposure-paves-way-for-emerging-ai-insurance-market-expert-says.

386. R&I Editorial Team, *supra* note 81.

387. *Id*.

388. It has been shown that cyber insurers often do very little to limit risk-taking behavior, do not condition premiums on effective discounts, and principally devote their efforts to ex-post-risk management rather than ex-ante. *See, e.g.*, Daniel W. Woods & Tyler Moore, *Does Insurance Have a Future in Governing Cybersecurity?*, IEEE SEC . & PRIV. (Sept. 2019); Tom Johansmeyer, *The Cyber Insurance Market Needs More Money*, HARV. BUS. REV. (Mar. 10, 2022), hbr.org/2022/03/the-cyberinsurance-market-needs-more-money.

losses," depending on the company and the verticals in which they operate.[389] This could be an effective initial means of providing valuable information to those who use AI in their work or everyday lives.

On the other hand, some participants expressed skepticism regarding what the industry should encourage their policyholders towards, given the current lack of data regarding proven safe practices. There is an overall agreement that insurance carriers should prompt their policyholders to thoroughly test their services and adopt structured AI frameworks and policies as part of the development and deployment of their AI products. However, as Woods of Coalition phrased it, the current quasi-regulatory approach adheres mostly to general "prompting and nudging" towards generic practices rather than recommending and rewarding specific techniques. With that in mind, it is probably too soon to implement strict "carrot and sticks" limitations.[390]

As a result, though all insurance carriers who participated in this research expressed their deep sense of duty to provide their policyholders with adequate tools to mitigate risks, in practice, those tools are too obscure to be deemed useful at the moment. Insurance carriers in the AI realm are in a good position to eventually provide these tools as they will have a front-row seat in the evolution of claims related to AI accidents. Once they gather that information, they can implement it into their policies and standards, living up to their reputation for influencing their policyholders to act in a safer manner. Until then, it is comforting to know that they consider themselves an ally to the safety of their policyholders and hopefully will be able to translate that into life-saving actions and guidelines in the near future.

3. Liability Regulation as Insurance Regulation

Mark Titmarsh, Co-Founder of Testudo, stated that, "new laws and regulations can help create new insurance markets."[391] He gave the cyber insurance market as an example. Security breach notification legislation created a regulatory obligation to report breaches to the regulator and residents.[392] This opened the door for regulatory fines and lawsuits, accelerating the need

389. Zoom interview with Alexandru Lascu, *supra* note 308.

390. Zoom interview with Daniel Woods, *supra* note 80.

391. Zoom Interview with Mark Titmarsh, *supra* note 123. *See also*, Ebert, *supra* note 264.

392. *Security Breach Notification Laws*, NSCL, www.ncsl.org/technology-and-communication/security-breach-notification-laws ("All 50 states, the District of Columbia, Guam, Puerto Rico and the Virgin Islands have laws requiring private businesses, and in most states, governmental entities as well, to notify individuals of security breaches of information involving personally identifiable information."). For more on California, see *Data Security Breach Reporting*, STATE OF CALIFORNIA, DEPARTMENT OF JUSTICE, oag.ca.gov/privacy/databreach/reporting.

to create a cyber insurance market. Some insurance carriers refused to pay a cyber-related loss, claiming that it was not covered under their policy, and breach of contract claims started to emerge. This accelerated the creation of a cyber insurance market, leading to affirmative and standalone cyber coverage.[393] "Mixing big scary losses and regulation," Titmarsh continued, can set a precedent for a new insurance market, especially if exposures are excluded from traditional policies. He states that these conditions are materializing in the AI context with different regulations in the EU, UK, and the US. These types of technology regulations have an enormous effect on the insurance market and the development of new policies.[394]

An underwriting manager from a large cyber insurance company emphasized the importance of regulations as they, "set expectations" for insurance companies in their underwriting process.[395] They generally focus on three aspects of the enforcement mechanism of a given regulation: (1) the ability of the attorney general (or other government agency) to bring regulatory action for fines or penalties; (2) whether the regulation creates a private right of action and; (3) whether the regulation sets statutory damages. These three elements significantly impact the insurer's risk exposure level.[396] For example, Illinois's Biometric Information Privacy Act (BIPA)[397] has both a private right of action and statutory damages, resulting in many significant claims. As a result, maintaining coverage by the insurance carriers highly depends on whether they feel comfortable that the policyholder complies with the Act. They can also minimize coverage via exclusions of certain industries (as a last resort), co-insurance, and elevated premiums. Regulations in the US that include these elements might lead insurance companies to limit coverage under their policies, charge higher premiums, scrutinize applicants for insurance more closely, or all three. This is especially true in the EU context, where the AI Act sets a variety of statutory fines, such as €35 million or 7% of global annual turnover (whichever is higher) for the most serious violations, such as performing prohibited AI practices. Other fines set in the EU AI Act are up to €15 million or 3% of global annual turnover (whichever is higher) for noncompliance with other obligations under the Act and fines of up to €7.5 million or 1.5% of turnover (whichever is higher) for providing incorrect, incomplete, or misleading information to notified bodies or competent authorities.[398]

393. Zoom Interview with Mark Titmarsh, *supra* note 123.

394. *Id*.

395. Zoom interview with an Underwriting Manager Cyber Lead, *supra* note 296.

396. *Id*.

397. 740 ILL. COMP. STAT. 14/1 (2008).

398. Commission Regulation 2024/1689, art. 99, 2024 O.J. L.

In the EU AI Act context, Zurich Insurance's Christian Westermann takes an optimistic approach.[399] He stated that, "the EU AI Act has outlined what type of AI is considered as high, medium, or low risk across industries, including insurance," assisting the insurance industry to better classify and identify different types of AI activities.[400] On top of that, "the AI Act uses a rather broad definition of AI. As such, insurance carriers need to assess if and how they are impacted by this regulation."[401] Other participants in the research have articulated this notion, focusing on how global regulation can impact the operation of insurance carriers. Woods of Coalition stated that the categories classified as high-risk applications by the AI Act are very useful in "helping drive increased underwriting scrutiny, leading to a more limited underwriting appetite."[402]

Another interesting legislation in this area is California's bill to prevent AI disasters, SB 1047.[403] The bill received support from AI experts but faced fierce objections from the AI industry.[404] In August, the bill was weakened before its final vote, following advice from Anthropic and other companies working on AI.[405] The bill aimed to prevent AI catastrophes that lead to loss of lives or damages from cybersecurity events of over $500 million. It did so by holding AI developers liable. The amendments gave California's government less power to hold AI labs accountable. Despite these attempts to soften the bill, many still had serious concerns, as manifested via a letter written by eight congress members representing California asking Governor Newsom to veto the bill.[406] They claimed that the bill, "would not be good for our state, for the start-up community, for scientific development, or even for protection against possible harm associated with AI development." These

399. Brettel, *supra* note 301.

400. Id.

401. Id.

402. Zoom interview with Daniel Woods, *supra* note 80.

403. SB-1047, 2024 Leg., Reg. Sess. (Cal. 2024).

404. *See e.g.*, Maxwell Zeff, *California's Legislature Just Passed AI Bill SB 1047; Here's Why Some Hope the Governor Won't Sign It*, TECHCRUNCH (Aug 30, 2024), techcrunch.com/2024/08/30/california-ai-bill-sb-1047-aims-to-prevent-ai-disasters-but-silicon-valley-warns-it-will-cause-one/.

405. Maxwell Zeff, *California Weakens Bill to Prevent AI Disasters before Final Vote, Taking Advice from Anthropic*, TECHCRUNCH (Aug. 15), techcrunch.com/2024/08/15/california-weakens-bill-to-prevent-ai-disasters-before-final-vote-taking-advice-from-anthropic/.

406. Letter from Members of U.S. Cong., to Gavin Newsom, Governor of Cal. (Aug. 15, 2024), democrats-science.house.gov/imo/media/doc/2024-08-15%20to%20Gov%20Newsom_SB1047.pdf.

concerns and others eventually led to the governor vetoing the bill in September 2024.[407]

Colorado passed its AI Act in May 2024, which will be enforced starting February 1, 2026.[408] The Act imposes obligations on developers and employers of high-risk AI systems.[409] The Act, "is enforced exclusively by the Colorado Attorney General; violations of its requirements are deemed to be an unfair trade practice under the Colorado Consumer Protection Act, with penalties of up to $20,000 per violation."[410] This will most likely influence the ability and willingness of insurance companies to offer liability policies, in their current format, to policyholders affected by this Act. More generally, the need for insurance companies to follow the regulation of individual U.S. states, rather than one encompassing regulation similar to the EU, is constraining their ability to react quickly to new demands in the market. AI legislation seems to be moving on a state-by-state basis rather than a federal approach, which requires insurance companies to do the proper research before being able to offer AI coverage based on their particular state. This is not new, as insurance companies are regulated on the state level,[411] but currently it presents difficulties given the vast differences states are taking to regulate AI.

A recent piece published by the *Insurance Thought Leadership* predicted that, "regulators globally are likely to soon demand safeguards and risk management practices around AI use, which will likely include insurance coverage."[412] Though this seems an over-optimistic approach as to the way the regulator will intervene regarding mandatory insurance policies, the piece continues to say that "even if these regulations do not mandate insurance, provisions for hefty fines may drive companies to seek insurance coverage for these risks." Lastly, the piece also states, as has been articulated by participants of this research, that businesses could be compelled to purchase coverage "if there were an increase in the severity and frequency of AI damages

407. Letter from Gavin Newsom, Governor of Cal., to Members of U.S. Cong. (Sep. 29, 2024), www.gov.ca.gov/wp-content/uploads/2024/09/SB-1047-Veto-Message.pdf.

408. SB24-205, 75th Gen. Assemb., Reg. Sess. (Colo. 2024).

409. *Id*.

410. Alex Siegal & Ivan Garcia, *A Deep Dive into Colorado's Artificial Intelligence Act*, NAT'L ASS'N OF ATT'YS GEN. (Oct. 26, 2024), www.naag.org/attorney-general-journal/a-deep-dive-into-colorados-artificial-intelligence-act/#:~:text=The%20CAIA%20creates%20and%20imposes,high%2Drisk%20artificial%20intelligence%20systems.&text=For%20developers%2C%20this%20duty%20extends,uses%20of%20their%20AI%20product.

411. 15 U.S.C. § 1012(a) ("The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.").

412. Suhrada et al., *supra* note 331.

and losses," (i.e., when claims arise), and the need will become more apparent.[413]

Gaschel from Amazon specifically mentioned the volatile and unpredictable AI regulation worldwide. He gives the example of cyber insurers as they "struggle to keep pace with the regulation because [they] don't know when one of these countries will change" their regulation.[414] In this case, committing to a policy a year in advance is hard on both sides as the regulatory landscape can significantly change within that period.[415]

Gaschel also mentioned the U.S. court system's vast influence on the insurance market and coverage of emerging technologies, given that the US is very litigious in nature.[416] By that, he means that the U.S. court system produces what he refers to as "nuclear or even thermo-nuclear verdicts,"[417] with extremely high punitive damages. This may deter insurance companies from offering coverage and significantly affect the "hyper-scalers" companies as those are sued more often than smaller AI companies. This should be accounted for when considering the role of insurance, the legislator, and the court system in encouraging or discouraging specific types of insurance products.

Ultimately, governments and regulators face deep challenges when regulating AI technology because they still do not understand the technology well enough. Finnis of WTW stated that this presents a challenge for insurance companies as they need to create their own frameworks and benchmarks.[418] There is guidance out there and best practices given by experts, but insurance companies cannot afford to wait to do "what is legally required" of them, because, "the legal requirement is not likely to encompass all that an organization needs to do from an enterprise risk management framework."[419] When asked specifically what legislators should do in the AI insurance context, she replied, "they could certainly get more granular in the recommendations relative to frameworks." Some insurance departments, including the NAIC (National Association of Insurance Commissioners), have different types of guidelines that ask for a framework but do not provide any type of baseline. Another challenge here is that once you provide a standard or baseline, there is no incentive to do better, essentially becoming the maximum a company is willing to do (i.e., the legislative ceiling) rather than the bare

413. *Id.*

414. Zoom interview with Matt Gaschel, *supra* note 325.

415. *Id.*

416. *Id.*

417. In the IP context, "Something like 60% of nuclear settlements — meaning damages awards exceeding $10 million — are IP-related." Agnew, *supra* note 307.

418. Zoom Interview with Lauren Finnis, *supra* note 149.

419. *Id.*

expected minimum (i.e., the legislative floor). However, Finnis continues, there is a need for "recommended thresholds of viability," such as what to do before taking the human out of the loop and similar basic checklist items.[420] On the other hand, one can claim that insurance companies have an incentive to treat these recommendations as the legislative floor and not the ceiling. This is because insurance companies are incentivized to do more for their policyholders than the bare minimum due to competition and reputation considerations.

All liability law is, to a certain degree, liability insurance law creating new markets or, at the very least, expanding existing ones.[421] They change and readjust the existing liability regime, thus altering the risk landscape for the insurance market. This may lead to simple adjustments and tweaks of existing policies or the creation of a new insurance market altogether. Thus, legislation influencing insurers is, in fact, broad in scope, creating a strong connection between the insurance industry and the law.

VIII. CASE STUDIES, INDUSTRIES & SECTORS

Swiss Re, the world's largest reinsurance company, recently published a paper ranking current and future risks on the industry level in the short term (2024-2025) and the long term (2032-2034), focusing on the probability and severity of AI risks per industry.[422] In the short term, IT services, energy and utilities, and health and pharma have the highest risk rank overall. IT services earned this rank as they are the "first movers" in this industry, developing the code, which leads to the high probability of materializing risks.[423] Both the energy and utilities, as well as the health and pharma industry, received low severity ranks, as they are relatively not in widespread use at the moment, but a high probability risk rank given the high likelihood of things going wrong in these sectors.

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420. *Id.*

421. Gerard Van Loon, *Under the Regulatory Spotlight: How European Fis are Adapting their Insurance Needs for 2025*, THE INSURER (Dec. 27, 2024), www.the-insurer.com/ti/viewpoint/under-the-regulatory-spotlight-how-european-fis-are-adapting-their-insurance-2024-12-27/.

422. Simon Woodward, Nikhilmon O U & Mitali Chatterjee, *Tech-Tonic Shifts: How AI Could Change Industry Risk Landscapes*, SWISS RE (May 23, 2024), www.swissre.com/institute/research/topics-and-risk-dialogues/digital-business-model-and-cyber-risk/ai-and-the-industry-risk-landscape.html. The report only focused on six risk categories: Data bias or lack of fairness, cyber incident risks, Algorithmic and performance-related risks, Lack of ethics, accountability, and transparency risks, Intellectual property (IP) risks, and Privacy risks. *Id.*

423. As is evident from Gaschel's interview, detailed above. Zoom interview with Matt Gaschel, *supra* note 195.

In the long-term evaluation, health and pharma climbed to first place in their overall risk ranks, given the predicted widespread usage of AI in this sphere. Ranked second is the mobility and transportation industry, given the important role automation is predicted to have in the next decade and the errors and underperformance likely to accompany it. In third place, the report ranked the energy and utilities industry again as risk frequency increases the more AI becomes entrenched in this industry. Other industries that are mentioned but have an overall low-risk rank are agriculture, food & beverages (10 in the short term and 9 in the long term), manufacturing (8 in both terms), and Financial & Insurance Services (6 in the short term and 7 in the long term).

The results of the report show that the industries involved with using this technology matter. The context of AI usage is important, especially in more susceptible and vulnerable industries with correlated/accumulated risks. These industries can lead to greater scope of harm, which is what Swiss Re refers to in its report as "severity ranks." Other than the traditional exclusions we usually see in policies underwritten by insurance carriers, such as force majeure and terrorism, the interviewees did not reveal any specific sector that they believe the insurance industry will choose not to cover. Different industries will receive different policy terms. Thus, caps, co-pays, and deductibles are important in insurance carriers' ability to operate in these vulnerable and critical industries. They will still choose to do so, but the meaningfulness of the policy will evolve as more data regarding the actual probability and severity of harm will crystallize.

Focusing on the healthcare sector, there has been discussion regarding the utility of a "well-designed AI liability insurance" that can "mitigate predictable liability risks and uncertainties in a way that is aligned with the interests of health care's main stakeholders, including patients, physicians and health care organizations leadership."[424] Stern, Goldfarb, Minssen, and Price claimed that, "a market for AI insurance will encourage the use of high-quality AI, because insurers will be most keen to underwrite those products that are demonstrably safe and effective."[425] They argue that efficient AI insurance products will be able to "reduce the uncertainty associated with liability risk for both manufacturers — including developers of software as a medical device — and clinician users and thereby increase innovation, competition, adoption, and trust in beneficial technological advances."[426] This is a good example of the quasi-regulator approach in the healthcare context, showcasing how good insurance can contribute to a better understanding and implementation of technologies, especially AI. As such, we see that there is a core

424. Ariel Dora Stern, Avi Goldfarb, Timo Minssen & W. Nicholson Price II, *AI Insurance: How Liability Insurance Can Drive the Responsible Adoption of Artificial Intelligence in Health Care*, 3 NEJM CATALYST 1, 1 (2022).

425. *Id.*

426. *Id.*

belief that given the significance of AI in the healthcare sector and the inherent risks associated with it, insurance for AI assumes an important role in supporting lifesaving innovation that would otherwise not be developed due to elevated fear of liability.

Issues of climate impact by AI,[427] which will have significant ramifications over time, are predicted to be covered by existing policies. Munich Re listed "environmental risks" as one of the risk types associated with GenAI.[428] "We still cover oil accidents," responded an underwriter while discussing energy consumption by AI technology, but they did mention that certain types of oil and coal risks are no longer offered coverage.[429] The desire to be viewed as a responsible company with a reputation for climate protection might lead companies to take a different path. Still, it seems reasonable to assume there will always be insurance companies ready to offer policies regardless of the climate implications of a given technology for the right price. The policy terms are important here to ensure both sides of the bargain are still actively incentivized to mitigate AI-associated climate risks. Munich Re presented this optimistic approach by stating, "insurance providers could play a role in ensuring responsible model development. By establishing guidelines for balancing training frequency and energy and water consumption, insurance companies could aid in ensuring the right balance between continuous improvement of the GenAI models and environmentally sustainable development."[430] This is also applicable to AI technologies other than GenAI. However, it is questionable if the insurance industry as a whole will make environmental protection a priority, given their financial incentives and lack of assumption of negative externalities.[431]

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427. Emily M. Bender, Timnit Gebru, Angelina McMillan-Major & Shmargaret Shmitchell, *On the Dangers of Stochastic Parrots: Can Language Models Be Too Big?*, *in* FACCT '21: PROCEEDINGS OF THE 2021 ACM CONFERENCE ON FAIRNESS, ACCOUNTABILITY, AND TRANSPARENCY 613 (2021), dl.acm.org/doi/pdf/10.1145/3442188.3445922.

428. IRIS DEVRIESE, YUANYUAN LI & YANG LIN, MUNICH RE, INSURING GENERATIVE AI: RISKS AND MITIGATION STRATEGIES BALANCING CREATIVITY AND RESPONSIBILITY TO ENABLE ADOPTION 9 (2024), www.munichre.com/content/dam/munichre/contentlounge/website-pieces/documents/MR_AI-Whitepaper-Insuring-Generative-AI.pdf/_jcr_content/renditions/original./MR_AI-Whitepaper-Insuring-Generative-AI.pdf.

429. Zoom interview with an Underwriting Manager Cyber Lead, *supra* note 296; Clara Denina & Sarah Mcfarlane, *Insight: Coal Miners Forced to Save for a Rainy Day by Insurance Snub*, REUTERS (Aug. 31, 2023), https://www.reuters.com/sustainability/coal-miners-forced-save-rainy-day-by-insurance-snub-2023-08-31/.

430. Devriese et al., *supra* note 428, at 9.

431. *See, e.g.*, OECD, ENVIRONMENTAL RISKS AND INSURANCE: A COMPARATIVE ANALYSIS OF THE ROLE OF INSURANCE IN THE MANAGEMENT OF

In considering specific use cases, such as AVs, the healthcare system, delivery robots, drones, etc., Gaschel from Amazon stated that a great deal of unknown liability takes effect as AI becomes more prevalent. These present a broader issue in the existing insurance ecosystem – "I don't know how prepared the market is to take a broader piece."[432] AI could be a net positive for the insurance industry as less damage will eventually occur once AI becomes safer, leading to better outcomes. A caveat to that, Gaschel continues, is that we are not sure of those outcomes just yet.[433] To reach that point in the future, Gaschel asserts that insurance companies must first figure out a distinct method to underwrite in the AI context considering its industry-specific technology.

As mentioned, the data required to assume this task is currently lacking, most likely leading to inaccurate premiums and inadequate policy terms. The different industries and sectors utilizing AI will be a particularly important element of the underwriting process considering the scope of damages AI could create in a specific context. Companies are already considering this in their underwriting process, though in an imperfect manner. Even though interviewees from the insurance industry claimed that there are no sectors that are uncoverable, the terms, exclusions, and premiums of risker industries are bound to be different. The industries presented above will continue to evolve until a more definitive risk landscape emerges, allowing insurance companies to provide holistic coverage to companies in different industries – whether with an AI-designed policy or without it.

IX. CONCLUSION: WHAT COMES NEXT FOR THE AI INSURANCE MARKET?

Some policies might disappear as AI becomes so safe that they are no longer needed, such as automobile insurance, assuming autonomous vehicles live up to expectations.[434] In return, other lines of policies will grow stronger, and new lines will be developed. Along the way, insurance should be incorporated as a vital tool in our goal to achieve AI safety. Even so, there is a possibility that eventually an AI policy line will be absorbed into the traditional Tech E&O or Cyber insurance coverage and other lines of business that predated it. Claire of Relm stated that in this case, there will be no point in

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ENVIRONMENT-RELATED RISKS (2023), www.oecd.org/content/dam/oecd/en/publications/reports/2003/10/environmental-risks-and-insurance_g1gh3adb/9789264105522-en.pdf/.

432. Zoom interview with Matt Gaschel, *supra* note 325.

433. *Id.*

434. Weil et al., *supra* note 347, at 40.

clinging to it if that is the natural order.[435] However, in the meantime, it will be hard to understand and monitor possible AI exposure if we don't draw it out and ring-fence it to "keep a close eye on it until we are comfortable that it could be swallowed in and normalized with all of these other risks and coverage."[436] This approach also enables insurance companies to better manage the "silent AI" issue by delving into their offered coverage, including its inherent limitations, and exploring whether an AI policy is something that is indeed necessary.

Josh Fourie from CoverYourAI stated that eventually, "insurance is the assurance you cannot do."[437] A similar notion is echoed in a Munich Re whitepaper quoting an IP lawyer stating, "whatever risk you can't shift, that's when you look to insurance to distribute it."[438] Insurance companies operating in the AI field have emphasized their desire to maximize assurance of the AI technology they are covering so that only a residual of the risks will have to be covered by insurance. This means that regarding the risks we cannot assure in advance, we turn to insurance to provide a safety net for these AI companies, vendors, and users. Hopefully, that should be a low percentage of the overall risk.

When it comes to AI coverage, a recurring theme in the interviews that should be addressed as soon as possible is achieving clarity regarding "silent AI." This will enable insurance carriers to solve potential overlaps and create meaningful policies to cover the risks AI vendors, users, and companies face. The low caps set in the cyber industry are a good example of that, as applying a similar method in the AI context might undermine the purpose of insurance coverage. Another important aspect of this is the expertise of carriers offering AI coverage. "It is hard for companies that do not understand the technology at a fundamental level to insure it properly," states Karthik of Armilla AI.[439] To succeed in this sphere and to achieve their goals to support this industry, insurance companies must cultivate the expertise necessary to better assist their clients. We already see this with most of the companies mentioned in this paper offering consulting, verification, and assessment services and hiring software engineers as part of their underwriting and claims

435. Zoom Interview with Claire Davey, *supra* note 101.

436. *Id.*

437. Zoom Interview with Josh Fourie, *supra* note 90.

438. TED PINE, MUNICH RE, FROM GOVERNANCE TO INSURANCE FRONTLINE PERSPECTIVES ON MITIGATING CORPORATE AI RISK 8 (2024), www.munichre.com/content/dam/munichre/contentlounge/website-pieces/documents/MunichRe-Whitepaper-Risk-Mitigation-2024.pdf/_jcr_content/renditions/original./MunichRe-Whitepaper-Risk-Mitigation-2024.pdf.

439. Zoom Interview with Karthik Ramakrishnan, *supra* note 75.

management teams.[440] This should be preserved to ensure that insurance can support the AI industry in identifying and mitigating risks associated with it, now and in the future.

At the moment, it seems that the hardest part of creating a new market for AI policies is getting answers to the underwriters' questions as they try to gather sufficient information to underwrite a new policy.[441] These questions focus, among others, on the existence of an AI governance policy within a company, the testing of their models for bias, the constant existence of a human in the loop, whether the product is internal or consumer-facing, and many other questions that can be challenging to answer. The ability and willingness to answer these questions boils down to whether the market for AI coverage is "soft" or "hard."[442] Softer markets have a problem in asking questions because the competition is fierce with other insurance companies, and potential policyholders can choose to find a different insurer who will not ask difficult questions. In this soft market, getting the information the underwriter needs is very difficult as it is easy to find another insurer. This influences the level of care and safety companies take to mitigate risks, as the insurer has no leverage to prompt them to act safely. If the scope of claims increases, there might be a shift to a hard market where it will be easier for insurance companies to ask these questions, though not necessarily receive sufficient answers, and have more scrutiny over the applications. A harder market also enables insurance carriers to play the quasi-regulatory role they believe they should play in shaping the development and deployment of AI. A soft market enables policyholders to shop around, avoiding this mechanism by finding coverage with minimum requirements.

At first glance, it seems likely to anticipate the growth of an AI-specific insurance market because there are big information asymmetries between insurers and firms regarding individual firms' exposure to AI risk. This means that insurers will not want to cover this risk via a general policy they

440. Pravina Ladva & Antonio Grasso, *AI Brings a Major Change to Insurance Risk Landscape*, SWISS RE (May 23, 2024), www.swissre.com/risk-knowledge/advancing-societal-benefits-digitalisation/ai-brings-major-change-to-insurance.html (last visited Mar. 13, 2025).

441. In the context of GenAI, see Autumn Demberger, *Cyber and Professional Liability Considerations to Take Before Incorporating Generative AI into Your Business*, RISK & INS. (Jan. 9, 2025), riskandinsurance.com/cyber-and-professional-liability-considerations-to-take-before-incorporating-generative-ai-into-your-business/ (last visited Mar. 13, 2025) ("There is no silver bullet when it comes to assessing the use of artificial intelligence, but it's incumbent on underwriters to understand their customers' businesses and work with them to understand where these new and evolving technologies will fit.").

442. *Market Conditions: Cycles And Costs*, INS. INFO. INST., www.iii.org/publications/commercial-insurance/how-it-functions/market-conditions-cycles-and-costs (last visited Apr. 19, 2025).

already offer because they will not be able to routinely screen all firms for AI-related risks, given its ubiquity and uncertainty. This is especially true since AI-related liability risks are likely to be correlated across firms in ways that may not be obvious. However, most participants on all sides of the insurance spectrum consistently argued that there is no need now, nor will there be a need in the foreseeable future for AI policies, given the sufficiency of existing traditional policies.

A different set of challenges in the context of AI insurance was expressed by CFC's Michael Brunero.[443] He states, "what worries me is that we're providing solutions and companies are not taking advantage of them."[444] He stated that to move forward, in addition to AI development, businesses will need insurance. But there is a good chance that they will not seek coverage. Though he does not elaborate much on the reasons for this concern, this paper has shown that many companies interacting with AI are not looking for AI solutions in the insurance sphere because they rely on existing policies and "silent AI" – both of which can backfire given their uncertainty in the scope of their coverage. Brokers are contributing to this trend as they are not currently recommending purchasing specific coverage for AI activities. For insurance to live up to its potential and support innovation, innovators must take advantage of it.

Insurance is important in supporting innovation, especially with cutting-edge technologies such as AI. Gaschel from Amazon referred to this as ensuring a mechanism "to provide a level of confidence" to users and developers.[445] This notion was also articulated by many of the other participants, focusing on the trust insurance companies generate in the market by offering coverage. It encourages investments as investors see that there are some minimum guardrails already in place in light of the existence of an insurance policy and an underwriting process that has taken place. Munich Re's Iris Devriese emphasized the trust element during her interview,[446] and the white-papers published by Munich Re support that as well – "with Munich Re's performance guarantee, AI developers can accelerate the process of building trust, establish their reputation and attain the deserved traction for their solution with less risk."[447] This is true regarding other AI policies offering coverage to innovative AI solutions.

Still, insurance is only one way to address the uncertainty surrounding the risks of AI. Given the lack of clarity as to the scope of the different policies covering AI risks, other instruments should be considered as part of

443. Agnew, *supra* note 307.

444. *Id.*

445. Zoom interview with Matt Gaschel, *supra* note 325.

446. Zoom Interview with Iris Devriese, *supra* note 55.

447. *Sarna*, *supra* note 298, at 8.

business risk management strategies. One of those could be "indemnification agreements as gap fillers."[448] As Levine and Pappas phrased it, "by including indemnification provisions in contracts, businesses can clarify responsibilities and reduce the likelihood of disputes over liability when losses occur." Indemnification clauses will probably change as insurance policies better adapt to the evolving risk landscape of AI, but until then, they could act as an important complementary tool for risk management.

Given the innovative context of this paper, experimentation is an essential part of the AI and insurance intersection that needs to be encouraged, as stated by Finnis of WTW.[449] Insurance plays an important role in encouraging such experimentation, leading to research and development, discoveries, and innovation. That is precisely the reason the conversation about policies covering AI should be developed and encouraged within academia and industry. Collaboration between these two important sectors will enable a better understanding of how insurance can assist AI innovation for the benefit of society at large. This paper aims to push this important conversation forward, further clarifying the role insurance carriers and legislators have when developing a marketplace for AI risks.

Lastly, a more general conclusion could be drawn from this study relating to an important question in the law and technology sphere: do we need designated legislation for a given emerging technology (such as an AI Act in our case), or could we use existing legislation that could readily cover this technology via legislative interpretation? Law and technology scholars have disagreed about the appropriate approach for years, some arguing that new technology will usually require new laws while others urging that the underlying legislative infrastructure is sufficient.[450] An identical question stands at the heart of this paper in the insurance context, with some stakeholders claiming that a new policy is required while others claim that traditional policies are sufficient. As we saw above, most insurance carriers opted for the latter. However, this parallel conclusion could be misleading as insurance carriers are heavily influenced by legislators and their decisions to act via liability legislation, especially AI Acts.[451] The paper presented a new aspect to the chicken-and-egg conundrum that is canonical to the intersection of liability

448. Michael S. Levine & Alex D. Pappas, *Artificial Intelligence Risk: Why Risk Professionals Should Consider Indemnification As A Gap-Filler*, HUNTON ANDREWS KURTH (Sep. 26, 2024), www.huntonak.com/hunton-insurance-recovery-blog/artificial-intelligence-risk-why-risk-professionals-should-consider-indemnification-as-a-gap-filler.

449. R&I Editorial Team, *supra* note 81.

450. Rebecca Crootof & BJ Ard, *Structuring Techlaw*, 34 HARV. J. LAW & TECH. 347 (2021).

451. *See supra* Chapter VII.3.

law and liability insurance – what came first, the regulation or the policy?[452] Though history clearly shows that tort liability came first in the initial instance, further legal developments may suggest the contrary.[453] However, this paper suggests that in the context of emerging technologies, without liability regulation the insurance industry would not recognize a need to create new liability products. If there are no new regulations there is no need for new policies. Thus, the law is the first to act, and the insurance policy responds to it. This should lead to the conclusion that current legislation/policies are enough, at least for the initial phase of new technologies, as litigation and claims submitted to insurance companies are minimal. That might change over time if the technology proves itself to shake the core of existing regulation/insurance policies. Only then does it seem rational to create new legislation and, as a result, new insurance policies. Until then, the current infrastructure should suffice, as was articulated throughout the paper by those who use insurance to manage emerging risks.

This empirical survey aimed to illuminate the intricate interplay between insurance policies and AI technologies, with an emphasis on GenAI, regulatory dynamics, and legislators' roles. The goal was to generate valuable insights that can inform stakeholders, policymakers, and industry players about the evolving landscape of AI risks within the insurance sector. Hopefully, this is only the beginning of a deeper conversation between the insurance industry and insurance law scholars. This is especially needed in light of the important fact illustrated in this paper – that all liability laws are, in essence, insurance laws, constantly readjusting the relationship between the insurance industry and regulation.

452. KENNETH S. ABRAHAM, THE LIABILITY CENTURY: INSURANCE AND TORT LAW FROM THE PROGRESSIVE ERA TO 9/11, at 173 (2008).

453. *Id.* at 197.

LIKE A GOOD NEIGHBOR, STATE COURTS ARE THERE: THE CASE FOR REMANDING COVID-19 BUSINESS INTERRUPTION ACTIONS TO STATE COURT

GABRIEL L. JOHNSON*

ABSTRACT

Following the emergence of COVID-19 and resulting civil orders seeking to stop its spread, many businesses filed claims with their insurance providers for "business interruption" coverage, a type of insurance intended to compensate businesses for income lost during a temporary forced closure. When insurance companies roundly denied these claims, many small-business owners filed lawsuits in state courts. Insurance company defendants largely removed these cases to federal courts, and businessowner plaintiffs filed to remand back to state court. In one consolidated appeal heard by the Third Circuit, DiAnoia's Eatery, LLC v. Motorist Mutual Insurance Co., businessowner plaintiffs seeking remand to state court argued these claims involved novel state law issues. Although the district courts agreed, the Third Circuit reversed, and held federal courts in Pennsylvania and New Jersey could not use their statutorily granted discretion to remand the actions to state court.

This Note asserts the Third Circuit's holding in DiAnoia's Eatery, LLC misinterpreted circuit precedent which, properly applied, permitted the district courts to remand the claims to state court under the Declaratory Judgment Act. But the Note also argues that DiAnoia's Eatery, LLC is merely one example of a trend seen nationwide in which circuit courts issued decisions on this issue prior to the ultimate authority—state courts—ruling. It explains how federal courts instead turned inwards, relying not on binding state court precedent but rather on other federal court decisions; an approach which displaced state courts' proper role, and risked mass federal reversal by the U.S. Supreme Court.

This Note provides an important building block in a field of scholarship which has generally, thus far, criticized federal courts' initial near-monopoly on business interruption claims, the influence they exerted on the development of this caselaw, and finally, the merits of their dismissal of COVID-19 business interruption claims. This Note goes further, arguing that in addition to those concerns, federal courts were the improper forum for these suits,

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and that remanding them to state courts under the Declaratory Judgment Act was, and is, the best approach.

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I. ARE YOU IN GOOD HANDS? AN INTRODUCTION TO BUSINESS INTERRPUTION COVERAGE FOR COVID-19 STAY-AT-HOME ORDERS

When COVID-19 swept across the country, civil orders seeking to "stop the spread"[1] left more than 700,000 shuttered businesses and boarded-up restaurants in their wake.[2] Despite these devastating closures, many businessowners saw a glimmer of hope in their insurance policies.[3] Nick Gavrilides, owner of the Soup Spoon Café in Lansing, Michigan, paid his insurance company over $12,000 annually for a policy offering "business interruption coverage"; insurance for a loss of income during a period of forced business closure.[4] Mr. Gavrilides wasn't alone; owners of businesses across the country, from the Los Angeles Lakers to the Ocean Casino Resort

1. *See How to Stop the Spread of COVID-19*, MT. SINAI, https://www.mountsinai.org/health-library/special-topic/how-to-stop-the-spread-of-covid-19 (last visited Mar. 18, 2025) (illustrating popular use of phrase "stop the spread").

2. *See* Ryan A. Decker & John Haltiwanger, *Business Entry and Exit in the COVID-19 Pandemic: A Preliminary Look at Official Data*, FED. RSRV. (May 6, 2022), https://www.federalreserve.gov/econres/notes/feds-notes/business-entry-and-exit-in-the-covid-19-pandemic-a-preliminary-look-at-official-data-20220506.html ("The early pandemic period featured surging establishment closures . . . . more than 700,000 establishments [temporarily] closed in the second quarter of 2020 . . . . [and d]uring the second quarter of 2020 [permanent business closures] surged to a historic 330,000 establishments.").

3. *See* Michael Liedtke, *Struggling Merchants, Insurers Battle Over Pandemic Coverage*, WASH. POST (July 28, 2020), https://www.washingtonpost.com/business/struggling-merchants-insurers-battle-over-pandemic-coverage/2020/07/28/4d2c6d30-d130-11ea-826b-cc394d824e35_story.html (quoting one attorney as saying "lot[s] of people . . . did the right thing and bought this coverage thinking they would be thrown a lifeboat if disaster struck"); Shanthi Ramnath, *What Is Business Interruption Insurance and How Is It Related to the COVID-19 Pandemic?*, FED. RSRV. BANK CHI. (May 2020), https://www.chicagofed.org/publications/chicago-fed-letter/2020/440 (noting "[m]any business owners clearly believed their [business interruption] insurance would cover losses due to Covid-19").

4. *See* Mary Williams Walsh, *Businesses Thought They Were Covered for the Pandemic. Insurers Say No.*, N.Y. TIMES (Aug. 5, 2020, 9:26 AM), https://www.nytimes.com/2020/08/05/business/business-interruption-insurance-pandemic.html (noting Gavrilides claimed over $650,000 in losses and telling the stories of several similarly situated businesses). This type of insurance has several names, but will always be referred to as a "business interruption" clause in this Article. *See Business Interruption & Business Owner Policy*, NAIC, https://content.naic.org/cipr-topics/business-interruptionbusinessowners-policies-bop (last updated Jan. 31, 2024) (noting clause sometimes identified as "business income" instead of "business interruption"). For a discussion of the function and applicability of business interruption claims see also *infra* notes 8–13 and accompanying text.

in Atlantic City, thought their businesses' closures were covered under this type of policy.[5] "I thought by paying my premiums for the past fourteen years and if my service was ever interrupted, I would be rescued," Mr. Gavrilides explained.[6] But insurance companies uniformly responded that they weren't on the hook at all.[7] Understanding why requires some basic knowledge of insurance claims generally, and business interruption coverage specifically.

Unlike property owners' insurance, which compensates for actual damage sustained to a property, business interruption coverage reimburses businesses for their lost income during a period of forced, temporary closure.[8] In other words, rather than reimbursing the cost of what caused a closure, it covers the effect. Most business interruption clauses are more or less identical, requiring "direct physical loss of or damage at" a property, often from a fire or flooding, for coverage to effectuate.[9] However, some courts have

5. Walsh, *supra* note 4 (quoting Gavrilides as saying "I think business interruption claims should be paid when business is interrupted."); *see also* Ramnath, *supra* note 3 (noting widespread belief among businessowners in 2020 that business interruption insurance covered COVID-19); Joyce E. Cutler, *Covid Coverage Case Heads to Argument with Billions on the Line*, BLOOMBERG L. (Mar. 5, 2024, 6:30 AM), https://news.bloomberglaw.com/litigation/covid-coverage-case-heads-to-argument-with-billions-on-the-line (noting Los Angeles Lakers and other notable sports franchises' interest in upcoming business interruption litigation); Nikita Biryukov, *New Jersey Supreme Court Weighs Insurance Payouts for COVID Closures*, N.J. MONITOR (Sep. 28, 2023, 7:01 AM), https://newjerseymonitor.com/2023/09/28/new-jersey-supreme-court-weighs-insurance-payouts-for-covid-closures/ (same for Ocean Casino Resort).

6. Liedtke, *supra* note 3.

7. *See id.* (noting insurers "contend they are being miscast as potential saviors."); *see also* Nguyen v. Travelers Cas. Ins. Co. of Am., 541 F. Supp. 3d 1200, 1208 (W.D. Wash. 2021) (describing how "[i]n response to severe limitations on their operations, many businesses turned to their insurance policies to recover lost wages and reduced income.").

8. *See generally* Paul E. Traynor, *The "Business Interruption" Insurance Coverage Conundrum: COVID-19 Presents a Challenge*, 19 DEPAUL BUS. & COM. L.J. 65, 78 (2021) (describing the purpose of business interruption clauses). Traynor notes this gap in operations is sometimes described as a "period of restoration" to the business property following damage, but that "[c]ase law is on both sides of finding coverage for business interruption claims where no direct loss is present . . . ." *Id.* Meaning there have been numerous instances where courts have enforced business interruption clauses even where no actual damage to real property occurred and where no period of restoration would have been necessary.

9. *Id.* (providing the current standard business interruption clause language) (citing Anne Gron & Georgi Tsvetkov, *History Can Inform Pandemic Biz Interruption Insurance Cases*, LAW360 (May 21, 2020, 5:51 PM), https://www.law360.com/articles/1275331/history-can-inform-pandemic-biz-interruption-insurance-cases). Traynor's example clause reads:

construed "physical loss" more liberally, such as to include bacteria and airborne particles, if their presence renders the site inoperable.[10]

In addition to "physical loss," most business interruption coverage clauses require that "access to the area immediately surrounding the damaged property also [be] prohibited by civil action."[11] The civil action "must be taken in response to dangerous physical conditions" – meaning the physical damage must have caused the civil action.[12] Still, courts sometimes hold that a civil action prohibiting access to a property, even absent physical damage, invokes business interruption coverage because it creates the required "physical loss of" use of the property.[13] The question of what truly constitutes a

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We will pay for the actual loss of Business Income you sustain due to the necessary suspension of your "operations" during the "period of restoration." The suspension must be caused by direct physical loss of or damage to property at the described premises. The loss of damage must be caused by or result from a Covered Loss.

Traynor explains that: "Coverage for 'Business Income' must be caused by 'direct physical loss of or damage at the described premises caused by or resulting from any Covered Cause of Loss.'" *Id.* This uniformity did not always exist, as "historical development of the coverage . . . has been legally inconsistent . . . . and this is further complicated by the fact that not all business policies contain disease or virus exclusions." *Id.*

10. *See infra* notes 25, 193 and accompanying text (citing numerous examples of courts holding airborne gasses like ammonia, or bacteria like e-coli, constituted physical damage).

11. Traynor, *supra* note 8, at 78 (providing standard business interruption clause language).

12. *Id.* (providing sample business interruption clause requiring "suspension must be caused by *direct physical loss of or damage to* property at the described premises." (emphasis added)).

13. *See* Traynor, *supra* note 8, at 78 (providing examples). Traynor notes, for example, *Southlanes Bowl v. Lumbermen's Mutual Ins. Co.*, which held that "where the insured businesses were closed by order of a civil authority, physical damage to the insured premises was not a prerequisite to the insurer's obligation to reimburse the insured for the net losses resulting therefrom." 208 N.W.2d 569, 570 (Mich. 1973). However, this type of holding has by no means been universal. *See id.* at 84 (noting "[j]ust as there are cases . . . holding that physical loss to property is not a condition precedent to coverage for business interruption claims, there are cases stemming from the same type of actions of civil authorities that hold the exact opposite"). The article cites numerous examples. *See* Traynor, *supra* note 8, at 84–85 (citing Pac. Coast Eng'g Co. v. St. Paul Fire & Marine Ins., 9 Cal. App. 3d 270, 270 (1970)). In sum, the article paints a portrait of uneven applications of business interruption clause in instances involving civil orders to halt business without damage unequivocally physical or direct in nature before the sudden unanimity of denials in 2020. *See id.*

"physical loss" was central to much of the business interruption litigation stemming from the onset of COVID-19.[14]

Following COVID-19's detection in the United States, various civil authorities issued mandatory "stay-at-home" orders curtailing both the public's permission to frequent businesses, and businesses' permission to operate.[15] These orders, along with widespread public anxiety of contracting COVID-19, led to hundreds of thousands of businesses' operations being "interrupted."[16] Many businesses subsequently filed claims with their insurance providers for business interruption coverage.[17]

To receive insurance coverage a covered entity must file a claim with their insurance company.[18] If that claim is denied, the entity may ask a court to "declare" that the insurance company was actually obligated to provide coverage.[19] Beginning in March 2020, thousands of businesses submitted

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14. *See generally, e.g.*, Nguyen v. Travelers Cas. Ins. Co. of Am., 541 F. Supp. 3d 1200, 1207–08 (W.D. Wash. 2021) (describing onset of COVID-19 business interruption litigation, and discussing meaning of "physical loss" in this context).

15. *See* Sarah Mervosh, Denise Lu & Vanessa Swales, *See Which States and Cities Have Told Residents to Stay at Home*, N.Y. TIMES, https://www.nytimes.com/interactive/2020/us/coronavirus-stay-at-home-order.html (last updated Apr. 20, 2020) (noting "at least 316 million people in at least [forty-two] states, three counties, [ten] cities, the District of Columbia and Puerto Rico [were] being urged to stay home."). For further discussion of the history of COVID-19, both as it relates to insurance litigation and generally, see *About Covid-19*, CDC (June 13, 2024), https://www.cdc.gov/covid/about/ (summarizing COVID-19's effects on health); Ronen Perry, *Who Should Be Liable For The COVID-19 Outbreak?*, 58 HARV. J. ON LEGIS. 253, 254 (2021) (detailing COVID-19 outbreak and offering analysis on financial obligations). For further discussion of Pennsylvania and New Jersey's stay-at-home orders *see infra* notes 70 (discussing Pennsylvania) and 71 (discussing New Jersey).

16. *See* Decker & Haltiwanger, *supra* note 2 (providing statistics on number of business closures); *see also* Perry, *supra* note 15, at 254 (explaining "[t]he global economic impact caused by the uncertainty, by government restrictions on economic activity, and by consumer sentiment is already estimated in the trillions of dollars as businesses collapse and millions have lost their jobs").

17. *See* Tom Baker, *COVID Coverage Litigation Tracker*, INS. L. CTR., https://cclt.law.upenn.edu (last visited Mar. 18, 2025) (noting lawsuits contesting business interruption claim denials were the most frequent of all insurance-related actions following COVID-19's emergence).

18. *See* Mark Rosanes, *Insurance Claims: How to Process, to File, and How Long it Will Take*, INS. BUS. (Nov. 23, 2022), https://www.insurancebusinessmag.com/us/guides/insurance-claims-how-to-process-to-file-and-how-long-it-will-take-428385.aspx ("The insurance claims process often begins with the filing of the claim.").

19. *See How Can Declaratory Judgment Actions Help Resolve Insurance-Coverage Disputes Arising from Coronavirus-Related Business Closures?*,

practically simultaneous business interruption claims to cover interruptions to operations following COVID-19 stay-at-home orders.[20] Insurance companies roundly denied business interruption claims related to COVID-19, and campaigned for lawmakers and the judiciary to rule in their favor in any resulting lawsuits.[21] Only then did most courts consider, for the first time, whether business interruption insurance coverage is available to businesses closed by issuance of a civil order responding to an airborne threat.[22] Questions on the outer bounds of business interruption insurance were rampant among claimants and the public at large.[23]

MOLOLAMKEN LLP, https://www.mololamken.com/knowledge-How-Can-Declaratory-Judgment-Actions-Help-Resolve-Insurance-Coverage-Disputes-Arising-from-Coronavirus-Related-Business-Closures (last visited Mar. 4, 2024); *see also infra* Section II.A (discussing legislative history and function of Declaratory Judgment Act).

20. *See* Baker, *supra* note 17 (noting widespread initiation, and subsequent denials, of insurance coverage claims; especially business interruption claims).

21. *See* Erik S. Knutsen & Jeffrey W. Stempel, *Infected Judgment: Problematic Rush to Conventional Wisdom and Insurance Coverage Denial in a Pandemic*, 27 CONN. INS. L.J. 185, 190 (2020). The authors describe the insurance industry's efforts to ensure they would not have to pay for any insurance-related matters as a "remarkable media campaign . . . . [i]n insurance industry publications, in lawyers' news media, and even in the news media consumed by the general public." *Id.*

22. *See id.* at 188–90 (discussing sudden onset of COVID-19 insurance litigation on an unseen scale). Before 2020, courts only infrequently addressed and inconsistently ruled on whether physical loss included airborne toxins, let alone something akin to COVID-19. *See supra* note 13 and accompanying text (providing examples of cases holding physical damage is prerequisite to business interruption claim, and cases holding the opposite). "When business owners turned to their insurers for coverage for interruption of their business operations, including payroll protection, they discovered that action by state and local governments did not constitute a 'direct physical loss' to their business operations." Traynor, *supra* note 8, at 78. Some commentators speculate these cases represent a capstone on the insurance industry's attempt to quickly crush any widespread coverage. *See* Knutsen & Stempel, *supra* note 21, at 190. The article notes the insurance industry's widespread efforts to normalize a denial of coverage, which led to positive results. *Id.* "By January 2021, roughly seventy-five of these cases had some sort of . . . pro-insurer result. Insurers prevailed in sixty-seven of the seventy-five cases . . . on the basis of a lack of sufficiently triggering damage, a virus exclusion that ousts coverage, or both." *Id.* The term "real property" in this context and wherever it appears in this Article refers to "[l]and and anything growing on, attached to, or erected on it, excluding anything that may be severed without injury to the land." *See Real Property*, BLACK'S LAW DICTIONARY (12th ed. 2024).

23. *See* Jill M. Bisco, Stephen G. Fier & David M. Pooser, *Business Interruption Insurance and COVID-19: Coverage Issues and Public Policy Implications*, 39 J. INS. REGUL. 1, 17 (2020) (describing whether business interruption would apply to COVID-19 as an open question in 2020).

By all accounts, the insurance industry's media campaign was a success. The vast majority of claimants lost as courts, largely in the federal system, mostly applied state contract law to hold that insurance companies were within their rights to deny the claims because COVID-19 did not cause physical loss or damage to property.[24] However, many insurance law experts opined these decisions were incorrect, pointing to prior caselaw holding microscopic substances like ammonia qualified as "physical loss or damage," as well as the principle of resolving insurance disputes in favor of insureds more generally.[25] Notwithstanding this skepticism, many of these claims have *still*

24. *See* Knutsen & Stempel, *supra* note 21, at 202. The insurance industry's widespread efforts to normalize a denial of coverage led to positive results in court. *Id.* Insurers not only widely denied COVID-19 related claims, but also anticipated the looming court battles and engaged in extensive media and lobbying efforts to ensure denials were upheld. *Id.* at 202–05. This "concerted industry effort" was enormous; spanning all types of media and scholars, and was "as legally misplaced as . . . brilliant." *Id.* at 207; *see also, e.g.*, Nguyen v. Travelers Cas. Ins. Co. of Am., 541 F. Supp. 3d 1200, 1207–08 (W.D. Wash. 2021) ("[T]he Court . . . joins the majority of those courts around the country . . . . [in] determin[ing] that COVID-19 does not cause the physical loss or damage to property required as a condition precedent to trigger coverage in all the relevant policies."). The *Nguyen* court noted that the primary reasoning behind these denials was that viruses do not cause physical harm or loss to property. *Id.* at 1210. It also noted virus exclusions as providing a secondary possible grounds for denial. *Id.* Although businesses initially fared poorly in court (perhaps due to the increased portion of claims being heard in federal forums), later rulings were more favorable. *See* Schwarcz, *infra* note 89, at 445 ("While judicial rulings on the merits of these suits have generally favored insurers at the federal level, policyholders have enjoyed relative success in the smaller set of state court decisions that have been issued as of April 2022.").

25. *See* Knutsen & Stempel, *supra* note 21, at 207, 251 (explaining that "[b]ecause the facility was unusable for a period of time, the court held that the property suffered a direct physical loss" but contending that the insurers' main argument based on the "'direct physical loss or damage' requirement – can be refuted in most cases."). The article criticizes the courts' problematic "rush to judgment" in denying coverage for stay-at-home orders. *Id.* at 185. The article asserts previous caselaw has held airborne substances like ammonia could "damage" a property by making it unusable in the same manner COVID-19 does. *Id.* at 246–47 (citing Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of Am., No. 2:12-CV-04418 WHW, 2014 WL 6675934 (D.N.J. Nov. 25, 2014)). This article also takes issue with the "false consensus" that "direct physical loss" necessarily excludes COVID, and says that outcome from courts on preliminary motions "ordinarily amounts to error in COVID claims." *See id.* at 258–59; *see also* Traynor, *supra* note 8, at 78 (noting development of caselaw permitting business interruption coverage where businesses were not physically harmed but were ordered to close by civil authorities).

not been heard by the relevant state supreme court, despite now years-old federal court rulings for insurers.[26]

This is possible because although insurance disputes are governed by state law, many business interruption cases meet federal diversity requirements, and are filed in or removed to federal court.[27] Federal courts may provide declaratory relief pursuant to the Federal Declaratory Judgment Act ("DJA").[28] Unique from legal relief (such as injunctions) or monetary relief, declaratory relief permits courts to declare parties' obligations and rights under a contract.[29] Of particular importance is that while the DJA empowers federal courts to provide declaratory relief, it also grants them discretion to remand these actions to state court, subject to jurisdiction-specific balancing tests.[30]

Declaratory relief is frequently sought by insurance claimants who ask courts to make a binding declaration that they are entitled to coverage under their insurance policy.[31] This was common for those seeking business interruption coverage following COVID-19 interruptions.[32] Some district courts utilized their discretion to remand these cases in light of the state law-

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26. *See* Knutsen & Stempel, *supra* note 21, at 250 (noting a "false consensus" on the part of federal courts to deny claims); DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192 (3d Cir. 2021) (holding district courts erred in exercising statutorily-granted discretion to remand issues); Wilson v. USI Ins. Serv. LLC, 57 F.4th 131, 133 (3d Cir. 2023) (holding business interruption coverage generally did not apply to COVID-19 shutdown orders).

27. *See, e.g.*, *DiAnoia's Eatery, LLC*, 10 F.4th at 192 (providing an example of a federal court hearing the issue); *Nguyen*, 541 F. Supp. 3d at 1200.

28. 28 U.S.C. § 2201 (2024). The DJA states "any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought."

29. *See id.* (noting courts "may declare the rights . . ." of parties). This is as opposed to monetary relief, which includes "damages, costs, attorneys' fees, and any other form of monetary payment." 17 U.S.C. § 512(k)(2).

30. *See* 28 U.S.C. § 2201 (2024) (noting courts "may" declare the relevant rights); *see also infra* notes 41–43 and accompanying text (further discussing DJA's discretionary nature); Reifer v. Westport Ins. Corp., 751 F.3d 129, 134–35 (3d Cir. 2014) (setting forth Third Circuit's balancing test).

31. *See Reifer*, 751 F.3d at 141 (noting "[t]he insurance coverage context has been particularly fertile ground for exercising—and testing the boundaries of—DJA discretion.").

32. *See, e.g.*, Mark Daniel Hosp., LLC v. AmGUARD Ins. Co., 495 F. Supp. 3d 328 (D.N.J. 2020), *vacated and remanded sub nom.* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192 (3d Cir. 2021) (noting plaintiff sued in state court for declaratory relief).

based nature of the claims.[33] However, district courts in Pennsylvania and New Jersey were barred from doing so in *DiAnoia's Eatery, LLC v. Motorists Mutual Insurance Co.* [34]

This Note argues that the Third Circuit's ruling in *DiAnoia's Eatery, LLC* misapplied binding precedent and undermined principles of federalism in coming to this conclusion. Specifically this Note asserts the court erred in (1) holding it was in a position to resolve uncertainty before the parties, despite its having to make an "*Erie* guess" on still-unresolved state law issues (2) taking an overly-restrictive definition of what cases qualify as having "the same issues proceeding in state court" and (3) downplaying the importance of state courts' role in deciding novel state law issues.[35] But it also argues that, rather than being an isolated mistake, *DiAnoia's Eatery LLC* exemplifies a trend of federal courts relying improperly on persuasive federal consensus, presenting a risk of mass reversal.[36]

Part II of this Note explains why courts have discretion to remand a case under the Declaratory Judgment Act and how Third Circuit precedent affects that discretion. Part III describes the facts of each case consolidated into *DiAnoia's Eatery, LLC*. Part IV explains the Third Circuit's reasoning in holding that the district courts had abused their discretion by remanding the cases consolidated into *DiAnoia's Eatery, LLC*. Part V asserts that the Third Circuit's holding erred, that the district courts were not only within their discretion to remand the cases, but also that they were correct to do so. It also examines this decision's effects in the Third Circuit. Part VI argues this decision was part of a nationwide trend and looks to other circuit court decisions holding similarly to assert that federal courts nationwide prioritized their own unanimity rather than allowing state courts to rule.

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33. *See id.* at 336 (remanding case back to New Jersey state court).

34. DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192 (3d Cir. 2021) (consolidating three district court cases, one of which is also named DiAnoia's Eatery, LLC v. Com. Mut. Ins. Co.).

35. The term '*Erie* guess' (same, '*Erie* prediction' or '*Erie* decision') describes "[when] state law controls a claim pending in federal court, [so] the federal court makes a prediction regarding how the relevant state supreme court would decide the case in the absence of an existing, controlling decision." Christopher C. French, *Federal Courts' Recalcitrance in Refusing to Certify State Law COVID-19 Business Interruption Insurance Issues*, 100 TEX. L. REV. ONLINE 152, 161 (2022) (quoting Grey v. Hayes-Sammons Chem. Co., 310 F.2d 291, 295 (5th Cir. 1962)). The term was coined by the Fifth Circuit Court of Appeals in *Grey* and references the Supreme Court's decision in *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938). *See* John L. Watkins, Erie *Denied: How Federal Courts Decide Insurance Coverage Cases Differently and What to Do About It*, 21 CONN. INS. L.J. 455, 456 n.3 (2015) (noting term "*Erie* guess" coined in *Grey*).

36. *See infra* Part VI.

II. CUSTOMIZED SOLUTIONS FOR LITIGANTS' NEEDS: A BACKGROUND ON BUSINESS INTERRUPTION CLAUSE LITIGATION

Whether a federal court must hear a business interruption clause dispute between diverse parties depends on the statutory text of the DJA and circuit-specific precedent. The DJA empowers federal courts to declare a contract's proper construction as law, or to instead decline to make such a declaration and instead remand a case to state court.[37] However, in the Third Circuit, this ability to remand a case is limited by a balancing test set forth through *Reifer v. Westport Ins. Corp.*'s[38] eight "*Reifer* factors" and *State Auto Ins. Cos. v. Summy*'s [39] "additional guidance."[40]

A. HERE TO HELP CONTRACTS GO RIGHT: THE LANGUAGE AND FUNCTION OF THE DECLARATORY JUDGMENT ACT

The primary function of 28 U.S.C. § 2201, the DJA, is to provide parties with the opportunity to have a federal court declare the obligations of each party to a contract—known as "declaratory relief."[41] Plaintiffs frequently seek this type of relief to force insurance companies to pay on a claim

37. *See infra* Section II.A and accompanying text (further explaining DJA functionality).

38. 751 F.3d 129 (3d Cir. 2014).

39. State Auto Ins. Cos. v. Summy, 234 F.3d 131 (3d Cir. 2000).

40. *See infra* notes 48–63 and accompanying text (further explaining Third Circuit precedent limiting federal district courts' ability to remand DJA cases).

41. *See* 28 U.S.C. § 2201 (2024) (providing "any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought"); 1 MANUAL OF FED. PRACTICE § 7.11(10)(a) (explaining how the DJA functions and the various processes and standards involved). One treatise specifically summarizes declaratory judgments, both in general, and as they operate in the Third Circuit. 4 NEW APPLEMAN L. OF LIABILITY INS. § 45.06(1). There, it lists eight *Reifer* factors and independently notes: "[T]he existence or non-existence of pending parallel state proceedings to the declaratory judgment action, while not dispositive, is a factor that militates significantly in favor of either declining or exercising jurisdiction." *Id.* (citing Reifer v. Westport Ins. Corp., 751 F.3d 129, 144–45 (3d Cir. 2014)). For an example of a DJA case seeking clarification on contractual obligations, see Zenith Ins. Co. v. Newell, 78 F.4th 603, 604 (3d Cir. 2023). For further discussion of this phenomenon, see *infra* note 42 (describing use of DJA for insurance disputes).

for coverage which had been denied, by asking the court to declare that the contract provides coverage as a matter of law.[42] But the DJA also grants federal courts discretion to instead remand the case to state courts, subject to certain limitations and reviewable by the relevant federal circuit court on an abuse of discretion basis.[43]

The DJA presents a rare exception to what is otherwise a "virtually unflagging obligation" of federal courts to hear cases within their jurisdiction.[44] The DJA provides that a federal court "*may* declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought."[45] The word "may," as opposed to "shall," "confer[s] on federal courts unique and *substantial discretion* in deciding whether to declare the rights of litigants."[46] For example, a federal court

42. *See, e.g.*, *Reifer*, 751 F.3d at 141 (noting "[t]he insurance coverage context has been particularly fertile ground for exercising—and testing the boundaries of—DJA discretion."); *see also* Allstate Ins. Co. v. Seelye, 198 F. Supp. 2d 629, 631 (W.D. Pa. 2002) (observing the "action presents the all too common case of an insurance company coming to federal court, under diversity jurisdiction, to receive declarations on purely state law matters.").

43. *See* 28 U.S.C. §§ 2201–2202 (2024) (utilizing "may" to describe federal authority on DJA matters). The DJA does provide for an abuse of discretion review. *Id.* However, in the Third Circuit, "a district court's decision to decline jurisdiction 'will be given closer scrutiny than normally given on an "abuse of discretion" review.'" *Reifer*, 751 F.3d at 138 (quoting Exxon Corp. v. FTC, 588 F.2d 895, 900 (3d Cir. 1978)). This type of abuse of discretion review is called "heightened scrutiny." *See* Cost Control Mktg. & Mgmt., Inc. v. Pierce, 848 F.2d 47, 49 (3d Cir. 1988). For a more detailed explanation of an "abuse of discretion" standard, see *infra* note 76 and accompanying text.

44. *Compare* Quackenbush v. Allstate Ins. Co., 517 U.S. 706, 716 (1996) (noting "federal courts have a strict duty to exercise the jurisdiction that is conferred upon them by Congress"), *with* Colo. River Water Conservation Dist. v. U.S., 424 U.S. 800, 817 (1976) (presenting an exception to that "unflagging obligation"), *and* 28 U.S.C. §§ 2201–2202 (providing DJA language).

45. *See* 28 U.S.C. § 2201(a) (2024) (emphasis added); *see also* 42 PA. CONS. STAT. § 7531 (2024). Section 7531 is the Pennsylvania state equivalent to the DJA: The Pennsylvania Declaratory Judgment Act ("Pennsylvania DJA"). The Pennsylvania DJA mostly follows the same principles and rules as the DJA; allowing parties to seek a binding interpretation of an insurance contract's validity and construction. *See generally* 28 U.S.C. §§ 2201–2202 (2024) (operating similarly to Pennsylvania DJA); 42 PA. CONS. STAT. § 7531 (2024) (operating similarly to DJA).

46. *See* Wilton v. Seven Falls Co., 515 U.S. 277, 286–87 (1995) (emphasis added) (discussing unique nature and textual history of DJA's discretionary nature); Public Serv. Comm'n of Utah v. Wycoff Co., 344 U.S. 237, 241 (1952) (noting DJA "confers a discretion on the courts rather than an absolute right upon the

should not hear a DJA action where doing so would undermine the interests of "practicality [or] wise judicial administration."[47]

B. WE KNOW CONTRACTS: THE DECLARATORY JUDGMENT ACT IN THE COURTS

Federal courts' discretion to remand DJA actions, first formally recognized in *Brillhart v. Excess Ins. Co. of America*,[48] is subject to a type of abuse of discretion standard known as "heightened scrutiny."[49] Two cases, *Reifer* and *Summy*, summarize the restrictions on district court discretion in the Third Circuit.[50] In *Summy*, decided in 2000, the Third Circuit reversed a district court which had heard a declaratory judgment action, holding the district court should have remanded in light of a pending Pennsylvania state court case involving identical issues.[51] In *Reifer*, decided in 2014, the Third Circuit held a district court had properly remanded a case to state court, even though there were no parallel state proceedings, because the issues were "better decided by [the Pennsylvania state court] system."[52] *Summy* and other prior

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litigant"); *see also Reifer*, 751 F.3d at 139 (asserting district court's discretion is "unique and substantial" and reviewable only for abuse of discretion).

47. See Katherine A. Gustafson, *To Hear or Not to Hear?—Resolving a Federal Court's Obligation to Hear a Case Involving Both Legal and Declaratory Judgment Claims*, 52 U. BALT. L. REV. 383, 393 (2023) (quoting Wilton v. Seven Falls Co., 515 U.S. 277, 288 (1995)).

48. Brillhart v. Excess Ins. Co. of Am., 316 U.S. 491, 495 (1942) (holding "[a]lthough the District Court had jurisdiction of the suit under the Federal Declaratory Judgments Act . . . it was under no compulsion to exercise that jurisdiction"). *See also* Wilton v. Seven Falls Co., 515 U.S. 277, 279 (1995) (referring to "the discretionary standard set forth in *Brillhart*"). The court in *Wilton* at numerous points indicates it was *Brillhart* which clarified courts may decline discretion under the DJA, while weighing whether that case's original "discretionary standard" or subsequent "exceptional circumstances" standard articulated in *Colo. River Water Conservation Dist.* and *Moses H. Cone Memorial Hosp.* governed whether federal courts could decline to exercise jurisdiction. *See id.* (citing *Brillhart*, 316 U.S. 491; Colo. River Water Conservation Dist. v. U.S., 424 U.S. 800 (1976); Moses H. Cone Mem'l. Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1983)).

49. *See supra* note 43 and accompanying text (explaining "abuse of discretion" standard); *see also infra* note 76 and accompanying text (explaining "heightened scrutiny" standard).

50. *See infra* notes 54–63 and accompanying text (describing factors set forth primarily in *Reifer*, often adopted from *Summy*).

51. *Summy*, 234 F.3d at 136 ("[N]o federal interests were promoted by deciding this case in the District Court. Not a single federal question was presented to the District Court.").

52. Reifer v. Westport Ins. Corp., 751 F.3d 129, 140 (3d Cir. 2014).

cases set forth the bulk of these factors, while *Reifer* standardized them into the balancing test used in *DiAnoia's Eatery, LLC*.[53]

Together, these cases established eight non-exhaustive factors which district courts must consider to the extent they are relevant, as well as suggested "additional guidance" from *Summy*.[54] The relevant factors in *DiAnoia's Eatery, LLC* and many other business interruption cases were:

> (1) [T]he likelihood that a federal court declaration will resolve the uncertainty of obligation which gave rise to the controversy . . .
> (3) the public interest in settlement of the uncertainty of obligation . . .
> (5) a general policy of restraint when the same issues are pending in a state court . . .
> (6) avoidance of duplicative litigation . . . .[55]

Other factors lacked relevance either because they did not weigh for or against remand, or because they were undisputed and not substantially important.[56]

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53. *DiAnoia's Eatery, LLC,* 10 F.4th at 196–97 (describing *Reifer* as "enumerat[ing]" the factors, but noting many originated in *Summy* or other Third Circuit precedent).

54. *See Reifer*, 751 F.3d at 140, 146 (citing Terra Nova Ins. Co. v. 900 Bar, Inc., 887 F.2d 1213, 1225 (3d Cir. 1989)) (describing seven previously provided factors at 140 and listing a total of eight non-exhaustive factors at 146). Subsequent courts have consistently referred to *Reifer* as providing an eight-factor test. *See, e.g.*, *DiAnoia's Eatery, LLC,* 10 F.4th at 196–97 ("We then enumerated *eight factors* that a district court should consider . . . .") (emphasis added) (citing *Reifer*, 751 F.3d at 146); *see also Reifer*, 751 F.3d at 137 (citing U.S. v. Pa., Dep't of Env't Res., 923 F.2d 1071, 1075) (noting Third Circuit previously "required district courts to consider four general factors . . . . [and] in the insurance context, [the court had] suggested [three] relevant considerations. . . ."); *Summy*, 234 F.3d at 134 (citations omitted).

55. *Reifer*, 751 F.3d at 146. The other factors are:

> (2) the convenience of the parties . . .
> (4) the availability and relative convenience of other remedies . . .
> (7) prevention of the use of the declaratory action as a method of procedural fencing or as a means to provide another forum in a race for res judicata; and
> (8) (in the insurance context), an inherent conflict of interest between an insurer's duty to defend in a state court and its attempt to characterize that suit in federal court as falling within the scope of a policy exclusion.
> *Id.*

56. *DiAnoia's Eatery, LLC,* 10 F.4th at 196 (primarily discussing *Reifer*'s first, third, and fifth factors, plus additional *Summy* guidance).

Also relevant were several points of guidance from *Summy*. That decision warned district courts to be "particularly reluctant" to exercise DJA discretion if applicable state law was "uncertain or undetermined."[57] It reasoned that "the proper relationship between federal and state courts requires district courts to 'step back' . . . [on] unsettled state law matters."[58] *Reifer* then noted that "*Summy* [also] concluded that federal courts should decline jurisdiction where 'doing so would promote judicial economy by avoiding duplicative and piecemeal litigation.'"[59] Furthermore, "such insurance cases lack a federal question or interest."[60] Finally, the court in *Reifer* held a lack of parallel state proceedings—one involving identical issues and parties in another court—weighed in favor of a federal court not remanding a case, and must be overcome by the other factors.[61]

Some subsequent Third Circuit panels have interpreted this language as lending special weight to the existence or non-existence of state proceedings with exactly identical parties and issues.[62] This became relevant in *DiAnoia's Eatery, LLC* because the Third Circuit interpreted this factor as weighing against a decision to remand.[63]

III. WERE THE PLAINTIFFS REALLY "PROTECTED FROM MAYHEM?" THE FACTUAL BACKGROUND OF DIANOIA'S EATERY, LLC

57. *Reifer*, 751 F.3d at 141 (citing *Summy*, 234 F.3d at 135–36).

58. *Id.* at 141; *see also* Watkins, *supra* note 35, at 459–60 (noting tendency of Third Circuit specifically, and circuit courts generally, to incorrectly apply state law to proceedings before them). The Article also notes the failure of federal courts to apply make correct *Erie* guesses in insurance contexts, particularly. *Id.* This seems to provide ample support for *Summy*'s advice for federal courts to "step back." *Summy*, 234 F.3d at 135–36.

59. *Reifer*, 751 F.3d at 141 (citations omitted) (citing *Summy*, 234 F.3d at 135); *accord* Gustafson, *supra* note 47, at 405 (stressing importance of judicial economy in courts' choice exercising or declining to exercise jurisdiction over DJA matters).

60. *Reifer*, 751 F.3d at 141 (citing *Summy*, 234 F.3d at 136).

61. *See id.* at 144–45 (noting although not dispositive, the factor "militates significantly" for or against remand).

62. *See, e.g.*, *DiAnoia's Eatery, LLC*, 10 F.4th at 196 ("In our most comprehensive discussion of these factors, *Reifer*, we began by noting that the 'existence or non-existence of pending parallel state proceedings [to the declaratory judgment action],' while not dispositive, is a factor that 'militates significantly' in favor of either declining or exercising jurisdiction, respectively.") (quoting *Reifer*, 751 F.3d at 144–45).

63. *See id.* at 206 (noting factor weighed against Plaintiffs). For further discussion on this topic, see *infra* notes 83–86 (explaining Third Circuit held district courts misinterpreted *Reifer*'s fifth factor).

In *DiAnoia's Eatery, LLC,* the Third Circuit heard an appeal from three federal district courts: two in Pennsylvania[64] and one in New Jersey.[65] Each district court proceeding was remarkably similar—some parties even shared the same attorneys and filed substantially similar briefs.[66]

In each case, after being denied business interruption coverage for profits lost as a result of a civil closure order responding to COVID-19, each insured filed a lawsuit against their insurance provider. Each of these lawsuits were framed as a request for declaratory judgment on a near-identical insurance policy.[67] Each insurance carrier then filed to remove the proceeding to federal court, which was granted. Once in federal court, each insured party sought to remand the case to Pennsylvania or New Jersey state court, citing the novelty of the issues. Each district court granted the motion to remand, and each of these decisions was appealed to the Third Circuit and consolidated with the two other proceedings.[68]

Although these cases unfolded more or less identically procedurally, the reasoning employed by each federal district court varied in places due to

64. Umami Pittsburgh, LLC v. Motorists Com. Mut. Ins. Co., No. 2:20CV999, 2020 WL 9209275 (W.D. Pa. Aug. 26, 2020), *vacated and remanded sub nom.* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192 (3d Cir. 2021); DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., No. CV 20-787, 2020 WL 5051459 (W.D. Pa. Aug. 27, 2020), *vacated and remanded,* 10 F.4th 192 (3d Cir. 2021).

65. Mark Daniel Hosp., LLC v. AmGUARD Ins. Co., 495 F. Supp. 3d 328 (D.N.J. 2020), *vacated and remanded sub nom.* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192 (3d Cir. 2021).

66. *DiAnoia's Eatery, LLC*, 10 F.4th at 199, n.5 (noting DiAnoia's complaint was "nearly identical to Umami's complaint, with only the name of the restaurant and details of the insurance policy changed" and that DiAnoia's and Umami were represented by the same counsel at both the trial and appellate stage).

67. *Id.* at 197 ("Each Restaurant . . . sought a declaration that its Insurer was obligated to cover losses arising from the COVID-19 pandemic and the associated government orders (or, in one case, solely because of the government orders)." The court noted the similarities between each policy. For instance, the court describes the virus exclusion in *Umami* as "not pay[ing] for loss or damages caused directly or indirectly by . . . [a]ny virus, . . . [a]nd . . . further provid[ing] that '[s]uch loss or damage is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss." *Id.* (quoting the policy in part). For an explanation of "all risk" policies generally, see Julia Kagan, *What is All Risk Insurance, and What Does (and Doesn't) It Cover?*, INVESTOPEDIA, https://www.investopedia.com/terms/a/all-risks.asp (last updated June 7, 2022) (describing it as "a type of insurance coverage that automatically covers any risk that the contract does not explicitly omit").

68. *DiAnoia's Eatery, LLC*, 10 F.4th at 197–201 (discussing procedural history of each district court case from each case's complaint to its remand, and then noting each was consolidated with the others and appealed).

slightly different arguments made by the Pennsylvania parties, as opposed to the New Jersey party.[69] Both Pennsylvania-based plaintiffs—DiAnoia's Eatery, LLC and Umami's—alleged that their insurance policies covered losses from both civil closure orders stemming from COVID-19, and COVID-19 itself.[70] The New Jersey-based plaintiff—Mark Daniel Hospitality, doing business as "INC"—only alleged that its insurance policy covered losses arising from the civil closure orders.[71]

IV. WE MAKE STATE COURT PROBLEMS OUR PROBLEMS: A NARRATIVE ANALYSIS OF DIANOIA'S EATERY, LLC

On consolidated appeal the defendant insurers first argued that rather than seeking declaratory relief, the claimant plaintiffs were actually seeking monetary relief; the proceeds from their insurance contracts.[72] If true, the

69. *Id.* at 197 ("Each Restaurant . . . sought a declaration that its Insurer was obligated to cover losses arising from the COVID-19 pandemic and the associated government orders (or, in one case, solely because of the government orders).").

70. In Pennsylvania, Governor Tom Wolf first ordered all "nonessential businesses" (like restaurants) to close on March 19, 2020. *A Year of COVID-19 in Pennsylvania*, ABC27 NEWS, https://www.abc27.com/timeline-of-a-year-of-covid-19-in-pennsylvania/ (last visited Nov. 18, 2023). He then issued several stay-at-home orders affecting different counties beginning on March 23, 2020. *Id.* The stay-at-home orders and other restrictions were lifted in whole or in part beginning in May 2020. *Id.* (noting DiAnoia's county, Allegheny County, had stay-at-home orders lifted May 15, 2020).

71. Mark Daniel Hosp., LLC. v. AmGUARD Ins. Co., 495 F. Supp. 3d 328, 332 (D.N.J. 2020) *vacated and remanded sub nom.* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192 (3d Cir. 2021) (explaining that "[a]t some point following the issuance of these Executive Orders, Plaintiff temporarily closed INC"); *DiAnoia's Eatery, LLC*, 10 F.4th at 200 (contrasting INC with the Pennsylvania parties by explaining that "unlike Umami and DiAnoia's, INC alleges that it is the government orders that 'physically impact[ed]' its business, not the virus that causes COVID-19"). In relevant part, New Jersey's stay-at-home orders were twofold: on March 16, 2020, Governor Phil Murphy initially issued an executive order limiting the hours and capacities of restaurants, and on March 21, 2020, the Governor issued a more expansive order "which ordered New Jersey residents to remain at home except for certain enumerated exceptions" and limited restaurants entirely to take-out or delivery offerings. *Mark Daniel Hosp., LLC*, 495 F. Supp. 3d at 331 (citing N.J. Exec Order 107 (Mar. 21, 2020), https://nj.gov/infobank/eo/056murphy/pdf/EO-107.pdf).

72. *DiAnoia's Eatery, LLC*, 10 F.4th at 203 ("Motorists suggests that Umami and DiAnoia's both 'stated a breach-of-contract claim under Pennsylvania law' by alleging that 'they were entitled to "coverage" — *i.e.,* money — for their "losses, damages, and expenses," and "entitled to recover" those expenses from Motorists.'").

district courts would not have jurisdiction under the DJA.[73] But under a *de novo* standard of review, the court quickly dismissed these arguments because caselaw interpreting the DJA has traditionally held that an ability or attempt to seek additional relief does not undermine a DJA claim.[74]

The insurers next argued that even if the claims fell under the DJA, the district courts erred in declining to exercise jurisdiction.[75] The Third Circuit reviewed this argument under an abuse of discretion standard.[76] The court analyzed DiAnoia's Eatery, INC, and Umami's claims collectively on a *Reifer* factor-by-factor analysis, rather than on a case-by-case basis.[77] Chief Judge D. Brooks Smith, writing for a 2–1 majority alongside Judge Peter J. Phipps, ultimately found that each district court had either misinterpreted or insufficiently discussed the *Reifer* factors, leading to remanding of the case in all three instances.[78]

The three district courts held the first *Reifer* factor, the likelihood that the federal court's decision will resolve the uncertainty, weighed in favor of remanding the cases to state courts because of the lack of state court jurisprudence.[79] The majority opinion disagreed and criticized the district courts' hesitancy to predict how state courts might rule as improperly considering the

73. *See id.* at 202 ("[I]t may, in some circumstances, be possible for a party's claim for legal relief to masquerade as a declaratory judgment, improperly activating discretionary jurisdiction.").

74. *Id.* at 202–05 (relying on both statutory and judicial text to dismiss the argument and noting it reviews "*de novo* the District Courts' determination that the DJA applied"). The court did not give much credit to this argument, and summarized why by noting, "it is irrelevant whether [the plaintiffs] *could have* sought legal relief as well." *Id.* at 203.

75. *Id.* at 202.

76. *Id.* ("We review such decisions for abuse of discretion.") (citing Reifer v. Westport Ins. Corp., 751 F.3d 129, 137–39 (3d Cir. 2014)). One legal encyclopedia describes this standard as probing whether a "discretionary decision was made in plain error." *Abuse of Discretion*, CORNELL L. SCH.: LEGAL INFO. INST., https://www.law.cornell.edu/wex/abuse_of_discretion (last visited Apr. 5, 2025).

77. *DiAnoia's Eatery, LLC*, 10 F.4th at 205 (explaining "[b]ecause the Courts' analyses of the *Reifer* factors overlap significantly, our discussion below will be grouped by *Reifer* factor rather than set forth by individual appeal").

78. *Id.* at 202 ("[W]e ultimately conclude that each of the District Courts either misinterpreted some of the non-exhaustive factors, . . . did not squarely address the alleged novelty of state law issues, or did not create a record sufficient to permit thoughtful abuse of discretion review.").

79. *Id.* at 205 ("The *Umami* and *DiAnoia's* District Courts both concluded that the first *Reifer* factor weighed in favor of remand. . . . That is a misreading of the first *Reifer* factor.").

development of state law.[80] It held this factor was intended to consider only whether a federal court could terminate the controversy and thus avoid duplicative litigation in state court.[81] As the court in *Umami* remanded to state court after only analyzing this factor, the Third Circuit remanded that case back to the district court solely on this ground.[82]

The majority opinion next held that the district courts misinterpreted *Reifer*'s fifth factor, a "policy advising restraint where the same issues pend before a state court."[83] It held that the language "same issues pend[ing] before state court" applied only if the state court proceedings featured identical parties.[84] The majority conceded that a district court *could* consider whether

80. *Id.* ("The first *Reifer* factor is not intended to be a vehicle for considering the effect of a declaratory judgment on the development of state law.").

81. *Id.* ("[T]he first *Reifer* factor captures whether a declaration would bring about a 'complete termination of the controversy' between the parties and thereby avoid duplicative, piecemeal litigation."). The court goes on to assert only two types of situations wherein the first *Reifer* factor can weigh in favor of remanding a case. *Id.* First, "when one or more persons have not been joined, but have an interest in the outcome of the action, and [second,] when one or more issues have not been raised, but are a part of the controversy or uncertainty." *Id.* at 205–06 (citing *Developments in the Law: Declaratory Judgments – 1941–1949*, 62 HARV. L. REV. 787, 806 (1949)). Rather than citing a case for this proposition, the Third Circuit cites to a Harvard Law Review article from 1949. *Id.* at 205; *see also id.* at 206 (noting the first factor weighed against remand because a decision "would bring about a complete termination of the parties' disputes without piecemeal litigation").

82. *Id.* at 206 (describing the *Umami* district court's reliance on *Reifer*'s first factor as falling "well short of a 'rigorous' weighing of factors 'articulated in a record sufficient to enable our abuse of discretion review'" in deciding to "vacate the order in *Umami* and remand for further proceedings").

83. *Id.* (moving on to discuss *Reifer*'s "[f]ifth factor: 'general policy of restraint when the same issues are pending in a state court'").

84. *Id.* ("The fifth factor's 'policy of restraint' is applicable only when the 'same issues' are pending in state court *between the same parties*, not when the 'same issues' are merely the same legal questions pending in any state proceeding.") (emphasis added). To support this contention, the court cited cases which featured identical parties and issues, but which did not explicitly limit the fifth factor to identical parties and issues. *Id.* (citing, e.g., Kelly v. Maxum Specialty Ins. Grp., 868 F.3d 274, 289 (3d Cir. 2017); Brillhart v. Excess Ins. Co. of Am., 316 U.S. 491, 495 (1942)). The Court in *DiAnoia's* relies heavily upon *Kelly* to support its contention that "same issues" also means "same parties." *Kelly* represents the first instance in which the Third Circuit held "that the mere potential or possibility that two proceedings will resolve related claims between the same parties is not sufficient to make those proceedings parallel; rather, there must be a substantial similarity in issues and parties between contemporaneously pending proceedings." *Kelly*, 868 F.3d at 283–84. The *DiAnoia's* court holds "same issues" pending refers to parallel proceedings (which *Kelly* also supports). *DiAnoia's Eatery, LLC*, 10 F.4th at 206. This point may be where the *DiAnoia's* court is on firmest ground, but it still ignores that

identical issues between different parties favored remanding to state court.[85] But it argued doing so would inevitably weigh for remand, and would underestimate federal courts' ability to apply settled state law to difficult facts.[86]

Finally, the majority opinion discussed the guidance from *Summy* and the third *Reifer* factor, "the public interest in settlement of the uncertainty of the obligation."[87] It held federal courts have an inherent interest in deciding diversity cases, and that a claim must be truly novel to overcome this interest.[88] The majority found that the district courts had overestimated the claims'

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(1) Motorists Mutual Insurance company is a party in state claims, and (2) all business interruption clauses and virus exclusions, including some in this case, are identically worded. *See* sources cited *supra* note 66 (noting the three contracts were either identical or substantially of the same effect). Even *Kelly* notes this factor is not dispositive: "We reiterate that a strict definition of parallelism need not hobble a district court's unique leeway to decline from issuing declaratory relief. Although 'the existence or nonexistence of pending parallel state proceedings' is important in a court's assessment, it is not dispositive." *Kelly*, 868 F.3d at 287–88 (citation omitted); *see also infra* note 85 (discussing point further).

85. *DiAnoia's Eatery*, LLC, 10 F.4th at 207 ("Because the *Reifer* factors are non-exhaustive, a district court may still consider, when relevant, whether the same legal question at issue in a declaratory judgment action is at issue in state court proceedings between different parties."); *see also Kelly*, 868 F.3d at 287–88 (arguing "although 'the existence or nonexistence of pending parallel state proceedings' is important in a court's assessment, it is not dispositive").

86. *DiAnoia's Eatery, LLC*, 10 F.4th at 207 (questioning "how this fact would ever militate against exercising jurisdiction" and reaffirming "[o]nce again, '[f]ederal and state courts are equally capable of applying settled state law to a difficult set of facts'") (citing Reifer v. Westport Ins. Corp., 751 F.3d 129, 147 (3d Cir. 2014)).

87. *Id.* (proceeding to "*Summy* and third [*Reifer*] factor: 'the public interest in settlement of the uncertainty of obligation'").

88. *Id.* (asserting "federal courts sitting in diversity have 'the usual interest in the fair adjudication of legal disputes'" and that "'[w]here state law is uncertain or undetermined,' . . . district courts . . . [should] 'squarely address the alleged novelty of . . . state law claims'") (quoting *Kelly*, 868 F.3d at 288 (at "the usual interest"); quoting *Reifer*, 751 F.3d at 148–49 (at "[w]here state law")).

novelty, because according to the court, "an insurance policy is a contract," and contracts are well-tread law.[89] Thus, it remanded each of the cases.[90]

Recognizing these cases' novelty and their proper forum in state court, Judge Jane R. Roth dissented.[91] In doing so she reiterated what the majority acknowledged: that *Reifer* factors are not exhaustive.[92] In Judge Roth's view, the non-exhaustive nature of the *Reifer* factors meant the district courts had true discretion to remand and should only have been overturned for legitimate abuse.[93] Legitimate abuse did not occur here, as the cases (1) would have sweeping results, (2) would upend state development of their jurisprudence, and (3) were not settled law, but instead "deeply tied to state public policy . . . novel[,] and involve[d] some of the most substantial policy

89. *Id.* at 208 (describing "the relevant principles of New Jersey insurance law [as] easily summarized and . . . familiar in every state") (quoting Villa v. Short, 947 A.2d 1217, 1222 (N.J. 2008)). *See also id.* at 207–08 (acknowledging "[t]he *INC* Court did address novelty more squarely" but asserting it "overstated the novelty of the first issue regarding the applicability of the virus exclusion.")). *Contra* Daniel Schwarcz, *Redesigning Widespread Insurance Coverage Disputes: A Case Study of the British and American Approaches to Pandemic Business Interruption Coverage*, 71 DEPAUL L. REV. 427, 445 (2022) (noting "[w]hile judicial rulings on the merits of these suits have generally favored insurers at the federal level, policyholders have enjoyed relative success in the smaller set of state court decisions that have been issued as of April 2022"); Watkins, *supra* note 35, at 460 (noting "federal courts have made incorrect *Erie* guesses in many insurance coverage cases [and e]ven worse, these mistakes have often been on important recurring issues regarding the interpretation of common insurance policy provisions"). Schwarcz's article posits state contract law in the insurance context is not only treated differently state to state, but also is frequently interpreted more favorably towards insurers at the federal level than in state courts. *See id.*

90. *DiAnoia's Eatery, LLC*, 10 F.4th at 211 ("[V]acat[ing] the orders on appeal and remand for renewed consideration under the DJA and the *Reifer* factors as clarified by this opinion").

91. *Id.* (Roth, J., dissenting) (agreeing with the district courts "that these cases should be decided in the first instance by the Commonwealth of Pennsylvania and the State of New Jersey through their own courts").

92. *Id.* (noting "*Reifer* is not exhaustive. Therefore, even if the District Courts' analysis of some *Reifer* factors was deficient, there is no need for renewed consideration of those factors in view of alternative considerations that justify the District Courts' decisions to decline jurisdiction under the . . . [DJA]").

93. *Id.* at 212, 215 (asserting "*Reifer* emphasized that these factors 'are non-exhaustive, and [sometimes] district courts must consult and address *other relevant caselaw or considerations*'" and claiming "[e]ven if [the district courts'] consideration of the *Reifer* factors was deficient . . . that deficiency does not warrant the delay for a renewed consideration of those factors in light of the alternative considerations that support their exercise of discretion").

questions of the last century."[94] This was further supported by the lack of state court guidance from New Jersey's highest court or Pennsylvania's highest or intermediate appellate courts.[95] In sum, Judge Roth wrote that because of the additional uncertainty the majority's decision would create, and the deference owed to the district courts, she would have affirmed the district courts' orders to remand.[96]

V. THINK EASIER, THINK 'REMAND': A CRITICAL ANALYSIS OF DIANOIA'S EATERY, LLC AND ITS EFFECTS

In *DiAnoia's Eatery, LLC*, the Third Circuit joined other federal circuit courts in a collective "problematic rush to judgment."[97] Its decision to overturn the district courts' decision to remand to state court was contrary to circuit precedent and principles of federalism.[98] The outcome of this decision ultimately led to binding precedent that business interruption cases in the Third Circuit cannot be remanded to state court, and that business interruption policies do not cover COVID-19 related losses.[99]

A. CRITICALLY ANALYZING DIANOIA'S FAILURE TO CONFORM TO BINDING CIRCUIT PRECEDENT

This decision erred for three reasons. First, it failed to account for the potential to be overturned by state courts when weighing the first *Reifer* factor.[100] Second, it defined *Reifer*'s fifth factor in an impractical and restrictive manner.[101] Finally, it did not heed either *Reifer*'s third factor or *Summy*'s

94. *Id.* at 214–15.

95. *Id.* at 215 (asserting without guidance from state courts, and considering "the sweeping economic consequences that a decision will have on the rights and obligations of the parties and of those similarly situated, it is more prudent and efficient for federal courts to abstain").

96. *Id.* (concluding by noting Judge Roth "would affirm the judgments of the District Courts").

97. Knutsen & Stempel, *supra* note 21, at 190 (discussing and criticizing this trend at length).

98. *See infra* Section V.A.

99. *See infra* Section V.B.

100. *See infra* notes 104–118 and accompanying text (describing how Third Circuit erred by failing to account for its inability to resolve uncertainty).

101. *See infra* notes 119–131 and accompanying text (describing how Third Circuit misapplied fifth *Reifer* factor).

caution against ruling on novel state court issues.[102] All of these missteps were exacerbated considering the high level of deference owed to the district courts under the applicable abuse of discretion standard of review.[103]

1. Save When You Switch (to State Court): The First Reifer Factor

The Third Circuit's holding in *DiAnoia's Eatery, LLC* misinterpreted the first *Reifer* factor: "the likelihood that a federal court declaration will resolve the uncertainty of obligation which gave rise to the controversy."[104] In discussing the first factor, the court held that because a federal court's declaration would bring an immediate resolution to the parties' dispute, it inevitably resolved uncertainty, and thus weighed against remand.[105] However, this interpretation assumed later state court decisions would match its ruling—if not, the federal court's ruling would not "resolve the uncertainty" at all.[106] But rather, as Judge Roth correctly highlighted, a federal court cannot resolve

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102. *See infra* notes 138–156 and accompanying text (describing how Third Circuit conflated *Reifer*'s third factor with separate *Summy* guidance).

103. *See* Reifer v. Westport Ins. Corp., 751 F.3d 129, 139 (3d Cir. 2014) (asserting district court's discretion is "unique and substantial" and reviewable only for abuse of discretion).

104. *Id.* at 146; *see* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192, 212 (3d Cir. 2021) (Roth, J., dissenting) (asserting "the Majority wants to restrict the District Courts' broad discretion to abstain in these kinds of cases by requiring an overly technical application of this Court's decision in *Reifer v. Westport Ins. Corp.*, that overrides other relevant considerations").

105. *DiAnoia's Eatery, LLC*, 10 F.4th at 206 (explaining how "the declaratory judgment actions would bring about a complete termination of the parties' disputes without piecemeal litigation"). *But see infra* note 106 (discussing potential for not solving uncertainty with *Erie* guesses).

106. *See DiAnoia's Eatery, LLC*, 10 F.4th at 214–15 (Roth, J., dissenting) (arguing "[a]lthough an *Erie* guess in these cases might resolve the uncertainty in the obligations of those at bar, it will undoubtedly create additional uncertainty for parties that are similarly situated by potentially upending the uniformity of outcomes between state and federal courts"). It is also notable here that a state court *had* come to a differing outcome, in Ungarean v. CNA, 286 A.3d 353 (Pa. Super. Ct. 2022). Indeed, this weakness of *Erie* guesses sometimes leads to state courts outright criticizing federal courts for misconstruing and circumventing state law. *See* Connor Shaull, Note, *An* Erie *Silence:* Erie *Guesses and Their Effects on State Courts, Common Law, and Jurisdictional Federalism*, 104 MINN. L. REV. 1133 (2019). The Note cites, for example, *Farmland Indus., Inc. v. Republic Ins. Co.*, 941 S.W.2d 505 (Mo. 1997), a case similar in aspects to *DiAnoia's Eatery LLC*, where the Missouri Supreme Court criticized "[t]he [Eighth Circuit] [for] misconstru[ing] and circumvent[ing] Missouri law" in an insurance dispute turning on the definition of the word "damages." *Farmland Indus.*, 941 S.W.2d at 510.

uncertainty when making an *Erie* guess if the dispute involves novel state law issues.[107] In her dissent Judge Roth explained that while an *Erie* guess might resolve the immediate uncertainty for *these* parties, in the long-term it would "undoubtedly create additional uncertainty" for others "by potentially upending the uniformity of outcomes between state and federal courts."[108]

The district courts in their opinions also acknowledged this concern, but the Third Circuit majority dismissed this reasoning as improperly considering how a federal decision might affect the development of state law.[109] However, the district courts were wise to consider this, as scholars contend federal court decisions *have* inordinately impacted subsequent state court business interruption jurisprudence.[110] Furthermore, although the district courts could have expressed concern for influencing a state law—given that the *Reifer* factors are non-exhaustive—they never actually did so.[111] Instead,

107. *See* Shaull, *supra* note 106, at 1134 (describing limitations on *Erie* guesses); *see also* French, *supra* note 35, at 156 (claiming "federal courts' decisions to make *Erie* guesses regarding the novel state law issues presented in COVID-19 business interruption insurance cases rather than certify the issues to the controlling state supreme courts is a mistake").

108. *DiAnoia's Eatery, LLC*, 10 F.4th at 214–15 (Roth, J. dissenting).

109. *See id.* at 205 (majority opinion) ("The first *Reifer* factor is not intended to be a vehicle for considering the effect of a declaratory judgment on the development of state law"). Despite the Third Circuit's disdain for considering the effect on state law, this may be a topic worth examining, and even remanding for. *See* French, *supra* note 35, at 156 (explicitly arguing federal courts impacted the direction of state law); *see also* Burford v. Sun Oil Co., 319 U.S. 315, 332 (1943) (noting the importance of allowing state courts and governments to make their own law, when putting forth instructions to the inferior courts about maintaining a "doctrine of abstention").

110. *See* French, *supra* note 35, at 160 (asserting that "early federal circuit court decisions have an inordinate amount of weight regarding how other courts subsequently have been and will be interpreting the same policy language," and this effect is "magnifying the impact of the early federal circuit court decisions on the overall direction of the COVID-19 business interruption insurance litigation"). This argument suggests "if . . . *Erie* guesses are incorrect . . . as some insurance law scholars have argued they are, then . . . subsequent court decisions . . . will be equally flawed." *Id.* The article cites numerous cases highlighting this phenomenon. *See, e.g.*, Sandy Point Dental, P.C. v. Cincinnati Ins. Co., 20 F.4th 327, 331–32 (7th Cir. 2021); Goodwill Indus. of Cent. Okla., Inc. v. Philadelphia Indem. Ins. Co., 21 F.4th 704, 710, 711–12 (10th Cir. 2021).

111. *See DiAnoia's Eatery, LLC*, 10 F.4th at 215 (Roth, J., dissenting) (arguing "[a]bsent guidance from state courts on how to resolve these questions and given the sweeping economic consequences that a decision will have on the rights and obligations of the parties and of those similarly situated, it is more prudent and efficient for federal courts to abstain"); *see also* French, *supra* note 35, at 156 (discussing outsized influence federal courts may wield on state law when adjudicating novel state law claims such as these). In his essay, French notes that "[b]ecause they

they noted the difficulty of correctly predicting how state courts might rule on novel state law issues, given the lack of any appellate guidance in Pennsylvania.[112] The Third Circuit acknowledged this "paucity of authority from *any* Pennsylvania court," but asserted federal adjudication was "still warranted" because contract law issues could not be truly novel.[113] This assertion ignored both clear evidence of the complexity of contract law and an ongoing spirited scholarly discussion about whether insurance policies even *are* contracts for these purposes.[114] Contrary to the Third Circuit's confidence in federal courts' ability to adjudicate these issues, scholarship suggests federal courts actually fare worse making *Erie* decisions on insurance law than in other areas.[115]

The majority's reasoning in *DiAnoia's Eatery LLC* sidestepped both the district courts' valid concerns about interfering with state law and a plain reading of the first factor's emphasis on an "ability to resolve the uncertainty."[116] Furthermore, the *Reifer* factors are non-exhaustive, so any

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are unable to cite any controlling state supreme court precedents interpreting the relevant policy language in the context of a pandemic to support their opinions, the federal circuit courts have cited each other's opinions and noncontrolling state court cases decided in other contexts." *Id.* at 155.

112. *See DiAnoia's Eatery, LLC*, 10 F.4th at 214 (Roth, J., dissenting) ("[I]n the absence of guidance from *any* intermediate state court that can help predict how they would address difficult questions of state law . . . federal courts ought to abstain from making an *Erie* guess. That is exactly what the District Courts correctly did here."). Others have noted federal courts' frequently incorrect predictions on state court rulings, and recommended certifying questions to state courts or simply using the statutorily-granted discretion to remand. *See* Shaull, *supra* note 106 (noting inaccurate *Erie* guesses); French, *supra* note 35, at 156 (recommending federal courts certify questions to state courts).

113. *DiAnoia's Eatery, LLC*, 10 F.4th at 206. The *DiAnoia's* court did not conclude the issues were not novel in its discussion of *Reifer*'s first factor; saving them instead for the third factor. *Id.* ("[F]or the reasons stated infra Section IV.B.3 . . . ."). This novelty of the claims touches all three sections of DiAnoia's analysis. For further discussion on this point see *supra* notes 20–22 and accompanying text (discussing unprecedented nature of business interruption COVID-19 claims).

114. *See* Christopher C. French, *Covid-19 Business Interruption Insurance Losses: The Cases for and Against Coverage*, 27 CONN. INS. L.J. 1, 10 (2020) (noting that while courts frequently treat insurance policies as contracts, they "arguably are not . . . because they are non-negotiable, and the purchaser generally does not get a chance to review the policy before purchasing it").

115. Watkins, *supra* note 35, at 457 (asserting federal courts' frequently incorrect Erie guesses on insurance law amount to the federal system meting out "a different brand of justice" than state courts).

116. *See* French, *supra* note 35, at 156 (criticizing federal courts' decision to rule on business interruption claims for COVID-19, and generally asserting federal courts were an improper forum for such novel state law claims).

discussion by the district courts about non-*Reifer* factors was not an abuse of discretion – the applicable standard of review.[117] Regardless of whether the Third Circuit in *DiAnoia's* believed the issues were novel, they were not the controlling court, and thus could not resolve the "uncertainty of obligation" present in this instance.[118]

2. We Know What it Means to Interpret: The Fifth Reifer Factor

The Third Circuit also misinterpreted *Reifer*'s fifth factor, which advises a policy of restraint.[119] Central to the break between the Third Circuit and district courts' rulings was whether that restraint should be applied any time the same issues pend before a state court, or only where the same issues pend before a state court in a proceeding involving the exact same parties. The district courts' textual reading of the fifth factor was straightforward – where the same issues pend before a state court a federal district court should adopt *Reifer*'s advised policy of restraint.[120] Nevertheless, the Third Circuit interpreted the words "same issues" as actually meaning "same issues and *same parties*," even though insurance disputes typically feature identical contracts (as was the case for two of the policies at issue in *DiAnoia's Eatery, LLC*).[121] This interpretation of the fifth factor, as being one and the same as parallel proceedings mitigating significantly against remand, is contradictory

117. *See* Reifer v. Westport Ins. Corp., 751 F.3d 129, 139 (3d Cir. 2014) (asserting district court's discretion is "unique and substantial" and reviewable only for abuse of discretion); *see also DiAnoia's Eatery, LLC*, 10 F.4th at 212 (Roth, J., dissenting) (also highlighting deference owed to district courts under applicable standard of review).

118. *See* Schwarcz, *supra* note 89, at 445 (noting while early federal court decisions were in favor of the insurers, recent trends have diverged in favor of insureds, suggesting many early federal courts did not resolve uncertainty).

119. *See DiAnoia's Eatery, LLC*, 10 F.4th at 213–14 (Roth, J., dissenting) (explaining that although "the Majority finds that the fifth *Reifer* factor only applies when the issues pending in state court involve the same parties" that the court has "never held that parallel state proceedings are irrelevant just because they involve different parties").

120. *See Reifer*, 751 F.3d at 140 (lacking any language beyond "same issues" despite the *DiAnoia's* court contrary holding).

121. *See DiAnoia's Eatery, LLC*, 10 F.4th at 206 (arguing "fifth factor's 'policy of restraint' is applicable only when the 'same issues' are pending in state court between the same parties, not when the 'same issues' are merely the same legal questions pending in any state proceeding"); *see also supra* note 66 (noting parties' contracts' similarities).

to Third Circuit precedent which previously listed those ideas separately.[122] It is also a pained interpretation of the words "same issues" to say that they necessarily require the same parties, in light of those words' plain meaning, typical canons of construction, and realities of insurance-related disputes.[123] The simple fact is that in matters of insurance contract interpretation, the very same issues can and do arise among different parties because most agreements are adhesive and feature industry-wide standard language.[124]

Interpreting statutory language and judicial precedent is often a difficult endeavor, for which scholars and jurists have suggested canons of construction as tools of assistance.[125] One such canon, the "surplusage canon," advises that each provision in a document should be interpreted as having its own unique effect unless the text suggests otherwise.[126] The surplusage canon applied here suggests *Reifer*'s factors and *Summy*'s "additional guidance" set forth different principles for district courts to consider.[127]

Summy stated that an absence of parallel proceedings in state court must be overcome by other considerations for a federal court to properly

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122. *See, e.g.*, *DiAnoia's Eatery, LLC*, 10 F.4th at 196 (listing "existence or nonexistence of pending parallel state proceedings" and "a general policy of restraint when the same issues are pending in a state court" separately) (quoting *Reifer*, 751 F.3d at 144–46).

123. *See infra* notes 125–131.

124. *See* Traynor, *supra* note 8 (providing the current standard business interruption clause language, used in numerous interruption policies nationwide).

125. *See* ANTONIN SCALIA & BRYAN A. GARNER, READING LAW: THE INTERPRETATION OF LEGAL TEXTS (2012); *see also Canons of Construction*, CORNELL L. SCH.: LEGAL INFO. INST., https://www.law.cornell.edu/wex/canons_of_construction (last visited Apr. 5, 2025) (explaining canons of construction and their applicability). Canons of construction, notably, are not binding rules; they are merely suggested principles. *See id.*

126. *See* SCALIA & GARNER, *supra* note 125, at 174 (defining the surplusage canon); *see also* Dru Stevenson, *Canons Of Construction (Adapted From Scalia & Garner)*, UNIV. HOUS. L. CTR., https://www.law.uh.edu/faculty/adjunct/dstevenson/2018Spring/CANONS%20OF%20CONSTRUCTION.pdf (last visited Apr. 5, 2025) (providing further explanations of surplusage canon from law professor); *see also Reifer*, 751 F.3d at 146–47 (listing eight factors and then noting "Summy's additional guidance should be considered"); Stevenson, *supra* note 126 (noting independent ideas should not be "needlessly" assumed duplicative). As discussed previously, the courts are not bound by canons of construction; the canons are simply guiding principles famously collected by Scalia and Garner. However, they are highly influential, and if applied here would demand a different outcome in interpreting *Reifer*'s fifth factor. *See* SCALIA & GARNER, *supra* note 125, at 137.

127. *See* SCALIA & GARNER, *supra* note 125, at 174 (noting independent provisions or clauses of precedential or statutory language should be interpreted as having unique and separate effects).

remand.[128] *Reifer* independently sets forth a non-exhaustive list of some of the considerations which might overcome *Summy*'s guidance.[129] The surplusage canon applied here suggests the fifth *Reifer* factor should not be interpreted as simply restating the additional guidance from *Summy* if it is simultaneously instructing courts to look to *Summy*'s guidance, and providing factors indicating what might overcome that guidance.[130] To the contrary, *Summy*'s suggestion—that an absence of parallel state court proceedings is one important consideration which might be overcome—is separate from the fifth *Reifer* factor.[131] Further, as Judge Roth noted, the Third Circuit had, to this point, "never held that parallel state proceedings are irrelevant just because they involve different parties."[132]

And of course, here, the same issues *were* pending before state courts all across the country.[133] The Third Circuit's contention that two different sets of parties cannot litigate the "same issues" simply does not hold water in the insurance context. Nearly all insurance policies are identical with one another, particularly in the business interruption context.[134] They are form agreements of adhesion, drafted by a small group of companies serving as defendants in every business interruption litigation in the country.[135] And although the

128. State Auto Ins. Cos. v. Summy, 234 F.3d 131, 135–36 (3d Cir. 2000) (describing parallel proceedings as "presenting opportunity for ventilation of the same state law issues, . . . underway in the state court").

129. *See* Reifer v. Westport Ins. Corp., 751 F.3d 129, 140 (3d Cir. 2014) (citing *Summy*, 234 F.3d at 134).

130. *See id.* at 146–47 (noting the factors are non-exhaustive and describing insurance as being situations where "*Summy*'s additional guidance should also be considered").

131. *Compare* SCALIA & GARNER, *supra* note 125, at 174 (noting independent provisions or clauses of precedential or statutory language should be interpreted as having unique and separate effects), *with* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192, 196 (3d Cir. 2021) (listing "existence or non-existence of pending parallel state proceedings" and "a general policy of restraint when the same issues are pending in a state court" separately) (quoting *Reifer*, 751 F.3d at 144–46).

132. *DiAnoia's Eatery, LLC*, 10 F.4th at 214 (Roth, J., dissenting).

133. For demonstration on the scale of state (and federal) court business interruption litigation, see Baker, *supra* note 17. For just one of many examples of a same-year state court proceeding featuring identical issues to *DiAnoia's Eatery, LLC* in the Third Circuit, see *Ungarean, DMD v. CNA*, No. GD-20-006544, 2021 WL 1164836 (Pa. Com. Pl. Mar. 25, 2021).

134. *See supra* note 9 and accompanying text (noting contracts are "mostly identical" and citing to Traynor to provide current universally-used form language).

135. *See* French, *supra* note 114, at 10 (observing insurance "contracts" are arguably a poor fit for contract law because they entail no negotiation and are agreements of adhesion). If insurance policies of this kind could be negotiated, then the Third Circuit's argument would have more merit. Their status as agreements of

individual plaintiffs differ case-to-case, they all seek the same remedy—judicial declaration that these basically identical contract provisions cover losses arising from COVID-19 civil orders.[136] For these reasons, the Third Circuit's interpretation of "same issues" as requiring the same plaintiffs lacks soundness in the business interruption context.[137]

3. Bundle and Save: The Third Reifer Factor and Additional Guidance From Summy

Finally, the Third Circuit erred by insufficiently heeding the guidance from *Summy* and the third *Reifer* factor.[138] At the outset, the Third Circuit asserted that, as a federal court, it had its "usual interest in fair adjudication of legal disputes."[139] However, this contradicted what the Third Circuit noted in *Reifer*, quoting *Summy*: "The desire of insurance companies and their insureds to receive declarations in federal court on matters of purely state law has no special call on the federal forum."[140] Beyond the lack of any special call to federal courts, the Third Circuit's intervention in a novel state law question necessarily tends to undermine state courts' ability to determine their law or even encourage forum shopping.[141] This lends credit to the plaintiff

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adhesion makes concrete the one-to-one nature of business interruption disputes, as demonstrated as the essentially identical contracts between the three separate litigations consolidated in *DiAnoia's Eatery, LLC*. *See* sources cited *supra* note 67 (noting similarities between contracts). For an example of the reoccurring status of insurance companies as defendants, see Baker, *supra* note 17, at 7 (listing the fifteen most common insurance group litigants, with the most frequent litigator—The Hartford Financial Services Group—appearing in 290 lawsuits).

136. *See, e.g.*, *DiAnoia's Eatery, LLC*, 10 F.4th at 197 ("Each Restaurant. . . sought a declaration that its Insurer was obligated to cover losses arising from the COVID-19 pandemic and the associated government orders.").

137. *See supra* notes 133–136

138. *See DiAnoia's Eatery, LLC*, 10 F.4th at 213 (Roth, J., dissenting) (criticizing majority opinion for "employ[ing] a hyper-technical interpretation of the third *Reifer* factor to conclude that the District Courts erred").

139. *Id.* at 207 (majority opinion) (quoting Kelly v. Maxum Specialty Ins. Grp., 868 F.3d 274, 288 (3d Cir. 2017)).

140. *See* Reifer v. Westport Ins. Corp., 751 F.3d 129, 141 (3d Cir. 2014) (quoting State Auto Ins. Cos. v. Summy, 234 F.3d 131, 136 (3d Cir. 2000)).

141. *See* Watkins, *supra* note 35, at 457–58 (noting federal courts undermine state courts when deciding novel state law issues, but also risk encouraging forum shopping when they conclude, or are perceived to conclude, differently than the state court).

claimants' arguments that there was no interest in resolving a federal question here.[142]

Third Circuit precedent further supported this contention; *Summy* and *Reifer* advised that where state law is unsettled federal courts should be "reluctant" to hear DJA matters, and where it is settled "there would seem to be even less reason" for federal adjudication.[143] The Third Circuit's insistence on exercising its purported "usual federal interest" in *DiAnoia's* thus directly contradicted *Summy* and *Reifer*'s guidance that the proper federal-state court relationship "*requires* [*federal*] *courts to step back*" so state courts may interpret their own unsettled laws.[144] Alternatively, if the Third Circuit viewed the claims as settled, then "there would seem to be even less reason" to hear the claims.[145]

Thus, whether the law was settled or unsettled, there was reason to remand these claims.[146] Particularly because the three plaintiffs were strenuously objecting to federal adjudication.[147] The alternative to federal adjudication of business interruption claims was to have the state court system, with final authority on the law, offer a more permanent resolution.[148] Far from

142. *DiAnoia's Eatery, LLC*, 10 F.4th at 207 (quoting INC's Brief as asserting "there is no federal interest" because "[t]he decisions on insurance coverage would involve not only an *interpretation of novel issues of state insurance law* but also on [sic] the legal impact of unprecedented orders of New Jersey state officials").

143. *See Reifer*, 751 F.3d at 141 (quoting *Summy*, 234 F.3d at 135–36).

144. *Id.* (emphasis added) (quoting *Summy*, 234 F.3d at 136); *see also* Watkins, *supra* note 35, at 457 (arguing federal courts should refrain from deciding novel state law issues); Burford v. Sun Oil Co., 319 U.S. 315, 332 (1943) (noting importance that states make their own law and advising a "doctrine of abstention").

145. *Reifer,* 751 F.3d at 141 (quoting *Summy*, 234 F.3d at 135–36). This quote is especially notable given how reliant the *DiAnoia's* court is on *Reifer*, and how stringently the *DiAnoia's* court argues *Reifer* demands district courts not remand to state courts—in spite of this directive. *See DiAnoia's Eatery, LLC*, 10 F.4th at 211 (holding *Reifer* and *Summy* compel district courts to not remand).

146. *See DiAnoia's Eatery, LLC*, 10 F.4th at 207; *see also* Watkins, *supra* note 35, at 457 (arguing federal courts should refrain from deciding novel state law issues); Schwarcz, *supra* note 89, at 445 (noting "[w]hile judicial rulings on the merits of these suits have generally favored insurers at the federal level, policyholders have enjoyed relative success in the smaller set of state court decisions that have been issued as of April 2022"). This article highlights federal and state courts' often divergent treatments of these cases – running counter to the federal courts' insistence they can apply state law as well as state courts. *Id.*

147. *See DiAnoia's Eatery, LLC*, 10 F.4th at 207; *see also Summy*, 234 F.3d at 136 (holding district courts should take a party's "vigorous objection" to federal litigation into account).

148. *See, e.g.*, Ungarean v. CNA, 301 A.3d 862 (Pa. 2023) (opportunity for the Pennsylvania Supreme Court to issue a controlling decision on whether business

permitting the district courts to act on the "reluctance" that *Summy* recommended in this type of case, the Third Circuit instead ordered them to hear such cases.[149] The Third Circuit argued this was because the disputes were not unsettled at all, again despite binding precedent advising "even less reason" to order the district courts to hear settled state law cases in light of one party's vigorous objections.[150]

Third Circuit precedent supported exercising this restraint in other ways as well. The court in *Summy* cautioned that it would be "counterproductive" for district courts to decide issues "which might otherwise be candidates for certification to the state's highest court. Such matters should proceed in normal fashion through the state court system."[151] Insurance law experts have identified business interruption cases, in light of COVID-19, as a compelling topic for certification to state courts.[152] Given this guidance, and the high level of deference owed to the district courts under an abuse of discretion standard, the Third Circuit should not have reversed on this ground.[153]

While the public, given the large number of cases on this issue, did have an interest in the settlement of the uncertainty, it was not a settlement a federal court limited to an *Erie* guess could provide.[154] The inherent

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interruption clauses cover COVID-19). *Cf.* French, *supra* note 35, at 156 (arguing "circuit courts' refusals to certify the novel state law issues to the controlling state supreme courts is also inconsistent with the spirit and purpose of the U.S. Supreme Court's abstention doctrine, which generally provides that federal courts should exercise their discretion to decline to adjudicate cases where novel or complex state law issues will be dispositive in the case").

149. *Reifer*, 751 F.3d at 141 (emphasis added) (quoting *Summy*, 234 F.3d at 135).

150. *Id.*

151. *Summy*, 234 F.3d at 135.

152. French, *supra* note 35 at 156 (arguing "federal courts' decisions to make *Erie* guesses regarding the novel state law issues presented in COVID-19 business interruption insurance cases rather than certify the issues to the controlling state supreme courts is a mistake"). Unfortunately, at the time of that Article, eight federal courts (the number is now at least nine) had ruled on the issue of business interruption clauses (against the insured's) before a single state's highest appellate court could hear the issue. *See id.* at 155 (noting federal courts simply cited to each other and non-controlling state court decisions). Other scholars have argued "the consequences of an incorrect *Erie* guess in [insurance] coverage cases can have profound practical implications beyond the immediate case because insurance policies are typically written on common forms. A mistaken determination in one case may thus be repeated many times over." Watkins, *supra* note 35, at 457.

153. *See Reifer*, 751 F.3d at 140 (asserting district court's discretion is "unique and substantial" and reviewable only for abuse of discretion).

154. *See* French, *supra* note 35, at 155 (discussing limitations on *Erie* guesses in this context); *see also* Watkins, *supra* note 35, at 457 (discussing federal courts'

uncertainties in *Erie* guesses and the federal courts' often divergent predictions as to insurance law limit federal courts' ability to truly conduct a "fair adjudication of a legal dispute."[155] Thus, *Reifer*'s third factor, *Summy*'s warnings, and even the *DiAnoia's* court's interest in "fair[ly] adjudicati[ng]" the dispute, all weighed in favor of remanding the business interruption clause cases back to state court.[156] The Third Circuit should have assigned more weight to the open-ended nature of DJA discretion and the importance of letting state courts decide novel issues before them.[157]

B. WE'RE BIG, SAFE, AND FRIENDLY (FOR INSURERS): CIRCUIT COURTS NATIONWIDE IMPROPERLY ADJUDICATED STATE LAW

Significant portions of this Note analyze the Third Circuit's decision to block district courts from remanding COVID-19-related business interruption cases where the appropriate state courts had yet to rule.[158] Much of that analysis is based on circuit-specific precedent which, properly applied, supported those district courts' decisions to remand to state court.[159] But the issue of federal courts' response to business interruption claims extends far beyond one circuit.

In one way the Third Circuit is unique: seemingly no other circuit court issued a precedential decision holding district courts cannot, as a matter

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tendency to undermine state court authority and invite forum shopping). The Pennsylvania Superior Court's recent divergent holdings on business interruption clauses demonstrated the difficult, novel questions posed by business interruption clauses following COVID-19. *See* MacMiles, LLC v. Erie Ins. Exch., 286 A.3d 331, 332 (Pa. Super. 2022) (holding business interruptions clause did not cover COVID-19 related losses); Ungarean v. CNA & Valley Forge Ins. Co., 286 A.3d 353, 356 (Pa. Super. 2022) (holding business interruptions clause did cover Covid-19-related losses).

155. *See* sources cited *supra* note 154 (discussing diverging Pennsylvania Superior Court decisions demonstrate complexity and debate on this matter); Schwarcz, *supra* note 89, at 458 (noting federal court tendency to rule for insurers at higher rates than state courts).

156. *See DiAnoia's Eatery, LLC*, 10 F.4th at 207 (quoting Kelly v. Maxum Specialty Ins. Grp., 868 F.3d 274, 288 (3d Cir. 2017)); *see also supra* notes 138–155 and accompanying text (arguing the third *Reifer* factor and *Summy*'s additional guidance weighed for remand).

157. *See DiAnoia's Eatery, LLC*, 10 F.4th at 211 (Roth, J., dissenting) (asserting without guidance from state courts, and considering "the sweeping economic consequences that a decision will have on the rights and obligations of the parties and of those similarly situated, it is more prudent and efficient for federal courts to abstain").

158. *See supra* Part IV and Section V.A.

159. *See supra* Section V.A.

of law, use their discretion to remand business interruption cases to state court.[160] However, the Third Circuit was far from unique in eventually issuing binding federal precedent on the issue of the state law business interruption clause applicability, despite an absence of state court authority.[161] Other circuit courts across the country reached the same decision.[162] Principles of federalism, and concern for development of unauthorized, improper federal common law, demonstrate why the collective U.S. Circuit Courts of Appeals should have permitted the remand of business interruption litigation to state courts.[163]

There is a perception that sophisticated litigants, or at least their attorneys, often prefer to adjudicate in federal courts for their supposed judicial quality and superior resources, particularly in complex commercial cases.[164]

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160. A case's nonexistence is naturally difficult to demonstrate, but a myriad of searches on standard search engines and legal databases invariably turned up only *DiAnoia's Eatery, LLC* when using different combinations of keywords like "business interruption," "remand," "circuit," etc.

161. *See infra* Part VI.

162. *See Third Circuit Joins Other Federal Circuits in Finding No Coverage for COVID-19 Business Interruption Claims*, CROWELL & MORING LLP (Jan. 6, 2023), https://www.crowell.com/en/insights/client-alerts/third-circuit-joins-other-federal-circuits-in-finding-no-coverage-for-covid-19-business-interruption-claims ("[F]ederal circuit courts for the First, Second, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth, and Eleventh Circuits now have all determined that there is no coverage for COVID-19 business interruption claims.").

163. Federal common law is technically authorized only where "a federal rule of decision is 'necessary to protect uniquely federal interests' and where 'Congress has given the courts the power to develop substantive law." *See Common Law Doctrines*, CONST. ANNOTATED, https://constitution.congress.gov/browse/essay/intro.4-3-6/ALDE_00000016/ (last visited Dec. 10, 2024) (citing *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938) for the proposition that "[t]here is no federal general common law"). In fact, Supreme Court precedent forbids the development of federal common law through federal courts "hearing cases that state courts can resolve by applying state law in a manner that relieves federal courts from making constitutional determinations." *Id.* (citing R.R. Comm'n of Tex. v. Pullman Co., 312 U.S. 496, 498 (1941)).

164. *See* Victor E. Flango, *Litigant Choice Between State and Federal Courts*, 46 S.C. L. REV. 961, 973 (1995) ("Attorneys who usually practice before federal courts tend to be from larger law firms and tend to view federal judges as better trained, better supported with resources, and more impartial . . . . They believe complex litigation belongs in federal court."); Will Newman, *Selecting a Court*, UNPREDICTABLE BLOG (Nov. 21, 2022), https://www.unpredictable-blog.com/blog/selecting-court ("Litigants often prefer federal court for several reasons. Many believe the judges are better. Federal courts also usually have fewer cases and more resources, and so they may handle cases more quickly than state courts.").

Indeed, while some litigants assuredly prefer state court, it is not uncommon to hear it referred to as "the wild west" or similar terms in conversation.[165] And perhaps nowhere is that perception of a preference for federal courts more demonstrably true than it is with insurance company litigants.[166] Potentially because insurance companies receive superior results in federal court.[167] Thus, when a statute gives federal courts discretion to hear a declaratory judgment action, it is a safe bet that insurer litigants will make every effort to ensure their arguments are heard by a federal judge.[168]

But issues arise where the declaratory judgment action displays novelty. Federal courts, staring down a paucity of authority, begin looking instead to other federal court opinions, which were written using a similar paucity of authority.[169] This creates a self-reinforcing cycle of federal decisions applying not state law, or even federal law, but federal *Erie* guesses. When federal courts do not apply state law, but instead apply federal court decisions

165. *See, e.g.*, litigation_god (@GodLitigation), X (Oct. 19, 2023, 9:20 AM), https://x.com/GodLitigation/status/1714994820085883215 (popular legal profession humor account asserting "State court is the Wild West"); @BobertFrost6, Comment to *How Big are the Differences Between State and Federal Criminal Courts?*, REDDIT, https://www.reddit.com/r/Ask_Lawyers/comments/191tmtb/how_big_are_the_differences_between_state_and/ (last visited Apr. 5, 2025) (observing users in forum titled "Ask_Lawyers" seemingly view federal courts as "very prim, proper, and strict," and state courts as "comparatively the wild west").

166. *See* Watkins, *supra* note 35, at 457 ("[T]he anecdotal view that insurers favor federal courts over state courts for both procedural and substantive reasons is supported by available survey and statistical evidence.").

167. *See* Baker, *supra* note 17 (demonstrating insurers lost at the motion to dismiss stage about 20% of the time in state court, and about 4% of the time in federal court); *see also* sources cited *supra* note 89. Specifically, Schwarcz in his article posits that insurance providers fare better in federal than in state court, both generally and in regard to coverage post-pandemic. Schwarcz, *supra* note 89, at 429 (highlighting that at time of writing, insurers had lost approximately 20% of their motions to dismiss in state court, a higher portion of failure compared to sweeping federal court success).

168. *See* Baker, *supra* note 17 (highlighting that COVID-19 business interruption claims, at least at the motion-to-dismiss level, are being brought at three times the rate in federal court as they are in state court).

169. *See* French, *supra* note 35, at 155–56 n.26 (citing three separate circuit court cases which held business interruption clauses do not apply to COVID-19 as examples of circuit court decisions which explicitly acknowledged their state supreme court had not defined the key terms, before turning to and citing other federal precedent as support for the decision); *see also, e.g.*, Goodwill Indus. of Cent. Okla., Inc. v. Phila. Indem. Ins. Co., 21 F.4th 704, 710 (10th Cir. 2021) (a case cited by French pointing to "the decisions of every other circuit and the vast majority of district courts" as reinforcing their holding).

similarly lacking state law authority, what results is a nationwide blanket federal policy on a state law issue in the absence of binding precedent to the contrary—*i.e.*, federal common law.[170] And while that federal common law ceases to exist once the appropriate state supreme court rules, a state supreme court decision often comes after practically every dispute has been heard[171]—or never at all.[172] In the business interruption context this is encouraged by insurer litigants; in seeking dismissal of business interruption cases they direct the federal court's attention to other federal courts that have ruled similarly.[173] And as discussed in this Note and in other scholarship, insurance cases—including COVID-19 business interruption claims—must be something less than straightforward, given the stark differences between state and federal outcomes.[174] Other scholars have identified this problem within COVID-19 business interruption litigation and convincingly advocated for solutions such as certification to state supreme courts.[175] This Note presents an alternative (or complementary) approach: order district courts to remand under the DJA.[176]

Several other doctrines and mechanisms exist which, if applied, would guard against a self-perpetuating cycle of federal decision-making on

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170. *See Common Law Doctrines*, *supra* note 163 (highlighting federal common law exists only in absence of contravening higher authority such as Congressional statute).

171. *See, e.g.*, Ungarean v. CNA & Valley Forge Ins. Co., 323 A.3d 593 (Pa. 2024) (holding four years after the policy was denied and eighteen months after the Third Circuit ruled on the merits of same issue that coverage did not apply).

172. *See* Baker, *supra* note 17 (featuring chart showing that still, as of December 2024, a majority of state supreme courts have not ruled).

173. Michael McCann, *Yankees' Minor League Insurance Fight Sheds Light on Pandemic Claims*, SPORTICO (Oct. 16, 2020, 2:55 AM), https://www.sportico.com/law/analysis/2020/covid-19-business-interruption-insurance-1234614821/ ("To bolster [their] position, [insurers'] attorneys assert that 'courts across the nation have dismissed COVID-19 business interruption cases under substantially similar circumstances,'" before citing to several federal court cases, including *DiAnoia's Eatery LLC*).

174. See sources cited *supra* note 167; Schwarcz, *supra* note 89, at 445–46 (pointing out federal courts' frequent incorrect *Erie* predictions in the insurance context, and the vastly different COVID-19 business interruption claim dismissal rate between state and federal courts).

175. *E.g.*, French, *supra* note 35.

176. *See generally supra* Section V.A (arguing under both precedent specific to the Third Circuit (but found similarly elsewhere) and the straightforward textual interpretation of the DJA, the appropriate action for federal courts to take when presented with business interruption claims brought under the DJA is to remand to state court, so the case may progress up to the ultimate decision-maker, the state supreme court).

state law issues, none which were adhered to in *DiAnoia's Eatery, LLC* or in circuits' decisions ruling on the merits of COVID-19 business interruption cases. The first preventative measure should have been the discretionary nature of the DJA itself, which is supposed to afford district courts broad discretion to remand where they deem it appropriate.[177] Here, considering the novel nature of the claims as proclaimed by insurance law experts and as evidenced by contradicting state court decisions, that discretion to remand should have been utilized.[178] Another solution to this mistake which would have placed the law back in state court hands, scholars assert, was certification to state supreme courts.[179]

The United States Supreme Court has also introduced doctrines advising that federal courts should avoid unnecessary adjudication of state law issues, particularly where it creates the potential for friction.[180] For instance, the Abstention Doctrine put forward by the Supreme Court instructs federal courts to let state courts hear these cases first, to further the interests of federalism.[181] By following Judge Roth's reasoning, nationwide U.S. Circuit Courts of Appeal would have provided parties an opportunity to obtain a more permanent, unassailable decision from the state supreme courts, while

177. For further discussion on this point, see *supra* Section II.A.

178. *See* Knutsen & Stempel, *supra* note 21 (insurance law treatise authors); Huntington Ingalls Indus., Inc. v. Ace Am. Ins. Co., 287 A.3d 515 (Vt. 2022) (state supreme court reversing and remanding case which had dismissed COVID-19 business interruption claim).

179. *See generally* French, *supra* note 35 (arguing that U.S. supreme court precedents support state supreme court certification in cases of business interruption insurance cases).

180. The Supreme Court has noted the importance of this doctrine on numerous occasions. *See Federal Non-Interference with State Jurisdiction and Abstention*, CONST. ANNOTATED, https://constitution.congress.gov/browse/essay/artIII-S1-6-7/ALDE_00001184/ (last visited Mar. 21, 2025). For instance, Justice Hugo Black urged "a doctrine of abstention . . . whereby federal courts, 'exercising a wise discretion,' restrain their authority because of their 'scrupulous regard for the rightful independence of the state governments' and the smooth working of the federal judiciary." Burford v. Sun Oil Co., 319 U.S. 315, 332 (1943).

181. *See Federal Non-Interference with State Jurisdiction and Abstention*, *supra* note 180 (noting "abstention can serve interests of federal-state comity by avoiding 'a result in "needless friction with state policies,"' and can spare 'the federal courts of unnecessary . . . adjudication'") (quoting La. Power & Light Co. v. City of Thibodaux, 360 U.S. 25, 33 (1959); Harrison v. NAACP, 360 U.S. 167, 177 (1959)). An example of this "friction" may be found in Shaull, *supra* note 106, at 1168 (discussing Farmland Indus., Inc. v. Republic Ins. Co., 941 S.W.2d 505 (Mo. 1997)). There, in support of his argument that federal courts should less frequently employ *Erie* guesses, the author points to *Farmland*, where the Missouri Supreme Court sharply criticized federal courts on the matter in a case involving the definition of "damages" in an insurance context. *Id.*

upholding "the Supreme Court's instruction to federal courts [to abstain] . . . when asked to resolve novel or difficult questions of state law that involve public policy problems of substantial public import, policies that transcend the importance of the cases at bar."[182]

Once the self-reinforcing federal lockstep is solidified, state courts rarely subsequently act to undo it—which is, of course, an issue unto itself.[183] But another issue is that the Supreme Court could, with a single decision, overturn the entire federal precedent on the issue. The Court could, and has, sided with circuit courts vastly outnumbered on an issue to—in effect—overturn the law for the vast majority of Americans.[184] This is why it is so crucial for state courts to issue these decisions, rather than federal courts. State courts can provide resolute, binding declarations on the law of their state. Federal courts merely guess (sometimes, poorly), and their guesses are subject to a review which could overturn business interruption insurance law nationally.[185]

The previously-noted perception of high-quality decision making from federal courts means that when the courts act in consensus, they are not often second-guessed. And indeed, some—although certainly not all—insurance law experts agree that the vast majority of federal courts got it right, and that the standard business interruption clause does not cover COVID-19.[186] But the manner in which that result was reached leaves open the opportunity for universal federal reversal. It also encroached on state courts' role as ultimate arbiter of state law, and disregarded Supreme Court precedent.[187] Thus,

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182. DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192, 215 (3d Cir. 2021) (Roth, J., dissenting); *see also supra* note 106 and accompanying text (discussing limitations on federal court decisions on state law matters). Another alternative would have been to certify the question of business interruption clause coverage to the Pennsylvania and New Jersey Supreme Courts. *See* French, *supra* note 35, at 156 (arguing federal courts frequently make incorrect *Erie* guesses, and instead should simply certify questions to state court).

183. *See* French, *supra* note 35, at 159 (observing the "butterfly effect" of federal court decisions on the topic influencing other courts' decisions).

184. For discussion of a recent, non-insurance example, see Mallory Brown, Note, *"Outside the Bounds":* Counterman v. Colorado*'s Effect on Amateur Athletics*, 32 JEFFREY S. MOORAD SPORTS L.J. 1 (2025) (highlighting Supreme Court decision which overturned seven out of nine circuits in establishing a subjective speaker test for state laws implicating First-Amendment "true threat" exceptions).

185. *See supra* note 184 and accompanying text; *see also* Shaull, *supra* note 106 (criticizing federal courts' *Erie* predictions in the insurance context).

186. For an example of insurance scholars who profoundly disagree, compare Knutsen & Stempel, *supra* note 22, with French, *supra* note 114 (each arguing policyholders' substantive arguments that business interruption litigation held merit).

187. *See supra* notes 180–181 and accompanying text.

federal courts' lockstep decisions to reject the remand of business interruption clause litigation to state courts resulted in the imposition of improper federal common law.[188]

VI. UNPROTECTED: THE AFTERSHOCKS OF DIANOIA'S EATERY IN THE THIRD CIRCUIT

The Third Circuit's decision in *DiAnoia's Eatery, LLC* tremendously affected how business interruption claims were treated in the federal district courts within Pennsylvania and New Jersey.[189] After *DiAnoia's Eatery, LLC*, no federal court in those states granted remand under similar circumstances.[190] And in the 2023 decision *Wilson v. USI Ins. Serv. LLC*,[191] the Third Circuit ruled that business interruption clauses were not, as a matter of law, applicable to COVID-19.[192] Other circuit courts landed on the same outcome in corresponding decisions. To reach this result those courts often sought to predict how state supreme courts might rule, years before those courts—or even their intermediate appellate courts—ever took a stance on the matter.[193]

The federal court system is predicated on deference to the ultimate decision maker. Here, the Third Circuit and other federal courts' failure to

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188. *See supra* Section V.B.

189. *See, e.g.*, Am. Eagle Outfitters, Inc. v. Zurich Am. Ins. Co., No. 2:22-CV-00246-CRE, 2022 U.S. Dist. LEXIS 156108, at *8 (W.D. Pa. Aug. 30, 2022).

190. *Id.* (noting "[*DiAnoia's*] *Eatery, LLC* changed the landscape for motions to remand in COVID-19 insurance coverage cases . . . . no case in the Third Circuit [has granted] remand under these circumstance since . . . [*DiAnoia's*] *Eatery*").

191. 57 F.4th 131 (3d Cir. 2023).

192. *Id.* at 133 (holding business interruption coverage generally did not apply to COVID-19 shutdown orders). The court held this way despite the existence of Third Circuit precedent applying Pennsylvania substantive law which indicates non-traditional harms might cause 'physical' damage. *See* French, *supra* note 114, at 20–21 (noting "the Third Circuit has held the presence of e-coli bacteria . . . could constitute physical loss or damage"); *see also* Motorists Mut. Ins. Co. v. Hardinger, 131 F. App'x 823, 826–27 (3d Cir. 2005) (noting *Port Authority* did not necessarily apply because Pennsylvania law governed, but holding even applying *Port Authority*, the bacteria constituted physical loss).

193. *See* Wilson v. USI Ins. Serv. LLC, 57 F.4th 131, 142 (3d Cir. 2023) (predicting each state court would rule for insurers). Three years after *DiAnoia's Eatery, LLC* was decided, the New Jersey and Pennsylvania Supreme Courts each ruled in accordance with the Third Circuit's decision. *See* Wayne Parry, *New Jersey Supreme Court Rules Against Ocean Casino in COVID Business Interruption Case*, AP, https://apnews.com/article/covid19-casino-insurance-coverage-business-interruption-dc4add53c3732b265a0bd4cec4974ce4 (last updated Jan. 24, 2024, 2:30 PM) (as to New Jersey); Ungarean v. CNA & Valley Forge Ins. Co., 323 A.3d 593 (Pa. 2024) (as to Pennsylvania).

defer was to the detriment of insureds and the federal system at large because it prevented the utmost authority on state law claims—state supreme courts—from exercising their authority.[194] The Third Circuit should have affirmed the district courts' reasonable exercise of discretion under the DJA to remand these cases. That decision, and those of circuit courts nationwide issuing rulings on the merits of COVID-19 business interruption cases, was a missed opportunity to remand a novel state law question back to state courts, where it belonged.[195]

194. *Cf.* DiAnoia's Eatery, LLC v. Motorists Mut. Ins. Co., 10 F.4th 192, 214–15 (3d Cir. 2021) (Roth, J., dissenting) (presenting Judge Roth's dissent based on similar arguments); *accord* Watkins, *supra* note 35, at 457–58 (arguing when federal courts decide such state law issues, they undermine state law sovereignty).

195. *See supra* Part V (arguing Third Circuit and other sister circuit ought to have remanded the business interruption claims to the appropriate state court, as authorized under the DJA).