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STEAL-A-DEAL, OTHER PEOPLES' MONEY, AND THE COMMERCIAL CRIME POLICY

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INTRODUCTION

Every now and then, you get the "Am I crazy?" call. The agent calls to tell you that the insured is making a big employee-dishonesty claim. When you ask about the nature of the loss, the agent tells you the employee was self-dealing, stealing corporate opportunities, breaching his fiduciary duties to the insured, peddling trade secrets, and making big bucks for himself and others by doing so.

That's when you think, "*This* is a covered loss under the crime policy? Am I crazy?" The agent knows this is a big account, and the insured has lost over a million dollars that it believes it would have banked but for the faithless former employee. Real money that the insured could and should have taken in is gone. They want to know how such a loss could *not* be covered. You want to know how to explain it to them.

"COVERED PROPERTY" LIMITS COVERAGE

Start with the policy language. Coverage Form A of the crime policy begins at Section A by promising that the insurer "will pay for loss of, and loss from damage to, Covered Property resulting directly from the Covered Cause of Loss [defined as "employee dishonesty"]." Subsection 1 defines Covered Property as '"Money,' 'securities,' and 'property other than money and securities.'"

The Crime General Provisions, at Section C "General Definitions," defines Money (subsection 2) as "a. Currency, coins and bank notes in current use and having a face value; and b. Travelers checks, register checks, and money orders held for sale to the public." Securities (subsection 4) are "negotiable and non-negotiable instruments or contracts representing 'money' or other property . . . but does not include 'money.'" Property other than money and securities is limited to tangible property with intrinsic value. All of these definitions are qualified by Section B, subsection 12., "Ownership of Property; Interests Covered: The property covered under this insurance is limited to property: a. That you own or hold; or b. For which you are legally liable."

These definitions provide some protection by themselves. In *Empire of Carolina, Inc. v. Continental Casualty Co.*, 414 S.E.2d 389 (N.C. Ct. App. 1992), the insured's former president embezzled over $278,000 during the policy period. The insurer conceded this amount, but the insured wanted another $222,000 in interest that allegedly accrued before proof of loss. The Comprehensive Dishonesty, Disappearance, and Destruction Policy covered loss of "money," defined in the policy as "currency, coins, bank notes and bullion, and travelers checks, register checks and money orders held for sale to the public." *Id.* at 391. Summary judgment for the insurer was affirmed on the ground that the court did not see the term "interest" in the definition and would not construe the term "money" as defined to include such interest.

In our scenario, did the dishonest employee cause the insured to lose money that it owned, instruments or contracts that it owned, or any tangible property with intrinsic value? If not, then the dishonesty did not cause a loss of Covered Property, which is all that the crime policy covers. Breaching duties to an employer by taking personal advantage of corporate opportunities, profiting from transactions that the employer had a right to do instead, or selling the employer's information do not cause losses of securities or tangible property owned by the employer.

What about loss of money? The insured's best argument is that the employee's dishonesty caused the loss of money to which the employer had a right. The employee did not take any "currency, coins, or bank notes" that the employer "owned or held." What he did was breach duties, enter into wrongful transactions, and thereby receive money that might or might not have come to the employer had the employee not been dishonest. The plain language of the crime policy General Conditions does not appear to cover such an occurrence.

CASES BEFORE THE POTENTIAL INCOME EXCLUSION

That was the result under similar language in *Levy v. American Mutual Insurance Co.,* 73 A.2d 892, 893 (Md. 1950), where the Maryland Court of Appeals held that the defined covered property, including "money," did not apply to the money the dishonest employee made by stealing the profits from a sales transaction for himself.

In *Levy*, the insured sold uniforms and the employee routinely received orders from customers. Upon receiving from a regular customer an order for cab driver's hats, the employee arranged for the insured's regular supplier to make and ship the hats and to bill him directly. The employee paid the supplier, collected from the cab company, and kept the profits. He then continued this scheme with that and other customers by telling them that the insured no longer could supply them but that he would instead. His total profits were over four times his highest annual salary while working for the insured. *Id*.

The insured argued that it lost both the profits that the dishonest employee made by diverting business belonging to the insured and the salary that it was paying the employee while he was competing with his own employer. The court rejected both arguments on the basis that the policy covered money, not loss of profits. Even though the salary paid was money, the insured received services from the employee in return (and gave him a raise each year, the court noted). *Id*. at 894. The court would not turn the crime policy into a liability policy for the employee's debt to the insured.

This type of result, though, has given other courts more trouble. When a transaction has occurred and generated real value that the employee should not have received, the employer clearly is the wronged party and is entitled to pursue recovery. The court in *Levy* saw that the remedy was against the employee. Two other courts focused on the insurer instead.

In *Eagle Indemnity Co. v. Cherry*, 182 F.2d 298, 298-299 (5th Cir. 1950), both the district court and the Fifth Circuit held that profits made by the insured's dishonest manager, who obtained steel in the insured's name but sold it for his own account, were a covered loss under

a fidelity bond with language somewhat similar to that in the crime policy. The steel industry was so tight that only long-standing customers could obtain steel from the mills. The manager used his employer's status as such a customer to order steel that he then sold to a conspirator, with whom he split the profits after marketing the steel. To add insult to injury, the manager even bought some of the steel back for his employer at over 150% of what it cost him originally.

The policy covered "loss of money or other property . . . belonging to the insured, or in which the insured has a pecuniary interest" if caused by fraud or dishonesty. *Id.* The court did not discuss the nature of the "money or other property" that the insured lost or how the manager's profits constituted such property. The court simply found "fraudulent and dishonest conduct on the part of [the manager] while the fidelity bond was in full force and effect, and that such constitutes a clear breach of the terms of the bond." *Id.* at 300.

Likewise, in *Boston Securities, Inc. v. United Bonding Insurance Co.*, 441 F.2d 1302 (8th Cir. 1971), the court held that profits generated by an employee's dishonesty were a covered loss to the insured employer. Boston Securities' office manager, Yates, sent potential customers to a competitor, who paid him a finder's fee in return. The manager claimed that he referred only those who his employer would not have accepted as customers. The court was unimpressed: "In referring potential or even rejected customers of [the employer] to other institutions of which the company was unaware, and which was contrary to the practices of the industry, Yates created a malfeasant conflict of interest from which the employer suffered." *Id.* at 1304. Again, the court focused on the employer's loss and the employee's liability for self-dealing and disloyalty, not on what covered property was lost.

These older cases did not involve the current language of the crime policy, which limits the loss to "covered property" "resulting directly from" employee dishonesty. The indirect nature of the lost potential gain in those cases should exclude them from coverage under the policy as it is today. The losses were indirect because the insured had no out-of-pocket reduction in net worth and because the claimed amount resulted not directly from the dishonesty but from the independent efforts of the unfaithful employee in generating a profit. In theory, this restrictive language alone should be sufficient to limit the scope of coverage so that stolen deals, self-dealing, and improper competition are excluded.

THE POTENTIAL INCOME EXCLUSION

Still, the more restrictive language of the policy today might well not deter a court from seeking to make the fidelity insurer effectively pay the insured for the wrongdoer's liability or some third-party's ill-gotten gains. Fortunately, the crime policy has a specific exclusion aimed at this type of problem claim. Section A of the Crime General Provisions states as follows:

> We will not pay for loss as specified below:
>
> 3. Indirect Loss: Loss that is an indirect result of any act or "occurrence" covered by this insurance, including, but not limited to, loss resulting from:

a. Your inability to realize income that you would have realized had there been no loss of, or loss from damage to, Covered Property.

The financial institutions bond version, and the one previously in the crime policy, is known as the potential income exclusion. The change in the crime policy from a separate exclusion to one of three parts of the "indirect loss" exclusion did not alter the substance of the exception from coverage. The insured may suffer a covered loss if a dishonest employee takes or damages the insured's money, securities, or tangible property with intrinsic value. Stolen corporate opportunities, "deals," or intangible rights, although valuable, are not property under the policy. Covered loss also does not include the indirect consequences of the employee's taking or damaging of covered property, such as the lost ability to generate revenue from the property.

The crime policy covers complete loss of or damage to limited categories of property owned by the insured. If the insured recovers the property, no loss occurs. For example, if an employee stole the insured's stud bull, kept it for a month, then was arrested and the bull recovered, the insured would have suffered no loss. From the insured's perspective, of course, the stud fees that could have been earned by the insured during that month would be a loss. Such unrealized fees are speculative, are not a loss resulting directly from the employee dishonesty (i.e. the employee did not steal the fees from the employer's cash box), and are excluded expressly by the above policy language.

Even worse for the insured, though, is accepting that the dishonest employee may profit from the dishonest acts and obtain value that the employer could have received, but for the dishonesty. In the above example, if the employee markets the bull's services and collects stud fees during the month before his arrest, the amount the employer might have received instead is much less speculative. The employer (and the court) will know exactly what amount of profit the dishonest employee received and which the employer perhaps could have received instead. Faced with stolen covered property and an easy way to quantify the loss from employee dishonesty, the insured will (and the court may) want to find that loss covered by the crime policy. The insured in essence will value the covered property for the time that it is gone by calculating the income it actually generated during that time.

The simple answer is that the fidelity insurer did not bargain to cover this type of loss. The loss may be real, in the sense that someone other than the employer profited from wrongful use of covered property, but the policy covers not wrongful use but only permanent loss of or damage to that property. If the bull were stolen and never recovered, the insurer would owe the replacement cost of the bull but not the lost potential stud fees during the time between loss and replacement. Again, if the bull were recovered after replacement, the insurer would be entitled to sell the bull and recover its payment, so that no loss ultimately would have occurred. The policy does not cover temporary loss of use of or loss of ability to profit from covered property.

Suppose the dishonest employee does not steal the employer's bull but rather engages in self-dealing by contracting the bull's services to customers for his own account and keeping the proceeds of those contracts. The insured has suffered no loss of or damage to covered

property, and the dishonest employee's profit is not the insured's loss. The employee has stolen a business opportunity and made money that, possibly, the employer could have made. Stolen deals and other peoples' money are not covered by the crime policy. What would be covered is embezzlement by the employee of stud fees already collected by the employer ("money") or damage to or permanent loss of the bull ("other property") due to the employee's dishonest acts.

DISTINGUISH THE EXCLUSION UNDER THE FIB

The conclusion reached by this analysis is that the language of Coverage Form A concerning loss of or damage to "covered property" "resulting directly from" employee dishonesty should be enough to limit coverage without the need for the indirect loss exclusion. The exclusion, when still known as the potential income exclusion, was imported to the predecessors of the current crime policy from the bankers blanket bond between 1976 and 1980, then transformed into its present version in 1986. The bankers blanket bond covers loss, which is neither defined nor limited to covered property. For this reason, the exclusion of potential income is much more important under that policy than under the more restrictive crime policy.

The litigation generated by the exclusion overwhelmingly has arisen under the bankers bond or its successor, the financial institutions bond. There, the primary problem is that bankers' losses are money, and what bankers do for a living is make money from money, i.e. interest. Banks seek to earn interest on their money every single minute, day and night. A banker must have coined the phrase, "Time is money." Judges, just like everyone else, are familiar with this concept that what bankers "produce" is interest earned from money invested.

When a dishonest bank employee embezzles by forging or creating a fictitious note, the bank delivers money to that employee. From that moment, the bank may look only to the dishonest employee for the interest that the bank's money otherwise would have been generating. When the employee's scheme blows up, the bank wants to recover its principal and the interest that could have been earned. The potential income exclusion tells the insured bank that the insurer will not cover the interest that could have been earned had the bank not been victimized by its dishonest employee.

Unfortunately, the courts have a hard time accepting this limitation on coverage, probably because of the nature of a bank's business in making money from money. Despite the potential income exclusion, many courts have insisted that interest on fictitious notes is part of the insured bank's covered loss under the FIB. Attached to this paper as an appendix is a list sampling some of the articles written on this exclusion and the courts' treatment of it under the FIB. Generally, the interest is treated no differently from the principal.

THE EXCLUSION, THE CRIME POLICY, AND THE COURTS

The addition of similar language of exclusion in the crime policy may have been less critical, since other businesses do not focus so directly on interest and interest-bearing instruments. Most losses under the crime policy involve either money or tangible property, such as inventory. The potential income exclusion nevertheless has not eliminated litigation over claims for unrealized income and other peoples' money.

In *United States Gypsum Co. v. Insurance Company of North America*, 813 F.2d 856 (7th Cir. 1987), an employee leaked the formula for a special adhesive to his employer's competitor, who grossed over $139,000 from sales of counterfeit adhesive before being stopped. The decision does not indicate whether or not the employee was paid for his information. The crime-policy insurer denied the claim based on the potential income exclusion, and the insured sought declaratory relief and penalties. The insurer first obtained summary judgment on bad faith, with the trial court ruling that, at a minimum, the exclusion provided a good-faith basis for the insurer's denial of the claim. *United States Gypsum Co. v. Insurance Company of North America*, No. 85 C 4704, 1985 WL 3514 (N.D. Ill. 1985). With that foreshadowing, the subsequent summary judgment for the insurer on the merits of the exclusion was no surprise.

The Seventh Circuit noted that the policy covered "Loss of Money, Securities and other property which the Insured shall sustain through any fraudulent or dishonest act or acts committed by any of the employees." 813 F.2d at 857. The court, and presumably the insurer, never addressed whether this scope of covered property included trade secrets. The insurer framed the defense around the potential income exclusion, and that became the sole focus of the decision.

The trial and appeals courts agreed that the case presented exactly the situation contemplated by the exclusion's language. The employee, Banks, did not steal tangible property valued by what it could earn while missing, as the insured argued.

> Even if we follow Gypsum's hypostatization and treat the trade secret, a concept, like an object, theft is not the correct analogy. Banks did not deprive Gypsum of the trade secret. It is not as though Gypsum had [an adhesive] making machine and Banks stole it; it is as though Banks used the [adhesive] machine in his garage after work and sold the illicitly made [adhesive]. Gypsum still had the formula and rights to it. Gypsum did not allege that the events caused Gypsum to lose the formula or the rights, through the formula becoming public, for example.

Id. at 858.

The court went on to demonstrate a full understanding of the exclusion. If Banks had stolen an adhesive-making machine, the policy would cover the cost of the machine but not the lost sales of adhesive during replacement. If the insured recovered the machine in working order, it would sustain no loss despite its lost potential revenue. The court then highlighted at least one rationale for the exclusion:

> Gypsum has the most control over how much it will suffer in the market as a result of the dishonesty of its employees. [The insurer] expressly declined to take on the risk of such losses, effectively forcing a strict duty of mitigation of such costs upon Gypsum. In the machine analogy, Gypsum must act quickly to

> replace the machine or face the loss of sales. In a case like the present, Gypsum must move to stop the sales of counterfeit [adhesive].

Id.

The court also offered a straw-man argument on the insured's behalf: the trade secret could be valued at its total income-generating potential over its useful life, so that any temporary loss of use or misuse by another would damage the value of the property. Knocking down the straw man, the court concluded that the trade secret still has the same income-producing ability to the insured before and after the competitor's improper use. *Id.* at 859. The court's logic is not crystal clear but appears to be based on valuation. Nor did the court explain why it even reached the exclusion, since no covered property had been lost. Still, the court did retain its grip on the key point that the insured had not lost any property as defined in the policy.

In *Diversified Group, Inc. v. Van Tassel*, 806 F.2d 1275, 1275-1276 (5th Cir. 1987), Van Tassel and an associate were employed by Diversified Group (DGI) to prepare bids to the federal government for lucrative, long-term contracts to berth sea-going vessels. In addition to preparing bids for DGI, Van Tassel used DGI facilities and resources to prepare and submit lower bids on behalf of his own corporations, which won the government contracts. DGI claimed for the lost profits it would have made had it received the contracts instead and also for the out-of-pocket expenses and diverted assets and resources used by Van Tassel in his disloyal activities. The trial court granted summary judgment for the insurer on all claims.

In a decision reinforcing the hard work of all volunteer authors in the fidelity practice, the Fifth Circuit panel read, cited, and confirmed Ben Lentz's early article on the likely effect of the potential income exclusion. *Id*. at 1277-1278 (citing Lentz, *Profit and the Potential Income Exclusion*, 19 FORUM 694 (1984)). That article persuaded the court that the exclusion is unambiguous and excludes future profits or future income flow lost because of an employee's dishonest acts. The court also correctly noted that the cases construing the exclusion in the context of bankers bonds offer "no guidance to our present inquiry," a helpful distinction. *Id*.

The circuit court affirmed the trial judge on lost profits but reversed and remanded as to DGI's claims for travel funds, salaries during diverted time, telephone charges, corporate facilities and overhead, secretarial assistance, and supplies taken by Van Tassel in furtherance of his dishonest scheme. These amounts were small in relation to the lost profits, but they were not "income that you would have realized" and so were not excluded. Instead, the court decided they were "money" and "other property" that could have been lost directly because of the dishonest acts, and so susceptible to coverage. The court did not address how the dishonesty "directly" caused the loss of the overhead and expenses but did note that DGI might have a hard time bearing its burden of proof as to those items of claimed loss. *Id*. at 1278.

Another court that had no problem applying the clear meaning of the potential income exclusion was the Supreme Court of New York for New York County in *Drexel Burnham Lambert Group, Inc. v. Vigilant Insurance Co.*, 595 N.Y.S.2d 999 (1993). Although almost lost in the waves of litigation, bankruptcies, criminal charges, securities violations, and other fidelity

questions arising out of the Michael Milken/Ivan Boesky insider-trading scandal, the exclusion played a part in the results for the 51 fidelity bonds in issue. Those bonds all were Bankers and Brokers Blanket Bonds, which therefore did not limit their coverage to "Covered Property" but did exclude "failure to realize potential gains" and losses caused by "disclosure of confidential information." *Id.* at 1004-1005. Milken and his dishonest colleagues misused insider information, allowing others to profit handsomely, and diverted corporate opportunities that should have accrued to his employer, the insured.

The court ruled against the insured without anything more than reciting the policy language:

> There is no coverage provided for lost profits or for "loss of potential income," though Drexel persists in alleging it was deprived of "opportunities." The complaint alleges Levine and Milken stole not assets but confidential information to amass their profits, but losses arising from "theft of confidential information" are expressly excluded (End. 7). Abuse of the use of confidential information is not the equivalent of monetary theft.

Id. at 1007. While not construing the current language of the crime policy verbatim, the observations about the nature of what was stolen or misused is pertinent and helpful. The definition of "Covered Property" under the crime policy excludes opportunities and confidential information as clearly as did these exclusions in the Drexel bonds.

THREE NATIONAL UNION CASES: WHAT WENT WRONG

Three National Union cases from 1986-1990 are important to understand because of what they say about the potential income exclusion—and what they do not say. All three unfortunately ruled against the insurer, one held the exclusion to be ambiguous, one did not but has been misread, and none truly dealt with "potential income." The lesson from these cases is that simply calling property "potential income" probably will not defeat coverage.

In *Koch Industries, Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA.*, No. 89-1158-K, 1989 WL 158039 (D. Kan. 1989), the dishonest employee, O'Brien, received kickbacks in return for selling oil to non-qualifying buyers at over-discounted prices. National Union first argued that this conduct did not fall within the definition of dishonesty under the policy; while the court agreed that summary judgment could not be entered against the insurer on this point, it also set a difficult standard for the insurer to meet at trial.

More importantly, National Union argued that the difference between the correct price to which Koch was entitled and the over-discounted price actually received for its oil was lost profit and therefore excluded as potential income. In support of its argument, National Union correctly told the court that "each and every one of the courts that has interpreted this exclusion, have [sic] found it to be 'clear and unambiguous," citing *Diversified Group* and *United States Gypsum*. *Id.* at *17. The court, unfortunately, found this statement to be "without merit, . . . false and viewed with much disfavor by this court." *Id.* Translated from judge-speak, that means, "I am going to see that you lose this case if at all possible."

The problem was that the trial judge had come upon and misread *James B. Lansing Sound, Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA.*, 801 F.2d 1560 (9th Cir. 1986). Without going into detail, *because it was not a potential income* decision, that case involved a complex scheme by JBL employees to divert audio equipment to unauthorized dealers who could undercut the employer's authorized dealers. The benefit to the employees was receipt of their standard commission on much increased sales, at their employer's expense. National Union in that case proposed to pay for the diverted equipment at JBL's cost, but the insured wanted the equipment valued at wholesale price.

The case therefore was about valuation under the policy, and the court found the valuation language to be ambiguous and not properly applied by the insurer. Just before the paragraph in which it made that finding, the court considered the inventory exclusion and the potential income exclusion and expressly found them to be inapplicable: "The proof of losses that JBL suffered did not require an inventory or profit and loss computation, nor does fair market value include potential income in the nature of interest and dividends." *Id.* at 1565. In the next paragraph, the court returned to the valuation language and found it ambiguous.

Despite these completely separate findings in *James B. Lansing Sound*, the trial judge in *Koch Industries* somehow concluded that the earlier case had ruled against National Union on the ambiguity of the potential income exclusion. He then assumed that National Union intentionally attempted to mislead him in the case before him, and he obviously took great offense. Without any further analysis, the trial judge ruled that the exclusion was ambiguous and therefore did not apply to the lost profits caused by the dishonest employee's underpricing of the oil. *Koch Industries,* 1989 WL at *19.

What did the insured lose in *Koch Industries*? Ironically, the insured itself viewed the fraudulent transactions as losing money on the sale of oil, which would be excluded potential income. No one knows if the colluding customer, or anyone else, would have bought the oil at full price. The employer did not have the proceeds of a full-price sale in the bank and then lose those proceeds to embezzlement by the employee. The pricing differential was lost only on paper and thus was nothing more than potential income.

Another way to view these transactions, though, is that the employee was delivering too much oil for the money received by his employer, which is no different from stealing the extra oil and selling it for the kickbacks. If the employee sold, for example, 1,000 gallons at $80 per gallon when the price should have been $100, the $80,000 received represented only 800 gallons at the correct price. Because 1,000 gallons are missing from inventory, while the employer got paid for only 800 gallons, the employee effectively stole 200 gallons. Under this view, the court already was leaning toward finding coverage for the stolen property, and the misreading of *James B. Lansing Sound* just added righteous indignation to the pre-ordained result. (This erroneous finding that the exclusion is ambiguous unfortunately was adopted in a bankers blanket bond case, *Mid-America Bank of Chaska v. American Casualty Co.*, 745 F. Supp. 1480 (D. Minn. 1990) (renewal loans).)

National Union also lost the flip-side of this fact pattern in *Hanson PLC v. National Union Fire Insurance Co. of Pittsburgh, PA.*, 794 P.2d 66, 75 (Wash. App. 1990). There, the dishonest employee knowingly paid a supplier not only for useable material but also for large

quantities of worthless material, allegedly because the supplier threatened to cut off all deliveries and leave the employee's part of the operation (and his job) at risk. National Union argued that the excess payments to the supplier resulted in decreased profits and thus were subject to the potential income exclusion.

The court saw it differently: "The damage sought in the present case is not potential income. Rather, [the insured] seeks damages equaling the amount by which [the supplier] was overpaid. Thus, National Union's argument that [the insured's] claim falls within the potential income exclusion is without merit." *Id.* As with *Koch Industries* above, one way to view the loss is as money taken from the employer in return for nothing of value, no different from any embezzlement. In one case, property was lost for no return of money; in the other case, money was lost for no return of property. Both property and money are covered by the crime policy, and neither was potential income on these facts.

A RECENT CASE: DÉJÀ VU

All is not lost, however. Ending up back near where we started, the definition of "covered property" together with the indirect loss exclusion should be adequate protection for the fidelity insurer, as it was in the relatively recent case of *Benchemark Printing, Inc. v. American Manufacturers Mutual Insurance Co.*, No. 00-CV-0865, 2001 WL 66310 (N.D.N.Y. 2001). Errico, sales manager for the insured, for years had been telling Benchemark's customers that their printing jobs were being subcontracted out. At the same time, he told his employer that the customers' business had been lost to competitors. In this way, Errico arranged for the printing to be done by another company, marked up those invoices, and kept the profit.

The crime policy language in issue was the current version, as quoted above, and employee dishonesty was not disputed. The first issue was whether the claimed losses are "covered property" under the policy. The court said no.

> In this case, what Benchemark really lost were business opportunities whereby Errico essentially put himself in the place of his employer. As a result, Benchemark lost the opportunity to either perform the contracts itself or refer them out. Had it performed the contracts itself, then it would have received a profit. Had it referred them out, then it would have received the kickback. In either case, Benchemark is asking [the insurer] to cover lost profits it hoped to receive. It cannot show that it actually earned, owned, ever held, or had any liability for these profits. Accordingly, Benchemark's alleged losses of the kickbacks paid to Errico and profits are not covered property under the clear language in the insurance policy and are not recoverable.

Id. at *3. The court did not fall into the trap of calling the potential income "money," because the insurer never "earned, owned, ever held, or had any liability for" that income.

The court also considered the indirect loss exclusion and found that it did not apply.

The starting point was the insured's claim that the lost profits were the covered property it had lost and sought to recover. The court noted that the exclusion denies coverage for loss of the ability to realize income that the insured would have realized but for the loss of covered property—in this case, the lost profits themselves. The conclusion was that the insured was not seeking to recover any income that it could have realized from the lost profits, so the exclusion was irrelevant. *Id.*

This tricky dicta was unnecessary, because the potential income exclusion by definition applies to claims for lost profits, not claimed loss of covered property. While the scope of coverage and the exclusion may overlap in their denial of some losses, that overlap does not make the exclusion any less applicable. The court's reasoning simply reveals the Catch-22 awaiting the insured seeking coverage for this type of claim.

CONCLUSION

Stolen deals and other peoples' money that insureds claim under the crime policy will continue to give both insureds and the courts indigestion. Although the policy covers some losses caused by employee dishonesty, and the insured's loss may be real, the loss must involve covered property and be a direct result of the dishonest act. Explaining the limited scope of coverage and the effect of the potential income exclusion will give insurers headaches for the same reasons: an employee was dishonest and caused the insured to suffer a loss, but not one that is covered. Careful reading of the policy and the cases may not be a cure-all, but it can help to keep you from going crazy.

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APPENDIX

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