Innovation Growth Partners Specialty®

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Cyber Insurance and Vendor Subrogation Issues

Cyber insurers pursue subrogation against vendors when the vendor's negligence contributes to a cyber incident for which the insurer paid a claim. This process allows the insurer, after compensating its policyholder, to seek recovery from the responsible third party, such as an IT provider who made configuration errors, failed to patch vulnerabilities, or neglected security controls. It is a growing area in cyber insurance, and insurers will scrutinize vendor contracts and performance as part of a claim.

How Subrogation Works

- After a cyber incident, a policyholder may file a claim with their cyber insurance company.
- The insurer pays for the covered losses, such as data recovery, business interruption, and other costs.
- The insurer then "steps into the shoes" of the policyholder to pursue the responsible party, which can be a vendor, for reimbursement of the claim amount. This is called subrogation.

Common Scenarios for Subrogation Against Vendors

Configuration Errors
An IT vendor makes an error during a firewall or security implementation, leading to unauthorized access.

Failure to Patch
A vendor neglects to apply critical patches or updates, allowing a vulnerability to be exploited.

Breach of Contract
A managed service provider (MSP) fails to maintain security controls as required by the contract, leading to an attack like ransomware.

Incident Response Failure
A vendor fails to properly notify stakeholders or take timely and effective remediation steps after an incident is detected.

Why This is a Growing Trend

Increasing Claims
The number of cyber insurance claims is rising, leading to higher premiums and increased scrutiny of potential sources of loss.

Vendor Vulnerability
Many breaches are traced back to third-party vendors, whether through direct attacks or vulnerabilities in their services.

Contract Analysis
Insurers are requesting vendor contracts to evaluate the terms, including security obligations and liability limitations, which can impact coverage and subrogation rights.

Considerations for Policyholders

Vendor Contracts
Your vendor contracts can directly affect your insurance coverage and potential subrogation rights. A contract that limits a vendor's liability can put you in breach of your own insurance policy if it impairs the insurer's subrogation rights.

Waivers of Subrogation
To address the liability limitations in vendor contracts, you can negotiate a partial waiver of subrogation for your cyber insurance policy to ensure the insurer cannot claim its subrogation rights have been impaired by your contracts.

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