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Fifth Circuit Finds No Coverage for \$6M Phishing Scheme Loss Where Insured Never “Held” Client Funds

BY: Jason Taylor

The Fifth Circuit recently affirmed a District Court decision holding that RealPage, Inc., was not entitled to insurance coverage for a \$6 million phishing scheme loss. *RealPage Inc. v. Nat’l Union Fire Ins. Co. of Pittsburgh*, No. 21-10299 (5th Cir., Dec. 22, 2021). The insured, RealPage, provided services for property owners and managers in the real estate industry, including the collection of rental and other payments from residents and the transfer of those payments to its property manager clients. After a RealPage employee clicked a fake link in a seemingly innocuous email and provided login information for RealPage’s account with a third party payment processor, Stripe, Inc., the fraudsters stole the login credentials. The fraudsters then used the credentials to divert millions of dollars in rent payments from tenants intended for RealPage’s property manager clients. RealPage and Stripe recovered some of the stolen funds but lost about \$6 million to the phishing perpetrators. RealPage reimbursed its clients and filed claims under its commercial crime insurance policies for the stolen funds. The insured’s primary insurer, National Union, denied coverage determining the lost funds were not covered losses because RealPage never “held” the funds. RealPage then filed a coverage action challenging the denial of coverage. The district court agreed with the insurer and granted summary judgment. Earlier this month, the Fifth Circuit affirmed.

The central issue to the coverage determination was whether the insured “held” the diverted funds despite its use of a third-party payment processor, Stripe. RealPage’s commercial crime policy issued by National Union covered losses from employee theft, forgery, alteration, theft of money and securities, robbery, safe burglary, computer fraud, and funds transfer fraud. Recovery under the policy, however, was conditioned on several factors. Specifically, subsection (p) of the policy’s Conditions stated:

The property covered under this policy is limited to property:

- (1) That you own or lease; or
- (2) That you hold for others whether or not you are legally liable for the loss of such property.

RealPage did not argue that it owned or leased the money that was designated for its property manager clients, so its claim for coverage turned on the meaning of “hold.” The Fifth Circuit looked first to the dictionary definition of the term “hold,” and reasoned that the one defining characteristic of the term “hold” was *possession*. According to the Court, RealPage never had possession or custody of the client funds. The transactions between tenants, Stripe, and RealPage’s property manager clients were structured so that once the tenants entered their bank or credit card account information into RealPage’s online portal, RealPage transmitted that information to Stripe for processing and did not save it. “Beyond providing tenants’ and property managers’ account information, RealPage had no further involvement. In other words, when money changed hands, RealPage’s fingers never touched it,” and thus, RealPage never “held” or “possessed” the funds intended for its property manager clients.

The insured also argued that “control,” rather than “possession,” was the proper definition of “hold” as used in the National Union policy. While the Fifth Circuit rejected RelPage’s interpretation, it reasoned that *even if* one were to conflate “hold” with “control,” RealPage ultimately never controlled the funds. For example, all funds processed through Stripe were deposited “in pooled clearing accounts” at Wells Fargo bank. These were Stripe’s accounts, not RealPage’s. In fact, Stripe’s services agreement with RealPage expressly provided that RealPage had “no rights to the Clearing Accounts or to any funds held in the Clearing Accounts.” RealPage was “not entitled to draw funds from the Clearing Accounts,” and Stripe reserved the right to impose conditions on the release of any funds. While Stripe handled the funds as RealPage directed, Stripe, not RealPage, ultimately controlled the funds in Stripe’s custody.

In the end, because RealPage never held the funds at issue, National Union was within its rights to deny coverage of the stolen funds intended for RealPage’s property manager clients, and the district court’s summary judgment in favor of the insurer was affirmed.