IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

TAGGED, INC.	*	
	*	
v.	*	Civil No. JFM-11-127
	*	
SCOTTSDALE INSURANCE COMPANY	*	
	*	
	*	

******

MEMORANDUM

Plaintiff Tagged, Inc. ("Tagged"), brings this action against its insurer, Defendant Scottsdale Insurance Company ("Scottsdale"). In November 2010, following an investigation of alleged fraudulent and deceptive acts and false advertising, Tagged entered into a settlement with the New York Attorney General ("OAG"). Tagged now seeks reimbursement from Scottsdale for its defense costs from this investigation and the fine paid under the settlement agreement. Pending before the court is Scottsdale's Motion to Dismiss.[1] The Motion will be granted.

[1] Scottsdale attached several exhibits to its Motion. Tagged contends consideration of these documents requires the court to convert Scottsdale's Motion to a motion for summary judgment. The Second Circuit has held that a district court may consider the following materials in deciding a motion brought pursuant to Federal Rule of Civil Procedure 12(b)(6): "the facts alleged in the complaint, documents attached to the complaint as exhibits, . . . documents incorporated by reference in the complaint," and documents that are "'integral' to the complaint" and about which there are "'no dispute[s] . . . regarding . . . authenticity or accuracy.'" *DiFolco v. MSNBC Cable L.L.C.*, 622 F.3d 104, 111 (2d Cir. 2010) (citations omitted); *see also Brass v. Am. Film Techs. Inc.*, 987 F.2d 142, 150 (2d Cir. 1993). A document is "integral" to the complaint if "the complaint 'relies heavily upon its terms and effect.'" *DiFolco*, 622 F.3d at 111 (quoting *Mangiafico v. Blumenthal,* 471 F.3d 391, 398 (2d Cir. 2006)). With its Motion, Scottsdale submitted the insurance policy it issued to Tagged and the OAG's "Notice of Proposed Litigation" ("OAG Notice"). Tagged does not contest the authenticity or accuracy of either document. The insurance policy falls within the classic category of documents that may be considered although not attached to the complaint because it is a contract that gives rise to the legal obligations on which Tagged's claims are based. *See Ackerman v. Local Union 363, Int'l Bhd. of Elec. Workers*, 423 F. Supp. 2d 125, 127 (S.D.N.Y. 2006) ("The classic examples of documents that may be considered on a motion to dismiss even though the plaintiff does not physically attach them to the complaint are the contracts that underlie the claims in suit.").

I.

The present suit concerns Scottsdale's duty to defend and indemnify Tagged under Business and Management Indemnity Policy No. EKS3012578. (Def.'s Mot. Dismiss, Ex. B, Scottsdale Business & Management Indemnity Policy No. EKS3012578 ("Policy").) The Policy contains several sections establishing insurance coverage, two of which are potentially applicable in the instant action. First, the "Technology, Media, and Professional Services Coverage Section" ("TMP Section") includes the following insuring clause: "The **Insurer** shall pay the **Loss** which the **Insureds** have become legally obligated to pay by reason of a **Claim** first made against any **Insureds** . . . for a **Media Services and Technology Based Services Wrongful Act**." (*Id.*, TMP Section, § A.2.) An endorsement to the Policy specifies that this clause obligates Scottsdale to insure against a Media Services and Technology Based Services Wrongful Act only "if committed by an **Insured** in the course of performing **Professional Services**." (*Id.*, Endorsement No. 3.) For purposes of the TMP Section, the Policy limits the definition of "professional services" to "providing advertising services for others, for a fee." (*Id.*, Endorsement No. 27 (emphasis in original).) The TMP Section further contains several exclusions from coverage, including a media marketing exclusion, privacy exclusion, and sexual harassment exclusion. (*Id.*, Endorsement Nos. 25, 26, 32.)

Likewise, the OAG Notice is "integral" to Tagged's Complaint. This document was in Tagged's possession: The OAG sent it to Tagged, which forwarded it to Scottsdale. In addition, it is this document, Tagged asserts in its Complaint, that first triggered Scottsdale's duty to defend, and Tagged seeks to recover the defense costs it incurred following the receipt of the OAG Notice. (Compl. ¶¶ 4–5.) Accordingly, I may consider both documents.

Tagged also attached to its Opposition an Affidavit of Louis Willacy, its general counsel. This document is not attached to, incorporated in, or integral to the complaint, however. I will disregard this exhibit rather than convert Scottsdale's Motion to a motion for summary judgment. *See United States v. Int'l Longshoreman's Ass'n*, 518 F. Supp. 2d 422, 450 (E.D.N.Y. 2007).

The second possibly relevant coverage section, entitled "Directors and Officers and Company Coverage Section" ("D&O Section"), provides, inter alia, that Scottsdale "shall pay the **Loss** of the **Company** which the **Company** becomes legally obligated to pay by reason of a **Claim** . . . for any **Wrongful Act** taking place prior to the end of the **Policy Period**." (*Id.*, D&O Section, § A.3.) Under a "Professional Services Exclusion," however, the D&O Section excludes coverage for "any **Claim** alleging, based upon, arising out of, attributable to, directly or indirectly resulting from, in consequence of, or in any way involving the rendering or failing to render professional services." (*Id.*, Endorsement No. 28.)

Tagged operates a social networking website, Tagged.com. Tagged.com permits users aged 13 years and older, but it is targeted towards teenagers. (Def.'s Mot. Dismiss, Ex. A, N.Y. Office of the Att'y Gen. Notice of Proposed Litigation (June 10, 2010) ("OAG Notice"), at 3.) To distinguish Tagged.com from other social networking sites, Tagged has encouraged "users, including its minor users, to meet and form other relationships with new people" through the site. (Compl., Ex. A, *In the Matter of Tagged, Inc.*, Assurance of Discontinuance, ¶ 2.) Prior to and during the OAG's investigation, Tagged made a number of representations to assure its users—and, in the case of minors, their parents and guardians—of their safety in using the website and establishing connections with other users. In particular, Tagged's "Terms of Service" barred "members from engaging in certain inappropriate conduct such as uploading sexually explicit content or content harmful to minors," and it represented that it had "safety features in place to identify and remove illegal or inappropriate content and contact." (*Id.* ¶¶ 7–8.) In addition, Tagged requested users' assistance in policing the site for inappropriate conduct, encouraging them to report offensive, threatening, or objectionable material through specified links or in

emails to the "Tagged Safety Squad." Tagged made numerous statements declaring it would remove content that violated its Terms of Service. (*Id.* ¶¶ 8–9; *see also* OAG Notice, at 3–4.)

In response to a consumer complaint, the OAG initiated an investigation in March 2010. It found that Tagged.com contained many examples of inappropriate content, specifically "child pornography and sexually exploitive pictures of children, adult users who made sexual advances towards minor users, and adult users engaged in sexually explicit discussions with minor users and who advocated pedophilia and/or incest between adults and minors." (*Id.* ¶11.) Contrary to the company's representations, Tagged failed to remove this content promptly, even when reported by users. In many cases, the content was never removed. (*Id.* ¶¶ 11–12; *see also* OAG Notice 6–7.)

On June 10, 2010, the OAG issued a "Notice of Proposed Litigation," alerting Tagged of its intention to "commence litigation . . . pursuant to New York Executive Law section 63(12) and [New York General Business Law] sections 349 and 350, which prohibit illegal, fraudulent and deceptive acts and practices and false advertising in the conduct of business or the furnishing of services." (OAG Notice, at 1; *see also* Compl. ¶ 4.) The OAG Notice stated that Tagged's statements regarding the safety of Tagged.com users and its efforts to protect them from inappropriate content were "false and misleading." (OAG Notice, at 3.)

Tagged provided Scottsdale with notice of the OAG's claim, but Scottsdale declined to proffer a defense on the grounds that the claim was not covered under the Policy. (Compl. ¶ 6.) Tagged incurred more than $45,000 in attorneys' fees defending the claim before reaching a settlement with the OAG in November 2010. Under the settlement, Tagged agreed to pay a $750,000 fine, with a potential additional payment of $250,000 for future violations. Scottsdale has refused to indemnify Tagged for this loss. (*Id.* ¶¶ 13–16.)

II.

When deciding a motion brought under Federal Rule of Civil Procedure 12(b)(6), a court is "constrained to 'accept all factual allegations as true, and draw all reasonable inferences in the plaintiff's favor.'" *DiFolco v. MSNBC Cable L.L.C.*, 622 F.3d 104, 110–11 (2d Cir. 2010) (quoting *Shomo v. City of New York,* 579 F.3d 176, 183 (2d Cir. 2009)). To withstand such a motion, "a complaint must set out only enough facts to state a claim for relief that is *plausible* on its face." *Vaughn v. Air Line Pilots Ass'n, Int'l*, 604 F.3d 703, 709 (2d Cir. 2010) (citing *Ashcroft v. Iqbal*, --- U.S. ----, 129 S. Ct. 1937, 1949 (2009)) (emphasis in original). "This standard 'is not akin to a 'probability requirement,' but it asks for more than a sheer possibility that a defendant has acted unlawfully.'" *Id.* (quoting *Iqbal*, 129 S. Ct. at 1949). At minimum, the factual allegations of a complaint "must be enough to raise a right to relief above the speculative level, . . . on the assumption that all the allegations in the complaint are true (even if doubtful in fact)." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555, 127 S. Ct. 1955 (2007) (internal citations and alterations omitted). Thus, the plaintiff's obligation is to set forth the "grounds of his entitlement to relief," offering "more than labels and conclusions." *Id.* (internal quotation marks and alterations omitted). To suffice, the complaint must provide sufficient facts to permit "the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Iqbal*, 129 S. Ct. at 1949 (citation omitted).

III.

Under California law,[2] the goal of contract interpretation is to "give effect to the 'mutual intention' of the parties." *E.M.M.I. Inc v. Zurich Am. Ins. Co.*, 32 Cal. 4th 465, 84 P.3d 385, 389 (2004). If possible, a court should divine this intention "solely from the written provisions of the

[2] For purposes of this motion, the parties agree California law governs the Policy's interpretation and application.

contract." *Id.* The California Supreme Court has declared, "Words used in an insurance policy are to be interpreted according to the plain meaning which a layman would ordinarily attach to them," unless they have been used in a technical sense or given a special meaning by the parties. *Reserve Ins. Co. v. Pisciotta*, 30 Cal. 3d 800, 807, 640 P.2d 764 (1982); *see also E.M.M.I.*, 84 P.3d at 389. Language should be interpreted in the context of the policy as a whole, not in the abstract. *E.M.M.I.*, 84 P.3d at 389.

"An insurance policy provision is ambiguous when it is susceptible of two or more reasonable constructions." *Ameron Int'l Corp. v. Ins. Co. of Pa.*, 50 Cal. 4th 1370, 242 P.3d 1020, 1024 (2010) (citation omitted). Where the meaning of the policy language is clear, "[c]ourts will not adopt a strained or absurd interpretation in order to create an ambiguity." *Pisciotta*, 30 Cal. 3d at 807 (citations omitted). If a policy contains ambiguous terms, however, California law commands that the ambiguity be "'resolved in the insureds' favor, consistent with the insureds' reasonable expectations.'" *E.M.M.I.*, 84 P.3d at 389 (quoting *Safeco Ins. Co. v. Robert S.*, 26 Cal. 4th 758, 763, 28 P.3d 889 (2001)). Thus, "'exclusionary clauses are strictly construed against the insurer and in favor of the insured. . . . [A]ny provision that takes away or limits coverage reasonably expected by the insured must be conspicuous, plain and clear.'" *N. Am. Bldg. Maint., Inc. v. Fireman's Fund Ins. Co.*, 137 Cal. App. 4th 627, 40 Cal. Rptr. 3d 468, 479 (Ct. App. 2006) (quoting *Zurich Ins. Co. v. Smart & Final, Inc.*, 996 F. Supp. 979, 987 (C.D. Cal. 1998)). The insurer bears the burden of showing that an exclusion from coverage applies. *Id.*

In the present action, Tagged asserts that Scottsdale has breached both its duty to defend and its duty to indemnify Tagged under the Policy. "The duty to defend is both separate from and broader than a duty to indemnify." *Food Pro Int'l, Inc. v. Farmers Ins. Exch.*, 169 Cal. App.

4th 976, 89 Cal. Rptr. 3d 1, 8 (Ct. App. 2008) (citations omitted). Whenever a claim "raises the *potential* for coverage," the insurer bears a duty to defend its insured. *Atl. Mut. Ins. Co. v. J. Lamb, Inc.*, 100 Cal. App. 4th 1017, 1032, 123 Cal. Rptr. 2d 256 (App. Ct. 2002) (emphasis in original). Where, as here, an insurer allegedly "improperly refuses to defend the insured in violation of its contractual duties, the insured is entitled to make a reasonable settlement of the claim in good faith and may then maintain an action against the insurer to recover the amount of the settlement." *Isaacson v. Cal. Ins. Guarantee Ass'n*, 44 Cal. 3d 775, 750 P.2d 297, 308 (1988) (en banc) (internal quotation marks and citation omitted). Therefore, the proper inquiry in deciding Scottsdale's Motion is whether Tagged has plausibly alleged that the OAG's Notice gave rise for the potential for liability covered under the Policy.

A.

The TMP Section requires that, to qualify for coverage, the act giving rise to the claim was committed by Tagged while performing "professional services," which is defined for this Section as "providing advertising services for others, for a fee." (Policy, Endorsement Nos. 3, 27.) The factual allegations of the Complaint, the OAG's findings in the Assurance of Discontinuance, and the OAG Notice make clear, however, that at no time did the OAG's claim have any relationship to Tagged's paid provision of advertising services to others. The OAG's investigation and allegations focused solely on content posted by Tagged.com users, who did not pay to use the website, and Tagged's representations and advertising of its *own* services. Moreover, there is no potentiality for coverage merely because Tagged's income derives entirely from fees paid by advertisers. The fact that the business was paid to provide advertising services does not transform every incident of misconduct by the business into a wrongful act "committed . . . in the course of performing Professional Services." It is not plausible that the insured would

agree to the narrow definition of "professional services" in this Section with the expectation that all wrongful acts relating to the operation of Tagged.com would be covered under this clause.

This insuring clause unambiguously extends only to those claims arising from Tagged's provision of advertising services to others for a fee. Accordingly, there was no potentiality for coverage under the Policy's TMP Section.[3]

B.

Tagged also contends that the coverage provided by the Policy's D&O Section applies to the OAG's claim. Scottsdale acknowledges that the alleged violations of New York Executive Law section 63(12) and General Business Law sections 349 and 350 constitute potential "Wrongful Acts" under this Section, but it argues that the claim is nonetheless excluded from coverage because it involved Tagged "rendering or failing to render professional services."

The Policy does not define the term "professional services" for purposes of the D&O Section.[4] California courts have had the opportunity to construe this term in other insurance-coverage disputes, however. In *Tradewinds Escrow, Inc. v. Truck Insurance Exchange*, 97 Cal. App. 4th 704, 118 Cal. Rptr. 2d 561 (Ct. App. 2002), the California Court of Appeals stated, "'Professional services' are defined as those 'arising out of a vocation, calling, occupation, or

---

[3] Even if the claim was covered under the insuring clause, it would be excluded from coverage pursuant to the Sexual Harassment Endorsement. This provision eliminates coverage of any claim "in any way involving any sexual action." (Policy, Endorsement No. 32.) As all of the OAG's allegations involved inappropriate sexual language, images, or contact, its claim would fall within this exclusion. Moreover, the breadth of the exclusion's plain language—addressing "any sexual action"—may not be disregarded as a result of its heading, "Sexual Harassment Endorsement." *See Res. Bank v. Progressive Cas. Ins. Co.*, 503 F. Supp.2d 789, 794 (E.D. Va. 2007); *Cross Petroleum v. United States*, 51 Fed. Cl. 549, 555 (Fed. Cl. 2002). Because I conclude that there is no coverage under the TMP Section as an initial matter and that the sexual harassment exclusion applies, I need not consider whether the claim would also be excluded from coverage by the media marketing or privacy provisions.

[4] The definition of "professional services" provided in Endorsement No. 27 applies only to the TMP Section.

employment involving specialized knowledge, labor, or skill, and the labor or skill involved is predominantly mental or intellectual, rather than physical or manual.'" *Id.* at 713 (quoting *Hollingsworth v. Commercial Union Ins. Co.*, 208 Cal. App. 3d 800, 806, 256 Cal. Rptr. 357 (Ct. App. 1989)); *see also Food Pro Int'l*, 89 Cal. Rptr. 3d at 9. Thus, in this context, "profession" does not refer solely "to those so-called learned professions," such as medicine, law, or engineering. *Hollingsworth*, 208 Cal. App. 3d at 807 (internal quotation marks and citations omitted). Rather, the term "professional services" in an insurance contract "generally signifies an activity done for remuneration as distinguished from a mere pastime." *Id.*

In *Hollingsworth*, the court further emphasized that, in determining whether an action constitutes a "professional service," it must be viewed in context. *See id.* at 806 ("[A]n insured's claim of coverage for 'professional services' must be evaluated in light of all the relevant circumstances in which that claim arises, including, but not limited to, the term's commonly understood meaning, the type and cost of the policy, and the nature of the enterprise."). The court in that case, which involved the interpretation of the general liability policy of a cosmetics business, found ear piercing constituted a professional service "as distinguished from an activity incidentally related to [the business's] everyday operations." *See id.* at 808–09. It reached this result even though the business did not specifically charge for ear piercing because the service was not "performed gratis," but was used to "attract[] prospective purchasers." *Id.* at 809. In addition, a service may be "professional" even though delegated to an administrative or clerical employee. In *Northern Insurance Co. of New York v. Superior Court*, 91 Cal. App. 3d 541, 154 Cal. Rptr. 198 (Ct. App. 1979), for instance, a professional services exclusion barred coverage for a claim arising where, as a result his clerical staff's mistake, a physician performed an abortion on the wrong patient. *Id.* at 543. Because it was the physician's "professional duty to

correctly identify a surgical patient," the delegation of this duty to his staff did not "alter [its] professional nature." *Id.* at 544.

Tagged argues that the broad definition of "professional services" provided by these prior cases is inapplicable in the present action because they concerned general liability policies, whereas the present dispute involves a narrower director, officer, and company coverage section. In support of this contention, Tagged cites an unpublished case from the United States District Court for the District of Hawaii, *Federal Insurance Co. v. Hawaii Electric Industries, Inc.*, CIV. NO. 94-00125 HG, 1997 U.S. Dist. LEXIS 24129 (D. Haw. Dec. 23, 1997), applying Hawaii law. There, the court found that "a broad reading of a professional services exclusion in a D&O policy would vitiate most of the coverage provided by such a policy." *Id.* at *32–33. It therefore concluded the professional services exclusion only applied to claims against the insured, an insurance company, that "[arose] out of the rendering of or failure to render professional insurance services to actual or potential . . . policyholders and clients." *Id.* at *41.

Tagged is correct that the type of insurance policy may be relevant to the contours of its professional services exclusion. *See Hollingsworth*, 208 Cal. App. 3d at 806. Here, the exclusion should not be read so as to vitiate the coverage provided by the D&O Section. *See Food Pro Int'l*, 89 Cal. Rptr. 3d at 13–14. The United States District Court for the Northern District of California, however, has previously held that a professional services exclusion—similar to that in the instant contract—in a directors and officers coverage section of a policy, though "appl[ying] broadly," did not render that section's coverage illusory under California law because "[i]n order for a policy to be deemed illusory, it must afford no coverage whatsoever." *Young v. Ill. Union Ins. Co.*, No. C07-05711 SBA, 2008 WL 5234052, at *1 (N.D. Cal. Dec. 15, 2008), *aff'd*, 366 F. App'x 777 (9th Cir. 2010) (citing *Scottsdale Ins. Co. v. Essex Ins. Co.*, 98

Cal. App. 4th 86, 94–95, 119 Cal. Rptr. 2d 62 (Ct. App. 2002)). Furthermore, the professional services exclusion here, like that at issue in *Young*, may be distinguished from the provision discussed in *Hawaii Electric* because the latter exclusion listed examples of the insured's professional services, allowing the court to apply the canon of *ejusdem generis* to determine the narrower definition of professional services intended by the parties to that contract. *See Haw. Elec.*, 1997 U.S. Dist. LEXIS 24129 at *37–41. Here, in contrast, the use of the term "professional services," without elaboration, demonstrates the parties intended to adopt the broader definition elucidated in prior California case law. Moreover, here, as noted in Scottsdale's Reply Memorandum, the professional services exclusion exempts claims brought by a plaintiff in her capacity as a security holder. (Policy, Endorsement No. 28.) Thus, coverage under this Section remains intact for a significant class of claims despite the exclusion.[5] In sum, as in *Young*, I find that the professional services exclusion, interpreted in accordance with prior California cases, does not render the coverage provided by the D&O Section illusory.

Against this background, it is clear that the OAG's claim falls within the professional services exclusion. Tagged, as the operator of a website, provides professional services in determining and regulating the content of that site because this activity is not merely incidental to the site's everyday operations. In addition, the identification of such content is intellectual and mental—rather than physical or manual—work, so the nature of the service is professional. *Northern Insurance Co.* therefore dictates it is not relevant that Tagged management opted to outsource the task of reviewing Tagged.com for inappropriate content to unskilled workers. Moreover, while unskilled workers were assigned the duty of removing inappropriate content,

[5] Although another exclusion in the D&O Section bars coverage of some securities claims, it applies only to claims involving or subsequent to an initial public offering ("IPO"). (Policy, D&O Section, § C.1.n; Policy, Endorsement No. 20.) Consequently, coverage remains, at minimum, for claims related to securities sales occurring prior to an IPO.

Tagged management made the determination to advertise its efforts to protect minor users from this content and made statements regarding the relative safety of using Tagged.com. It was these statements—not merely the presence of certain website content—that the OAG's office claimed violated New York law, and decisions regarding advertising tactics clearly constitute professional services.[6] Finally, although Tagged.com users did not specifically pay the company for the service, Tagged discussed its measures to remove inappropriate content in advertisements in order to attract users to its site and, ultimately, to increase its revenues. Thus, under *Hollingsworth*, it should be considered an activity done for remuneration and a professional service. The OAG's claim could not potentially fall outside of the professional services exclusion. As such, Scottsdale had no duty to defend or indemnify Tagged under the D&O Section.

For the foregoing reasons, the Defendant's Motion will be granted. A separate Order will be entered herewith.

May 27, 2011
Date

/s/
J. Frederick Motz
United States District Judge

[6] It should be noted that, while this violation involved advertising, it did not fall within the TMP Section's definition of professional services because the allegedly false and misleading statements were made when Tagged was advertising *its own* services. In contrast, in order to fall within the definition of professional services for purposes of the TMP Section, the advertising must be provided "for others, for a fee." (Policy, Endorsement No. 27.) As a result, it is not incongruous to conclude that the TMP Section fails to provide coverage at the same time the professional services exclusion bars coverage under the D&O Section.