Looking for IP Coverage: What's In or Out for CGL, Excess & Specialty Policies?

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I. Introduction

"An insurance company's duty to defend intellectual property claims under the rubric of 'advertising injury' is the subject of countless lawsuits – indeed a recent litigation explosion – throughout the country." *State Farm Fire and Casualty Co. v. Steinberg*, 393 F.3d 1226 (11th Cir. 2004), *quoting Winklevoss Consultants, Inc. v. Federal Insurance Co*., 991 F. Supp. 1024, 1026 (N.D. Ill. 1998). Insurers and policyholders have continued to litigate coverage under general liability policies for the growing number of intellectual property claims. The numerous court decisions have created an ever-changing area of insurance law that insurance practitioners must frequently monitor.

The proliferation of IP-related risks has prompted some US and foreign market insurers to revise their CGL policies to limit coverage for many IP claims. Some now contain broad IP exclusions. This paper will also address this recent trend, what is standard in the insurance market today and potential for coverage in policies underwritten in Canadian and other foreign markets. Further, IP-specific specialty policies, which vary widely, are now available to address a broader array of IP-related risks than those covered by modern CGL policies, including infringement liability policies and abatement or enforcement coverage.

II. The CGL Policy – Personal and Advertising Injury

A. In General

United States courts generally recognize that in order for there to be a covered advertising injury, a claim must contain these elements: (1) an injury arising out of an enumerated advertising offense; (2) which was committed during the policy period; (3) and which injury occurred "in the course of," i.e., was causally connected to the named insured's advertising activities; and (4) claimed damages. *See e.g. New Hampshire Ins. Co. v. R.L. Chaides Const. Co.*, 847 F. Supp. 1452, 1455 (N.D. Cal. 1994); *National Union Fire Ins. Co. v. Siliconix, Inc.*, 729 F. Supp. 77 (N.D. Cal. 1989).

In Canada*,* In *Reform Party of Canada v. Western Union Insurance Co.*, 2001 BCCA 274 [*Reform Party*]. the BC Court of Appeal, in the context of determining PAI coverage in a CGL insuring agreement, referred to an article summarizing the historical US roots of PAI coverage and the relevance of US case law:

> The Reform Party requested insurance coverage for advertising liability and the insurer responded by providing them with a commercial general liability policy containing the most commonly used advertising injury provision. Steve Winder in an article entitled "Insurance Coverage for Intellectual Property Claims: Understanding "Advertising Injury" Provisions in Liability Policies", [1998] 12 I.P.J. 127 at 129-130 traces the history of this provision… developed in the United States by the Insurance Services Offices ("ISO") and subsequently adopted by the Insurance Bureau of Canada ("IBC"). Before 1986, the provision was normally inserted into U.S. policies as a "broad form endorsement." Since 1986, the ISO has incorporated advertising injury coverage into the main body of the

> policy, as did the [Canadian] insurer in the policy we are considering. Given that the standard form provision under consideration is the same as its American counterpart, American jurisprudence on the scope of coverage afforded to this advertising injury provision is helpful.

Ibid at para 17.

B. Advertisement and Advertising Activities

Most IP-related coverage disputes under CGL policies involve advertising-related offenses or exclusions. The newer CGL forms define an "advertisement," while some manuscripts forms and the older version of the CGL forms do not. The standard definition provides:

> "Advertisement" means a notice that is broadcast or published to the general public or specific market segments about your goods, products or services for the purpose of attracting customers or supporters. For the purposes of this definition:
>
> **a.** Notices that are published include material placed on the Internet or on similar electronic means of communication; and
>
> **b.** Regarding web sites, only that part of a web site that is about your goods, products or services for the purposes of attracting customers or supporters is considered an advertisement.

For those policies that do not define advertisement, courts look to a variety of sources. Black's Law Dictionary defines the verb "advertise" as follows:

> To advise, announce, apprise, command, give notice of, inform, make known, publish. To call a matter to the public attention by any means whatsoever. Any oral, written, or graphic statement made by the seller in any manner in connection with the solicitation of business and includes, without limitation because of enumeration, statements and representations made in a newspaper or other publication or on radio or television or contained in any notice, handbill, sign, catalog or letter or printed on or contained in any tag or label attached or accompanying any merchandise.

Black's Law Dictionary (5th ed. 1979). When applying this definition to material that is not disseminated to the public through print or broadcast media, but rather is merely posted the Internet via a social networking page, courts have, for the most part, applied the same test as that applied to distribution via traditional media (i.e., defining advertising as "the widespread distribution of promotional material to the public at large"). *Amazon.com International, Inc. v. American Dynasty Surplus Lines Ins. Co*., 85 P.3d 974, 977 (Wash. Ct. App. 2004).

In *Teletronics International, Inc. v. CNA Insurance Co.*, 120 Fed. Appx. 440 (4th Cir. 2005). a manufacturer and seller of radio amplifiers posted a user manual on its website that was nearly identical to the copyrighted manual of its competitor. The court held that posting the infringing manual on its website constituted advertising because the defendant admitted that it employed the user manual to promote the sale of its amplifiers, and because by posting the manual on its website, it distributed the document to a large number of potential customers, i.e. engaging in widespread distribution of promotional material to the public at large. In contrast, in *Rombe Corp. v. Allied Insurance Co.*, 27 Cal. Rptr. 3d 99 (Cal. Ct. App. 2005), the court held that an insured's e-mail newsletter to clients of its direct competitor did not constitute advertising activity because it was more in the form of targeted solicitation rather than widespread distribution to the public at large. *Id* at 104-05. *See also Toffler Assoc. Inc. v. Hartford Fire Ins. Co.*, 651 F. Supp. 2d 332 (E.D. Pa. 2009).

In addition, when looking at the coverage grant/enumerated offenses, set forth below, courts generally require that the injury allegedly caused by the enumerated offense must have occurred "in the course of" the insured's "advertising activities". In other words, coverage exists for advertising injury only if the allegations satisfy the definition of advertising injury and there is a causal connection between the allegations and the insured's advertising activities. *Amazon.com International,* 85 P.3d at 976.

The "caused by an offense" connection is required to limit the coverage to injuries that are the result of the specific enumerated offenses. A careful examination of the facts is required to determine: (1) if there was any advertising, and (2) if the offense occurred in the course of that advertising. In *Hyundai Motor America v. National Union Fire Insurance Co.*, 600 F.3d 1092 (9th Cir. 2010), Hyundai was sued by a third party for patent infringement arising out of an interactive feature of Hyundai's website that allowed the user to build their own vehicle. The plaintiff in the underlying action alleged that it held a patent on the method of generating customizations for potential customers of an automobile dealer. Hyundai sought coverage under the advertising injury provision of its policy with National Fire, who filed a declaratory judgment action. *Id.* at 1096. The court held that the website feature constituted an advertising activity because, even though it created customized proposals for individual users, one at a time, since the feature was on the Internet, it was available to an unlimited amount of potential customers. The court also found that there was a "causal connection" between the advertisement and the injury because Hyundai's use of the website feature, i.e. the advertisement, was itself the patent infringement about which the third party complained.

In *Crum & Forster Specialty Ins. Co. v. Willowood USA, LLC et al.,* 696 Fed. Appx. 276 (9th Cir. August 17, 2017), the insured, Willowood, settled claims against it for trademark infringement and unauthorized use of a trademark. Willowood then sought defense and indemnity under its CGL policies that covered advertising injury "arising out of . . . the use of another's advertising idea in your 'advertisement.'" The Ninth Circuit held that "arising out of" is interpreted broadly, thus, the insured's use of the trademark satisfied the causal element.

In the governing Canadian case on this issue, the BC Court of Appeal analyzed the required nexus between the alleged injury and the policyholder's advertising injury for the purposes of a PAI coverage grant. See *Grayson v. Wellington Insurance Co*., 1997 CanLII 4112 (BC CA), leave to app ref'd [1997] S.C.C.A. No. 487 [*Grayson*]. Based in part on US case law, the Court concluded that the mere fact a product, manufactured in breach of a patent or copyright, was advertised would not necessarily bring the injury or infringement within the PAI coverage grant. *Ibid* at para 24. Instead, a sufficient causal link must be established by show the underlying plaintiff either alleged the plaintiff has suffered injury "as a result of" the policyholder's advertising activities or sought a remedy which would stop the policyholder's advertising activities from continuing. *Ibid*. Most recently affirmed by *Blue Mountain*, (BCCA) above at paras 40 (Confirming status as leading case on issue) and 53-54 (Applying *Grayson* causal link test). Careful attention must be given to the pleaded facts to determine whether such allegations or remedies are specifically raised or could be inferred. See *PrairieFyre Software Inc. v. St. Paul Fire and Marine Insurance Co.*, [2003] O.J. No. 3116 (SC) aff'd [2004] O.J. No. 2555 (CA) at para 24 (Concluding no duty to defend under "2000 policy" given no allegations supported direct causal link between the advertising and the offence alleged). See also *Halifax Insurance Co. of Canada v. Innopex Ltd.*, [2004] O.J. No. 4178 (CA) at para 44 (Inferring trademark infringement occurred "in the course of" advertising for duty to defend purposes given allegations of infringement. Court concluded infringement occurs once policyholder promotes the products to customers, satisfying coverage grant).

C. Enumerated Offenses

The modern CGL form defines person and advertising injury as follows:

> "Personal and advertising injury" means injury, including consequential "bodily injury", arising out of one or more of the following offenses:
>
> **a.** False arrest, detention or imprisonment;
>
> **b.** Malicious prosecution;
>
> **c.** The wrongful eviction from, wrongful entry into, or invasion of the right of private occupancy of a room, dwelling or premises that a person occupies, committed by or on behalf of its owner, landlord or lessor;
>
> **d.** Oral or written publication, in any manner, of material that slanders or libels a person or organization or disparages a person's or organization's goods, products or services;
>
> **e.** Oral or written publication, in any manner, of material that violates a person's right of privacy;
>
> **f.** The use of another's advertising idea in your "advertisement"; or
>
> **g.** Infringing upon another's copyright, trade dress or slogan in your "advertisement".

The initial inquiry in the advertising injury coverage analysis is whether the complained-of act falls within one of the enumerated offenses covered by the applicable policy. If the policyholder's alleged actions do not fall within one of the described types of conduct, there is no coverage. Several of these offenses will be discussed below.

1. Disparagement

One of the offenses that have seen many recent interpretive court decisions is coverage for liability arising from the publication of material that "disparages a person's or organization's goods, products or services." Thus, whether a claimant is asserting a claim of disparagement against an insured is the crux of the coverage issue.

On June 12, 2014, the California Supreme Court issued its decision in the closely watched case of *Hartford Casualty Insurance v. Swift Distribution, Inc.*, 59 Cal. 4th 277, 326 P.3d 253, 172 Cal. Rptr. 3d 653 (Jun. 12, 2014). The Court affirmed the Court of Appeals ruling that an insurer did not have a duty to defend its insured against allegations that it had infringed a competitor's trademark and patents by producing and selling a similar looking music equipment cart with a very similar name ("Multi-Cart" vs. "Ulti-Cart"). *Id*. The insured argued that there was a potential for covered damages, and hence a duty to defend, because the underlying complaint alleged facts supporting a claim of implied disparagement, and its general liability policy covered damages because of the publication of material that "disparages a person's or organization's goods, products or services." The Court found no potential for liability based on disparagement, either express or implied, reasoning that the insured was not alleged to have identified the competitor or its product, or to have "necessarily referred to and derogated" the claimant's product.

In ruling against the insured, the Court clarified the circumstances under which one may be found to have impliedly disparaged a competitor or its goods, products or services. The Court held that allegations that the insured had infringed a competitor's trademark and patents and engaged in unfair competition by producing and selling a similar looking music equipment cart with a very similar name ("Multi-Cart" vs. "Ulti-Cart") did not support a claim of disparagement. The court found no potential for liability based on disparagement, either express or implied, reasoning that the insured was not alleged to have identified the competitor or its product, or to have suggested that the insured's product was superior to that of the competitor. *Id*. In short, this decision was about the facts a plaintiff must allege to support a claim of disparagement. The case is highly relevant to insurance practitioners because many times IP and unfair competition lawsuits involve facts that suggest the possibility of disparagement

The Fifth Circuit in *Uretek USA, Inc. v Continental Casualty Co*., 701 Fed. Appx. 343 (5th Cir. July 28, 2017), overturned the trial court and afforded the insured coverage under its CGL policy. Uretek sued its competitor for patent infringement and the competitor asserted a counterclaim against Uretek claiming misrepresentation to customers regarding the competitors ability to work on various projects without infringing Uretek's patent. The Fifth Circuit focused its analysis on the definition of "disparage" and held that a statement about a competitor's ability or inability to take on work disparages that competitor and the services it offers.

2. Unfair Competition

The 1976 and 1981 advertising injury provisions expressly included coverage for "unfair competition." Coverage for "unfair competition" in these early provisions was intended to be limited to the common law tort of that name, which traditionally involved the "passing off" of one's product as that of another, and a few early opinions established corresponding boundaries on "unfair competition." For example, in, *Ruder & Finn v. Seaboard Surety Co*., 422 N.E.2d 518, 522, 52 N.Y. 2d 663 (1981), cited in *Granite State v. Aamco*, 57 F.3d 316, 320 (3d Cir. 1995), held that, viewed most broadly, "the primary concern in unfair competition is the protection of a business from another's misappropriation of the business' organization or its expenditure of labor, skill and money."

Some courts adopted a more restrictive meaning of the term, holding that unfair competition includes only the common law tort of "passing off." *See, e.g., Smartfood Inc. v. Northbrook Prop. and Cas. Co.,* 35 Mass.App.Ct. 239, 618 N.E.2d 1365 (Mass.App.Ct. 1993) (unfair competition did not cover breach of contract action because at common law it means passing off and policy does not refer to unfair business practice statute); *Sachs v. Industrial Indem. Ins. Co.*, 1993 WL 93562 (C.D. Cal. 1993) (objectively reasonable person would understand "unfair competition" to mean passing off)

Unfair competition is not included in the more modern versions of the CGL policy. Nevertheless, claims of unfair competition are frequently asserted in relation to other IP-specific claims, thus it becomes important to define the context and parameters of such a claim to then determine whether it may fit within an enumerated offense under the policy.

In many states, a claim for unfair competition is now codified. For example, in California, there is a statutory claims for Unfair Competition in Violation of Cal. Bus. & Prof. Code § 17200, which defines unfair competition as "any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising and any act prohibited by Chapter 1 (commencing with Section 17500) of Part 3 of Division 7 of the Business and Professions Code." Cal Bus & Prof Code § 17200. This claim could allege "personal and advertising injury" under Cal. Bus. & Prof. Code § 17200 by asserting that an insured committed unlawful, unfair, and fraudulent business practices, and engaged in unfair, deceptive, untrue, or misleading advertising. In other words, such a cause of action could fall within the definition of "personal and advertising injury" that includes "written publication, in any manner, of material that slanders or libels a person or organization or disparages a person's or organization's good, products or services."

As with some US jurisdictions, Canadian common law claims alleging unfair business practices were largely limited to the tort of "passing off". *See 599960 Ontario Inc. v. Taylor Steel Inc*., 2000 CanLII 22664 (ONSC) at para 19 ("Passing off is a form of misrepresentation by a trader concerning another trader's business and made to customers of that other trade to lure those customers into falsely believing they are trading with their former trader"). The tort of passing off is one of the oldest remedies in the realm of unfair competition, and stands distinct from a statutory action. *Sharp Electronics of Canada Ltd. v. Continental Electronic Info. Inc*., 1988 CanLII 3340 (BC SC) [*Sharp Electronics*].The Supreme Court of Canada discussed the history of the tort of "passing off" and its development in Canadian law in the decision of *Kirkbi AG v. Ritvik Holdings Inc*., 2005 SCC 65. stating:

> This tort has a long history. At a very early point in its development, the common law became concerned with the honesty and fairness of competition. For that reason, it sought to ensure that buyers knew what they were purchasing and from whom. It also sought to protect the interest of traders in their names and reputation. As far back as the 17th century, the courts started to intervene. Actions based at first on some form of deceit were allowed. The modern doctrine of passing off was built on these foundations and became a part of Canadian law. Its principles now inform both statute law and common law.

Ibid at para 63. Courts have acknowledged the tort has expanded "to take into account the changing commercial realities in the present-day community". *Atkinson & Yates Boatbuilders Ltd. v. Hanlon*, 2003 NLSCTD 113 (CanLII) at paras 75-76. See also *Sharp Electronics*, (BCSC). This area has now expanded such that it no longer addresses solely one trader deceitfully selling its goods as those of another, but now encompasses protecting the community from the consequential damage of unfair competition or unfair trading. *Sharp Electronics*, (BCSC) above at para 9.

An examination of the development of the common law of "unfair competition" in Canada indicates the sphere of business torts have grown over time, and with this the purpose for the court's involvement has shifted as well. The number of business torts has increased, thereby increasing the number of practices that may constitute "unfair competition". In addition, where the focus of the tort was at one time protecting competitors, it now seems to be protecting the consuming public at large. As stated by one Ontario trial court, "in recent years, Ontario tort law has become a major factor when examining the affairs of the free market place." *Bass Clef Entertainments Ltd. v. Hob Concerts Canada Ltd*., 2007 CanLII 17186 (ON SC) at para 62 [*Bass Clef*].

3. Canadian Business Torts and PAI Coverage

There is a group of torts in Canada, referred to as economic or business torts, dealing with the intentional interference with economic interests. The business torts can be divided into two categories. Firstly, those dealing with deceptive market practices such as deceit, injurious falsehood, passing-off, and misappropriation of personality. *Ibid* at para 118 (Citing chapter 4 of <u>The Law of Torts</u>, Phillip Osborne, 2nd ed., Irwin Law: 2003). Traditionally these practices have been recognized by the Canadian common law as being wrongful and requiring some form of action. However, there has also been the development of an "amorphous group that deals with improper market practices". *Ibid*. This group includes conspiracy, intimidation, inducement to breach a contract, and a general tort of intentional interference with economic interest by unlawful means. These torts focus on the illegitimacy of combined coercion, competition by unlawful means, and the deliberate interference with contractual rights. *Ibid*.

In addition to the common law business tort, an unfair competition claim can be brought in Canada pursuant to the federally enacted *Competition Act*. R.S.C., 1985, c. C-34, as amended [*Act*]. Part VI of the *Act* ("Offences in Relation to Competition") lists and prohibits certain anticompetitive conduct harming competitors and/or consumers, such as misleading advertising (s. 52). See generally the unfair competitive practices at *ibid*, ss. 45-62. The *Act* provides a statutory cause of cause of action (s. 36), allowing “any person” suffering loss or damage “as a result of” conduct contrary to a Part VI provision to sue for damages.

The recent *Blue Mountain Log Sales Ltd. v. Lloyd’s Underwriters,* 2019 BCCA 240 [*Blue Mountain*]. BC Court of Appeal decision involved a CGL “advertising liability” claim for unfair competition. In the underlying US action, the plaintiffs sued for the misappropriation of trade secrets and unfair competition with respect to the policyholders’ manufacturing of a fire retardant product. The underlying plaintiffs eventually amended their pleading to only include one cause of action: misappropriation of trade secrets and confidential information in breach of the Washington *Uniform Trade Secrets Act*. Chapter 19.108 RCW. The BC Court of Appeal, agreeing with the trial judge’s decision, concluded the pleading alleged a claim for unfair competition within the PAI coverage grant based on the *UTSA* cause of action. See *Blue Mountain*, (BCCA) above at para 59 (Concluding trial judge entitled to rely on Washington law expert witness evidence that while *UTSU* displaced common law unfair competition tort, statutory claim for misappropriation of trade secrets was codified species of unfair competition). The Court of Appeal concluded the trial judge made no error in analysis, noting the CGL definitions of “advertising liability” and “advertising injury” were broad and referred to forms of conduct rather than “technical elements or legal labels that may apply to particular causes of actions in particular jurisdictions.” *Ibid*.

D. Damages

Because general liability policies only insure against damages that the insured becomes legally obligated to pay, courts have also carefully examined the complaint to determine whether the requested monetary relief is “damages.” Because the intellectual property subject matter tends to give rise to claims for injunctive relief, some cases may not be covered for the lack of a covered damage claim. Although it seems unlikely that there would not be a prayer for damages, in at least one case coverage was denied for this reason. *Feed Store v. Reliance Ins. Co.*, 774 S.W.2d 73 (Tex. App. 1989).

Additionally, claims under state unfair trade practices acts brought by attorney general typically do not request damages. In *Bank of the West v. Superior Court*, 2 Cal.4th 1254 (1992), the statute allowed for restitution, not actual damages. The court, again referring to the common law tort of “passing off,” found that actual damages were an element of that tort, therefore the relief requested by the consumers was not within the coverage. Similarly, courts reviewing cases brought by state agencies under such acts have found that there is no coverage for the statutory damage awards. *Seaboard Sur. Co. v. Ralph Williams’ Northwest Chrysler Plymouth, Inc.*, 81 Wash.2d 740, 742-3, 504 P.2d 1139 (1973) (Attorney General’s action for injunction under RCW 19.86.080 is not one for unfair trade practice because the State is not seeking “damages” and there is no allegation of harm to a competitor).

In *American Employers Insurance Co. v. DeLorme Publishing Co., Inc.*, 39 F.Supp.2d 64 (D. Me. 1999), the underlying complaint sought a permanent injunction, an equitable accounting by the insured of all its profits, advantages obtained by its sale of the alleged infringing item, costs and attorneys' fees, and contained a general request for "other and further relief as the Court deems just and proper." The court rejected the insurer's argument that it had no duty to defend because the underlying complaint did not seek money damages. Adopting the reasoning of the Eleventh Circuit's decision in *Limelight Productions, Inc. v. Limelite Studios, Inc.,* the court held that the Lanham Act allows recovery of ill-gotten profits as a form of damages because of the unavailability of proof in such cases. The court further reasoned that because the underlying complaint did not seek compensation for lost sales, it was possible that the accounting for lost profits would equal compensation for lost sales.

The court also held that the underlying complaint sought "damages" because of the general request for "other and further relief as the Court deems just and proper." As the Lanham Act permits recovery of compensatory damages, if the claimant proved it was entitled to equitable relief, it also could have received money damages. Therefore, the court held that a request for an accounting of lost profits under the Lanham Act is a request for damages. Ultimately, however, the court held that there was no duty to defend based on an exclusion to coverage.

In the Canadian decision of *Mead Johnson Canada v. Ross Pediatrics*, [1996] O.J. No. 3869 (Gen. Div.), the court states that although the *Competition Act* remedy for unfair competition appears to have been limited to damages, recent decisions by the Supreme Court of Canada call for a broader application of the injunctive power of courts in such cases. *Ibid* at para 30.

E. Exclusions

Some of the typical PAI coverage exclusions include the following:

2. Exclusions

This insurance does not apply to:

a. "Personal and advertising injury":

(1) Knowing Violation Of Rights Of Another

Caused by or at the direction of the insured with the knowledge that the act would violate the rights of another and would inflict "personal and advertising injury".

(2) Material Published With Knowledge Of Falsity

Arising out of oral or written publication, in any manner, of material, if done by or at the direction of the insured with knowledge of its falsity.

(3) Material Published Prior To Policy Period

Arising out of oral or written publication, in any manner, of material whose first publication took place before the beginning of the policy period.

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(7) Quality Or Performance Of Goods – Failure To Conform To Statements Material Published Prior To Policy Period

Arising out of the failure of goods, products or services to conform with any statement of quality or performance made in your "advertisement".

(8) Wrong Description Of Prices

Arising out of the wrong description of the price of goods, products or services stated in your "advertisement".

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(10) Insureds In Media And Internet Type Businesses

Committed by an insured whose business is:

(a) Advertising, broadcasting, publishing or telecasting;

(b) Designing or determining content of web sites for others; or

(c) An Internet search, access, content or service provider.

However, this exclusion does not apply to Paragraphs **14.a., b.** and **c.** of "personal and advertising injury" under the Definitions section.

For the purposes of this exclusion, the placing of frames, borders or links, or advertising, for you or others anywhere on the Internet, is not by itself, considered the business of advertising, broadcasting, publishing or telecasting.

(11) Electronic Chatrooms Or Bulletin Boards

Arising out of an electronic chatroom or bulletin board the insured hosts, owns, or over which the insured exercises control.

(12) Unauthorized Use Of Another's Name Or Product

Arising out of the unauthorized use of another's name or product in your e-mail address, domain name or metatag, or any other similar tactics to mislead another's potential customers.

* * *

In advertising injury disputes, courts generally adhere to the maxim that exclusions should be interpreted narrowly so that coverage is not unduly restricted. *See, e.g., Harleysville Mut. Ins. Co. v. Buzz Off Insect Shield, L.L.C.,* 692 S.E.2d 605, 612 (N.C. 2010) ("[W]e strictly construe against an insurance company those provisions excluding coverage under an insurance policy."); *JAR Laboratories LLC v. Great Am. E&S Ins. Co*., No. 12 C 7134, 2013 WL 1966386, at *7 (N.D. Ill. May 10, 2013)("[P]rovisions limiting or excluding coverage 'are . . . construed liberally in favor of the insured and against the insurer.'"); We*stfield Ins. Co. v. Robinson Outdoors, In*c., 700 F.3d 1172, 1175 (8th Cir. 2012) ("Insurance contract exclusions are construed strictly . . . and narrowly against the insurer."); B*ridge Metal Indus., L.L.C. v. Travelers Indem. Co*., 812 F. Supp. 2d 527, 542-43 (S.D.N.Y. 2011) ("An insurer must establish that the exclusion is stated in clear and unmistakable language, is subject to no other reasonable interpretation, and applies in the particular case.”);

1. Knowing Violation of Another’s Rights

California law is clear that this exclusion does not apply merely to “unproved and disputed allegations” and therefore even though this exclusion may affect a carrier’s liability for indemnification, it does not affect a carrier’s duty to defend. *KM Strategic Mgmt., LLC v. Am. Cas. Co. of Reading, PA*, 156 F. Supp. 3d 1154, 1170 (C.D. Cal. 2015). The *KM Strategic* court explained that even though intentional conduct is alleged, there is “usually at least a possibility of coverage because…the insured’s conduct may be shown to have been merely reckless or negligent.” 156 F. Supp. 3d at 1170; see *Mesa Underwriters Specialty Ins. Co. v. Blackboard Ins. Specialty Co*., 400 F. Supp. 3d 928, 941–42 (N.D. Cal. 2019) (relying in part on KM Strategic to hold that the knowing-violation exclusion did not preclude coverage for allegedly intentional habitability issues that could have arisen from negligent conduct)

2. Failure to Conform

Coverage B’s Personal and Advertising Injury Liability coverage for injury arising out of a publication that libels a person or disparages a person’s or organization’s goods, products or services is intended to address the insured’s statements about another person or entity or its goods or services. This intent is reinforced by the “Quality or Performance of Goods – Failure to Conform to Statements” exclusion, commonly referred to as the Failure to Conform exclusion.

At its most basic level, the Failure to Conform exclusion “envisions a scenario in which the plaintiff shows that the insured’s product is, in reality, something different from what the insured has advertised. . . . Thus, the exclusion removes from coverage ‘personal and advertising injury’ proximately caused by a false statement an insured has made about its own product.” *See Harleysville Mut. Ins. Co. v. Buzz Off Insect Shield, L.L.C.*, 692 S.E.2d 605, 613 (N.C. 2010).

Some courts analyzing whether the Failure to Conform exclusion applies to a particular claim have addressed whether the exclusion applies only to false advertising claims asserted by consumers of the insured’s goods, products or services or whether the exclusion also applies to claims asserted by the insured’s competitors. *See, e.g., Harleysville Mut. Ins. Co. v. Buzz Off Insect Shield, Inc., 692 S.E.2d 605, 609 (N.C. 2010); Skylink Techs., Inc. v. Assurance Co. of America*, 400 F.3d 982, 983 (7th Cir. 2005); *Dollar Phone Corp. v. St. Paul Fire and Marine Ins. Co.*, 514 Fed. Appx. 21, 22 (2d Cir. 2013); *Jarrow Formulas, Inc. v. Steadfast Ins. Co.*, No. 2:10-CV-810-JST, 2011 WL 1399805, at *5 (C.D. Cal. April 12, 2011); *Superformance Int’l Inc. v. Hartford Cas. Ins. Co.*, 203 F. Supp. 2d 587, 589-90 (E.D. Va. 2002).

The “Failure to Conform” exclusion usually applies when there is a claim alleging that the insured engaged in false advertising by making false statements about the quality of its own goods or services. *See Westfield Ins. Co. v. Robinson Outdoors, Inc.*, 700 F.3d 1172, 1175 (8th Cir. 2012). However, the insured’s statements that expressly disparage another company’s goods, products or services do not fall within the exclusion. *See Dollar Phone*, 2012 WL 1077448, at *10 (finding claim for injury caused by alleged misrepresentations about the insured's products was "precisely the type of harm contemplated by the plain language of the non-conformity exclusion"); *PCB Piezotronics, Inc. v. Kistler Instrument Corp.*, No. 96-CV-0512E(F), 1997 WL 800874, at *3 (W.D.N.Y. Dec. 31, 1997) (excluding coverage for claims that insured misrepresented the nature, characteristics and qualities of its own products). It is less clear when the claim alleges that the insured's statements about its own products or service indirectly disparage the claimant's good or services by implication.

A typical fact pattern in an implied disparagement claim is that the insured's statements about the superior qualities or characteristics of its own product implicitly disparage the claimant's product by making a false comparison. Examples are statements that the insured's product is "the first" or "only" product on the market with a certain characteristic or that the insured's product is "superior to" or "more powerful" or "more advanced" than other products. *See Tria Beauty, Inc. v. Nat'l Fire Ins. Co. of Hartford*, No. C 12-05465 WHA, 2013 WL 2181649, at *3 (N.D. Cal. May 20, 2013); *E. Piphany, Inc. v. St. Paul Fire & Marine Ins. Co.*, 590 F. Supp. 2d 1244, 1253 (N.D. Cal. 2008). Some courts have held that the Failure to Conform exclusion does not apply to implied disparagement claims due to the fact that the claimant's injury does not arise from statements about the insured's own product or that the insured's product does not live up to the advertised qualities. Rather, the injury arises from the negative perception of the claimant's product or service created by implication regardless of the truth or falsity of the statement about the insured's products. *See Tria Beauty, 2013 WL 2181649,* at *4-*6; *JAR Laboratories, LLC v. Great Am. E&S Ins. Co.*, No. 12 C 7134, 2013 WL 1966386, at *5 (N.D. Ill. May 10, 2013) (noting insured's statements that did not refer to claimant by name were clearly directed at the claimant's product and made false comparison between the insured's product and plaintiff's product).

However, in other cases, courts have held that claims of implied disparagement are excluded by the Failure to Conform exclusion. For example, in *Dollar Phone Corp.,* the plaintiff claimed that the insured falsely advertised its phone card product by making false statements about the number of minutes the insured's card provided. The court held that the Failure to Conform exclusion applied because "the failure of [the insured's] products to perform as promised is the entire basis of . . . the plaintiff's alleged injuries [and] the harm to . . . the plaintiff's reputation is premised entirely on the inaccuracy of [the insured's] promises as to the number of minutes their [phone] cards provide." *Dollar Phone Corp. v. St. Paul Fire and Marine Ins. Co.*, No. cv-09-1640, 2012 WL 1077448 at *10 (E.D.N.Y. Mar. 9, 2012), *aff'd* 514 Fed. Appx. 21, 22 (2d Cir. 2013). Although the insured argued that the alleged false statements about the insured's product created a false impression that the plaintiff's products were inferior, the court held that this implied disparagement did not negate the exclusion.

The case of *Harleysville Mutual Ins. Co. v. Buzz Off Insect Shield, L.L.C.*, 692 S.E.2d 605 (N.C. 2010), provides another example of a court rejecting an implied disparagement claim. In this case, the North Carolina Supreme Court rejected the insured's attempt to avoid the Failure to Conform exclusion by characterizing allegations of the underlying claim to include false statements concerning the plaintiff's products. The insured sold clothing with insect repellant incorporated into the fabric. The insured was sued by S.C. Johnson & Son, Inc. ("SCJ"), which sold topical insect repellants. The court evaluated each of the allegations in the underlying claim that the insured contended rendered the exclusion inapplicable.

First, the court addressed statements that the insured's product was "superior in performance to topical insect repellants, such as those containing DEET." The court stated that "the comparison is alleged to be false not because [the insured] made representations that SCJ's products were ineffective, but because [the insured] made allegedly false claims that their products worked as well, if not better than, SCJ's products . . . [a]s such, the alleged falsity of the advertisements arises from the failure of the [insureds'] products to actually perform as well as [the insureds] claim they perform." Next, the court addressed the insured's advertising statements that topical insect repellents were "messy," "nasty" and "a hassle." The court observed that although these statements implied that SCJ's products were a nuisance, SCJ did not allege that these descriptions of its products were false. The court also stated that these statements were opinions that likely were not actionable as a source of injury in the plaintiff's claim. Finally, the court rejected an implied disparagement claim based on the insured's statements that its products were naturally derived. The court concluded that "while SCJ did allege that [the insured's] advertisements portrayed SCJ's products in a negative light, the alleged falsity of that portrayal lies solely in the alleged failure of [the insured's] products to be of the quality and as effective as [the insured] claimed." *Harleysville Mut. Ins. Co. v. Buzz Off Insect Shield, Inc.*, 692 S.E. 2d 605, 621-22 (N.C. 2010). For these reasons, the Failure to Conform exclusion negated coverage.

3. Insureds in Media and Internet Type Businesses

The Policy's Insureds In Media And Internet Type Businesses exclusion specifically precludes coverage for "'personal and advertising injury' committed by an insured whose business is: (1) Advertising, broadcasting, publishing or telecasting; (2) Designing or determining content of web sites for others; or (3) An Internet search, access, content or service provider."
At least one court has held that this exclusion applied to Dish Network ("Dish"), where the carrier sought a declaration from the court that it was not obligated to defend Dish in an underlying case for alleged TCPA violations. *Ace Am. Ins. Co. v. Dish Network, LLC*, 173 F. Supp. 3d 1128, 1130 (D. Colo. 2016). The court explained that the exclusion applied to DISH because "the terms 'broadcasting' and 'telecasting' undoubtedly encompass Dish's transmissions." *Dish Network,* 173 F. Supp. 3d at 1138.

4. Unauthorized Use

The CGL policy's Unauthorized Use Of Another's Name Or Product exclusion specifically precludes coverage for "'personal and advertising injury' arising out of the unauthorized use of another's name or product in your e-mail address, domain name or metatag, or any other similar tactics to mislead another's potential customers."

In a California Court of Appeal case, the court analyzed an insured's appeal from an order sustaining, without leave to amend, the carrier's demurrer for breach of contract and breach of the implied covenant of good faith and fair dealing for the carrier's alleged failure to defend the insured in an underlying complaint for various breaches of a music recording agreement, including the alleged wrongful use of the artist's domain name after expiration of the agreement. *The Oglio Entm't Grp., Inc. v. The Hartford Cas. Ins. Co.*, 200 Cal. App. 4th 573, 575–78 (2011). In holding that the carrier had no duty to defend, the lower court explained that the underlying complaint did not plead facts alleging advertising injury which created a potential for coverage under the policy because, in part, the unauthorized use exclusion applied to preclude coverage for "any advertising injury '[a]rising out of the unauthorized use of another's name or product in your e-mail address, domain name or metatag, or any other similar tactics to mislead another's potential customers.'" *Oglio*, 200 Cal. App. 4th at 580; 583. On appeal, the insured argued the carrier owed a duty to defend based on a number of allegations, but it did not argue that the trial court erred in concluding that the unauthorized use exclusion applied and that there was no duty to defend based on allegations that the insured continued to use the domain name of another to market itself. *Oglio* at 581 n.4. The court of appeal affirmed the lower court's ruling that the carrier owed no duty to defend based on any allegation in the underlying complaint. *Id.* at 586.

In another California case, the court affirmed the lower court's order granting the carrier's motion for summary judgment on the basis that the unauthorized use exclusion unambiguously precluded coverage for allegations that "CollegeSource used AcademyOne's domain name in its own domain name in a way likely to cause confusion in the marketplace." *CollegeSource, Inc. v. Travelers Indem. Co.*, 507 F. App'x 718, 719–20 (9th Cir. 2013). In so holding, the court explained that the allegations fall within the unauthorized use exclusion because the only reasonable reading of the allegations "is that it claims injury from an activity that (1) is 'similar to' the unauthorized use of another's name or product in one's domain name, and (2) would mislead customers." *CollegeSource*, 507 F. App'x at 719–20.

5. Infringement of copyright, patent, trademark or trade secret

Many policies recently issued contain some form of exclusion for certain intellectual property claims. For example, one common exclusion is for injury arising out of infringement of "trademark, trade name, service mark or other designation of origin or authenticity." In *Superperformance International, Inc. v. Hartford Casualty Insurance Co.,* 332 F.3d 215 (4th Cir. 2003), the Fourth Circuit held that this exclusion applied to all trademark infringement claims. In *Native American Arts, Inc. v. Hartford Casualty Insurance Co*., 2004 WL 2065065 (N.D. Ill. Sept. 10, 2004), aff'd, 435 F.3d 729 (7th Cir. 2006), the court held that this exclusion was not restricted to just trademark infringement claims, finding that this exclusion barred coverage for claims of false representation in violation of the Indian Arts and Crafts Act of 1990. However, in *Specific Impulse, Inc. v. Hartford Casualty Insurance Co*., 2002 WL 32052699 (N.D. Cal. Sept. 17, 2002), a California federal court ruled that this exclusion did not apply to copyright infringement claims.

In *Lemko Corp. v. Federal Insurance Co.*, 70 F. Supp. 3d 905 (N.D. Ill. 2014), the policyholder sought coverage under its professional liability policy for alleged theft of copyrighted and confidential material. The intellectual property exclusion, claims "based upon, arising from, or in consequence of any actual or alleged infringement of copyright, patent, trademark, trade name, trade dress, service mark or misappropriation of ideas or trade secrets," was upheld by the Court and the insured was denied coverage.

In *Hartford Fire Ins. Co. v. Vita Craft Corp.*, 911 F. Supp 2d 1164 (D.Kan. 2012), the insurer sought a declaratory judgment that it owed no duty to defend or indemnify its insured under CGL policies for claims of patent infringement and misappropriation of trade secrets. The insurer argued that the intellectual property rights exclusion barred coverage however, the Court disagreed because the underlying complaint alleged that the insured "spread false rumors" and those allegations fell outside of the exclusion. Similarly, in *MedAssets, Inc. v. Federal Insurance Co.*, 705 F. Supp. 2d 1368 (N.D. GA. 2010), the insurer sought a declaratory judgment under a professional liability policy that the insured was barred from coverage under the intellectual property rights exclusion. However, because the complaint characterized the pricing information as both a "trade secret" and "confidential information," the latter of which did not fall into the exclusion, the insured was provided with coverage.

In *Tela Bio, Inc. v. Federal Insurance Co., No*. 18-1717, 2019 WL 211507 (3d Cir. Jan. 16, 2019), the insured, a hernia mesh manufacturer, for a suit alleging the insured misappropriated confidential trade secrets and poached employees from a competitor. The district court denied the insured coverage and Third Circuit upheld. The Third Circuit reasoned that the insurer had no duty to defend because the underlying complaint had no allegations of libel, slander, or any other defamatory conduct causing reputation harm. Further, even if the underlying complaint did allege libel, slander, or defamatory conduct causing reputational harm, the insured would be denied coverage under the Intellectual Property Exclusion.

6. Prior Publication

The Material Published Prior To Policy Period exclusion specifically precludes coverage for "'personal and advertising injury' arising out of oral or written publication, in any manner, of material whose first publication took place before the beginning of the policy period." This exclusion applies to publications that pre-date the policy period, as well as publications during the policy period that are "substantially similar" to any pre-coverage publications. *St. Surfing, Ltd. Liab. Co. v. Great Am. E&S Ins. Co.*, 776 F.3d 603, 605 (9th Cir. 2014); *MGA Entm't, Inc. v. Crum & Forster Specialty Ins. Co.*, No. CV 07-08276-SGL(RNBx), 2009 U.S. Dist. LEXIS 134871, at *7 (C.D. Cal. June 26, 2009).

In *St. Surfing*, the lower court granted summary judgment to the carrier and found no duty to defend an underlying complaint with allegations of trademark infringement, unfair competition, and unfair trade practices arising from the advertising of a skateboard product under a commercial general liability policy. 776 F.3d at 605–07. In affirming summary judgment, the appellate court held that the prior publication exclusion barred coverage because "an allegedly wrongful advertisement published before the coverage period triggers application of the prior publication exclusion" and because "[i]f this threshold showing is made, the exclusion bars coverage of injuries arising out of republication of that advertisement, or any substantially similar advertisement, during the policy period, because such later publications are part of a single, continuing wrong that began before the insurance policy went into effect." *St. Surfing* at 610.

The court continued that "[i]f a later advertisement is not substantially similar to the pre-coverage advertisement, however, it constitutes a distinct, or 'fresh,' wrong that does not fall within the prior publication exclusion's scope." *Id.* The court in *St. Surfing* found that the advertisements Street Surfing published during the coverage period were substantially similar to its pre-coverage advertisements because (1) the underlying complaint did not mention any specific advertisements, but rather made general allegations that the insured used the same name and logo on its product and advertisements; (2) the underlying complaint did not allege that the post-coverage advertisements were separate torts occurring during the policy period; (3) the alleged misappropriated advertising terms arose out of each term's similarity to the same individual's advertising idea (*i.e.*, all publications carried out the same alleged wrong); and (4) it was immaterial that the advertisements were for different products because the advertising idea being used was the same regardless of the product. *Id.* at 612–15 (explaining that the advertisements need not be identical and that to assess substantial similarity, courts have not considered all differences between pre-coverage and post-coverage publications, but have focused on the relationship between the alleged wrongful acts manifested by those publications).

Similar to *St. Surfing*, the court in *MGA Entm't* found that the prior publication exclusion precluded coverage for an underlying lawsuit for alleged infringement of intellectual property as to the BRATS versus BRATZ characters. No. CV 07-08276-SGL(RNBx), 2009 U.S. Dist. LEXIS 134871 (C.D. Cal. June 26, 2009). In so holding, the court explained that the only alleged wrong was that "[i]n about June 2001…MGA began advertising and flooding the market with a substantially and confusingly similar genre of characters called 'BRATZ.'" *MGA Entm't* at *9–10. The court continued that "[n]o part of the complaint suggests that the underlying wrongful actions were different in any substantive manner during 2003 [(*i.e.*, during the policy period)]" and that the "underlying complaints reveal that there are no allegations of anything unique or different to the advertising, infringement, or trade libel during the relevant policy period." *Id.* The court also specifically stated that even though the "precise characters, fashions, and accessories may have changed…there is no suggestion in the underlying complaints that any changes occurred in the substance of the advertisements." *Id.* at *10.

The court in *Atl. Mut. Ins. Co. v. J. Lamb, Inc.* sided with the insured and its contributing carrier against the insured's non-contributing carrier regarding a settlement agreement in an underlying action concerning disparaging statements allegedly made by the insured about the third party's business and products. 100 Cal. App. 4th 1017, 1017, 1039 (2002). The insured and the paying carrier sought to appeal a decision by the trial court ruling that the non-paying carrier had no duty to defend on the basis that there was no "advertising or personal injury" during the policy period. *J. Lamb* 100 Cal. App. 4th at 1028. The court of appeal reversed the trial court's decision on the basis that the "first publication" exclusion was inapplicable and the non-paying carrier owed sums for equitable contribution and subrogation. *J. Lamb* at 1045–46.

The court explained that "an insurer may only defeat an existing potential for coverage by *undisputed* facts that *conclusively* negate such coverage." *Id.* at 1038, *relying on Gray v. Zurich Ins. Co.*, 65 Cal. 2d 263 (1966); *Montrose Chem. Corp. v. Superior Court*, 6 Cal. 4th 287 (1993). The court then found that the "first publication" exclusion was inapplicable because "[t]he allegations of the Continental complaint did not specify the date of Lamb's first utterance of any disparagement," such that a possibility of coverage existed. *Id.* at 1038. The court also found that a declaration by the claims adjuster that stated he had spoken with a representative of the insured who stated the dispute originated "with a conversation which occurred in September of 1998", did not *conclusively establish* the date of first publication. *Id.*

III. <u>Other Common Policies Potentially Providing Coverage for IP Risks</u>

The proliferation of IP-related risks has prompted some insurers to revise their CGL policies in recent years to limit coverage for many IP claims that would be covered under traditional "advertising injury" coverages. Some now contain IP exclusions. As a result, a growing number of companies no longer rely solely on CGL policies and are instead purchasing IP-specific policies to address a broader array of IP-related risks than those covered by modern CGL policies.

For example, it is now possible to purchase "infringement liability policies" to cover third-party patent, trademark, copyright, or other infringement claims. Some limit coverage to certain products and cover only those aspects of the products that fall within the insured's own patents. Policies may also obligate the insured to advance defense costs pending the resolution of the underlying case, rather than a true duty to defend. In addition, companies who enforce their own intellectual property rights against potential infringers may purchase "enforcement" coverages. These policies are designed to provide coverage for initiating infringement claims, or in some circumstances cover the costs of defending against counterclaims seeking to invalidate a policyholder's patents and the costs to reissue the patent to strengthen the insured's patent claim.

In addition to IP-specific policies, media liability insurance may also provide coverage for certain types of IP exposures arising from e-commerce activities. These policies address the risks facing entities using non-patentable forms of intellectual property, such as media or entertainment companies. The policies generally cover liabilities stemming from the dissemination of the insured's creative works and/or advertising. The policies are usually written on a named peril basis, typically covering copyright infringement, misappropriation of ideas, trademark infringement, defamation, trade libel and violation of privacy rights.

Cyber policies can also focus on multimedia liability for risks associated with a company's activities when displaying, transmitting, and otherwise using protected content on the Internet. This can include coverage for liability arising out of claims alleging copyright infringement, trademark infringement, defamation, trade libel and violation of privacy rights. These policies, however, generally do not cover claims for patent infringement, false advertising or trade secret misappropriation.

Lastly, Technology Errors and Omissions policies are generally geared toward technology companies and insure against third-party liabilities arising from the provision of technology products and services, which can sometimes include coverage for copyright and patent infringement related to a company's provision of technology. The interplay between CGL and technology E&O coverages can be subject to coverage disputes. For example, in *Educational Impact v. Travelers Property Casualty Company*, No. 15-CV-0510-EMC, 2016 WL 7386139 (N.D. Cal., December 21, 2016), Educational Impact and Teachscape sought insurance coverage for claims arising out of Teachscape's alleged false advertising. In the underlying lawsuits, Educational Impact argued that Teachscape violated the Lanham Act, engaged in unfair competition, and tortiously interfered with Educational Impact's contractual rights when Teachscape publicly claimed that it had exclusive rights to market and sell a product licensed to Educational Impact.

Teachscape tendered the claim to its technology errors and omissions (Tech E&O) insurer and its commercial general liability (CGL) insurer. Educational Impact (now acting as assignee of Teachscape's claims) argued that if coverage for advertising injuries was available under one policy, it must also be available under the other. The District Court for the Northern District of California disagreed. It concluded that coverage was available only under the Tech E&O policy, which provided coverage for "wrongful acts," including for copyright infringement related to false advertising. The CGL policy, in contrast, provided coverage only for "infringement of copyright . . . in your advertisement." Because the complaint did not allege copyright infringement in the advertisement itself, the district court concluded that the CGL policy offered no coverage.

This case highlights a difference between the scope of coverage for advertising and intellectual property claims provided by the "personal and advertising injury" coverage in CGL policies and the coverage in Tech E&O policies for acts, errors or omissions in the performance of technology services or the sale of technology products. Coverage for certain intellectual property claims may be significantly broader under Tech E&O policies than under CGL policies.

In addition, though the court here determined that coverage was only available under the E&O policy, CGL policies often offer coverage for claims alleging product disparagement or other character harms, even if there is not a formal cause of action for disparagement in the complaint. For example, an erroneous assertion of exclusive ownership of a product or intellectual property right can cause reputational harms to competitors marketing the same or similar products, which may be enough to support an implied disparagement claim. The court in *Educational Impact* did not address this argument, and it is unclear whether the policies at issue contained the applicable language. It is possible that the policyholder and the court overlooked the potential for defense coverage under the CGL policy based on allegations that could have supported an implied disparagement theory of liability.

IV. <u>Conclusion</u>

`The "litigation explosion" observed by the Eleventh Circuit in *State Farm Fire and Casualty Co. v. Steinberg*, 393 F.3d 1226 (11th Cir. 2004) is a reality. *See also RGP Dental, Inc. v. Charter*

Oak Fire Ins. Co., 2005 U.S. Dist. LEXIS 28199 (D. R.I. 2005). As the number of intellectual property claims and lawsuits rise, so do the insurance coverage disputes between policyholders and insurers. In order to meet the challenges of this ever-changing area of insurance law, practitioners must be aware of the new decisions and new trends created by courts addressing advertising injury claims.