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Insurance Coverage News, Volume 2

"RISKY BUSINESS"

insurance coverage from a policy holder's perspective

SUBJECT:

**DOES YOUR COMMERCIAL
GENERAL LIABILITY INSURANCE
COVER INTELLECTUAL
PROPERTY CLAIMS?**



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What can cost a business millions of dollars in legal fees and costs? What can stop the production of a business' primary product? What can wipe out a business entirely? An intellectual property infringement lawsuit can result in all three. Litigation over intellectual property rights has increased year to year over the last decade. The intellectual property rights of a company, in most cases, is more valuable than physical property. You may think that your company's commercial general liability ("CGL") insurance will provide a defense and even indemnity of these types of claims. Not so fast. A decade ago, CGL insurance provisions arguably provided coverage for many intellectual property rights lawsuits. However, recently, insurers have added limiting definitions and exclusions to their CGL policies, barring coverage for intellectual property rights liabilities except in very narrow circumstances. Nevertheless, depending on the wording of an insured's CGL policy and the law of the jurisdiction, coverage may be afforded for the gamut of intellectual property rights claims.

I. The Advertising Injury Coverage Of A Typical CGL Policy

If there is coverage under a CGL policy for intellectual property claims, it will fall under the CGL policy's "Advertising Injury" coverage. Most of these policies are written on standard forms published by the Insurance Services Office ("ISO"). ISO's CGL forms with advertising injury coverage are dated 1976, 1986, 1998, and 2001. (This newsletter will focus on the last three policy forms). Whereas, the 1986 form arguably provided coverage for a wide range of intellectual property claims, the 1998 and 2001 forms dramatically reduce that coverage with limiting definitions and exclusionary language.

Most of the published case law discussing coverage for intellectual property claims under the advertising injury provision involves the 1986 form. The 1986 form defined advertising injury as injury arising out of one or more of the following offenses:

- (a) Oral or written publication of material that slanders or libels a person or organization or disparages a person's or organization's goods, products, or services;
- (b) Oral or written publication of material that violates a person's right of privacy;
- (c) Misappropriation of advertising ideas or style of doing business;
- (d) Infringement of copyright, title, or slogan.

In 1998 and 2001, ISO introduced new forms. The differences in these forms from the earlier 1986 forms that are significant to intellectual property claims are as follows:

(1) The new offense of "[t]he use of another's advertising idea in your 'advertisement'" replaced the offense of "[m]isappropriation of advertising ideas or style of doing business."

(2) "Infringing upon another's copyright, trade dress or slogan in your 'advertisement'" replaced the offense of "[i]nfringement of copyright, title or slogan."

(3) Advertisement was defined as "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." And the 2001 form added limitations to coverage for Internet activities by specifying in the definition of "advertisement" that "advertisement" with respect to a web site means only that part of a web site that is about your goods, products or services for the purposes of attracting customers or supporters.

(4) The 2001 form introduced new exclusions, the most important of which excludes "personal and advertising injury arising out of copyright, patent, trademark, trade secret or other intellectual property rights." But, the exclusion does not apply to "infringement, in your 'advertisement,' of copyright, trade dress or slogan." The other significant exclusions bar coverage for advertising injury in connection with various Internet activities, including for (a) web site designers; (b) Internet search, access, content or service providers; and (c) for chat rooms and bulletin boards.

Even though the policy forms for "Advertising Injury" coverage have changed in the last two decades, the steps to proving a covered claim, or at least a potentially covered claim, basically remain the same. Most recently the California Supreme Court held that the policyholder must demonstrate: (1) the insured was engaged in "advertising" during the policy period when the alleged advertising injury took place; (2) the claimant's allegations create a potential for liability for a covered advertising injury "offense"; and (3) a causal connection existed between the alleged injury and the "advertising." *Hameid v. National Fire Ins. of Hartford*, 31 Cal. 4th 16, 21-22 (2003).

A. Is The Claim An Enumerated Offense?

1. Trademark And Trade Dress Infringement Claims

Most courts that interpreted the 1986 CGL form concluded that the advertising injury provision covering the enumerated offense of "misappropriation of advertising ideas or style of doing business" or "infringement of copyright, title or slogan" provided coverage for trademark and trade dress infringement claims--at the very least a defense. *See, e.g., State Auto Property & Cas. Ins. Co. v. Travelers Indem. Co.*, 343 F.3d 249 (4th Cir. 2003); *Lebas Fashion Imports of USA, Inc. v. ITT Hartford Ins. Group*, 50 Cal. App. 4th 548, 564-66 (1996).

The deletion of these very enumerated offenses ("misappropriation of advertising ideas or style of doing business" and "infringement of copyright, title or slogan") in the 1998 form in favor of the offense of "infringing upon another's copyright, trade dress, or slogan in your advertisement" and the "use of another's advertising idea in your advertisement" has not been widely tested by the courts. Under the 1998 form, though, copyright and trade dress infringements are expressly covered. Whereas, trademark infringement is not. However, in *Central Mutual Ins. Co. v. StunFence, Inc.*, 292 F. Supp.2d 1072, 1079 (N.D. Ill. 2003), the court held that even though not expressly covered, trademark infringement fits within the offense of "use of another's advertising idea" and upheld coverage.

The 2001 ISO form, in contrast, expressly excludes liability arising out of infringement of "trademark . . . or other intellectual property rights." Infringement of trade dress in an advertisement, however, is not excluded. Thus, courts have found that, under the 2001 form, trade dress infringement in the insured's advertisement is covered, but trademark infringement is not. *See, e.g., id.* at 1977-78.

2. Trade Secret Misappropriation Claims

Coverage for trade secret misappropriation claims was possible under the 1986 CGL form under the "misappropriation of advertising ideas or style of doing business" offense. *See, e.g., Sentex Sys., Inc. v. Hartford Acc. & Indem. Co.*, 93 F.3d 578 (9th Cir. 1996). Insurers nipped that in the bud by eliminating coverage for "misappropriation of advertising ideas or style of doing business" and "infringement of title" as covered offenses in the 1998 form. And, insurers solidified that there could be no coverage for trade secret misappropriation claims in the 2001 form by expressly excluding coverage for trade secret claims.

3. Copyright Infringement

Copyright infringement was one of the enumerated offenses in the 1986 ISO form CGL policy, and therefore generally covered so long as the infringement occurred in the course of advertising. Under the 1998 and 2001 form policies, however, the only copyright infringement covered is that that allegedly occurs in an advertisement itself. Prior to the 1998 form, covered copyright infringement included infringement "in the course" of advertising, not simply just the advertisement itself.

4. Patent Infringement

Before 1996, looking to CGL insurance for coverage of patent infringement claims was, by and large, a losing proposition. In 1996, however, Congress amended the Patent Act to include as patent infringement the act of "offering for sale" a product that violates a plaintiff's patent rights. Prior to this time, patent infringement had to be based on the "mak[ing]," "use" or "sale or import" of a patented product. Under the 1996 amendment, a company's CGL policy under the 1986 ISO form may cover patent infringement claims because "an offer to sell," or advertisement constitutes patent infringement.

Prior to 1998, the standard advertising injury endorsement covered the insured for various enumerated offenses, which included "piracy," "unfair competition," "infringement of copyright, title or slogan," "slander, libel, invasion of privacy, misappropriation of advertising ideas or style of doing business" that arise out of the "insured's advertising, promotional or publicity activities."

In pre-1996 cases, courts almost unanimously found no coverage for patent infringement under CGL policies. The courts reasoned that because the original Patent Act only found the conduct of "mak[ing]," "use" or "sale" of a patented product valid types of patent infringement, there was no "causal nexus" between the "advertising" of the product and the alleged act of infringement. However, when Congress amended the Act to include the "offering for sale" of a product that infringes plaintiff's patents, some courts began to find that the "causal nexus" between advertising of the product and the infringement may be established.

Even so, courts have been split on whether the 1996 amendment to the Patent Act, in fact, results in coverage for insureds under their CGL policies for patent infringement claims. In *Everett Associates, Inc. v. Transcontinental Insurance Co.*, 57 F. Supp. 2d 874 (N.D. Cal. 1999), and *Everett Associates, Inc. v. Transcontinental Insurance Co.*, 1999 U.S. Dist. LEXIS 11792 (N.D. Cal. June 28, 1999), the Northern District of California held that when advertising activity or offers to sell result in alleged infringement under the Patent Act, the "misappropriation of . . . style of doing business" language is broad enough to cover patent infringement claims.

Whereas, in *Maxconn Inc. v. Truck Ins.*, 74 Cal. App. 4th 1267 (1999), the court of appeal in California, after acknowledging that the changes to the Patent Act in 1996 did not bar coverage for patent infringement as a matter of law, held that the "infringement of copyright, slogan or title" language does not allow for coverage for patent infringement claims. The court instead held that if the policy were intended to provide coverage for patent infringement, the word "patent" would appear. *Id.* at 1275-76.

Coverage for patent infringement claims under CGL policies, however, was short-lived. Both the 1998 and 2001 ISO CGL forms eliminated coverage for the advertising injury offense of "infringement of title" and "misappropriation of advertising ideas or style of doing business." These covered offenses were the ones under which policyholders typically sought coverage for patent infringement claims. The 2001 form expressly excludes coverage for patent infringement claims, resolving any ambiguity there may have previously existed.

B. Is The Insured Engaged In "Advertising?"

Once the allegedly infringing activity fits into one of the enumerated offenses in the policy, the activity must also be found to constitute an "advertising activity" under the policy. Like the enumerated offenses covered under CGL policies, the definition of "advertising" has evolved to limit coverage for intellectual property liability.

The 1986 ISO form did not provide a definition of "advertising." Not surprisingly, this resulted in differing interpretations by the courts. A majority of jurisdictions found that "advertising" meant widespread promotional activities directed to the public at large. *See, e.g., Hameid*, 31 Cal. 4th at 19. Some jurisdictions, however, held that "advertising" could mean single one-on-one solicitations. *See, e.g., John Deere Ins. Co. v. Shamrock Indus., Inc.*, 696 F. Supp. 434, 439-440 (D. Minn. 1988) (single solicitation coupled with demonstration of the item for sale is "advertising"). And some jurisdictions found that courts should consider whether there is "advertising" in connection with the infringing activity on a case-by-case basis. *See New Hampshire Ins. Co. v. Foxfire, Inc.*, 820 F. Supp. 489, 494 (N.D. Cal. 1993) (solicitations to only a target audience constitutes "advertising").

The 1998 and 2001 CGL forms attempted to resolve any ambiguity by defining "advertisement" as "a notice or published to the general public or specific market segments . . . for the purpose of attracting customers or supporters." Although eliminating coverage for a "one-on-one" solicitation, the definition arguably provides coverage for a smaller segment than the "widespread" promotion to the public at large required under *Hameid*. The 2001 form also provides that the definition of "advertisement" includes "material placed on the Internet or similar electronic means of communication."

C. Establishing The Causal Nexus Between The Alleged Injury And The Advertising

Once an enumerated offense, and "advertising" has been established, the policyholder must demonstrate that the alleged injury was caused by the advertising activity. Like the definition of "advertising" the policy wording requiring a causal nexus between the alleged advertising injury and advertising has changed from the 1986 to 1998 to 2001 ISO forms.

Under the 1986 CGL form, the alleged injury had to arise out of an enumerated offense committed "in the course of advertising." This wording led to differing interpretations by the courts. In California, the State Supreme Court held that, under the 1986 wording, the alleged "advertising injury" must have been caused by the advertising itself and that it must have resulted from the alleged "advertising activity." *Bank of the West v. Superior Court*, 2 Cal. 4th 1254, 1277 (1992). Other courts similarly held that the injury "be complete in the advertisement" for there to be coverage. *See Frog, Switch & Mfg. Co. v. Travelers Ins. Co.*, 193 F.3d 742, 750 (3d Cir. 1999). In contrast, other jurisdictions found coverage with only a tenuous connection between the injury and the advertising. For example, in *John Deere*, the policyholder had sent letters to potential customers promoting products that allegedly infringed patent rights. Even though the letters themselves were not the alleged infringing material, the court found a

potential for coverage because the policy did not require that the advertising activity be the proximate cause of the injury.

In the 1998 and 2001 policy forms, coverage requires that the alleged offense occur "*in your advertisement*" (emphasis added), eliminating the broader coverage for offenses that arise out of advertising activities.

II. Specialty Intellectual Property Insurance Policies

Given the uncertainty as to whether a company will have coverage for intellectual property claims under its CGL insurance policies, how can a company be assured of a defense and indemnity for claims of intellectual property infringement?

The best insurance protection for intellectual property claims is actual intellectual property insurance. Although the Advertising Injury coverage in CGL insurance policies, may provide some coverage for copyright, trademark, or trade dress infringement claims, patent infringement and trade secret claims are unlikely to be covered. And, insurers are likely to continue adding exclusions to their CGL policies to narrow even further the coverage provided.

In the last decade, specialty products have been created to address intellectual property claims. Intellectual property insurance policies provide both first-party and third-party coverage. First-party coverage, also known as "enforcement," "abatement," or "offense" coverage, provides coverage for the cost of enforcing intellectual property rights against others. Third-party coverage provides coverage for claims against the insured that it has infringed another party's intellectual property rights.

As the name suggests, "enforcement" policies provide coverage for the cost of enforcing intellectual property rights. The types of costs usually covered include: (1) suits by the insured against third parties for infringement of the insured's intellectual property that begins during the policy period; (2) defense against countersuits alleging invalidation of the intellectual property; (3) re-examination costs if there is an attempt to invalidate the intellectual property; and (4) costs to re-issue the intellectual property if necessary. But, buyer beware, generally these policies provide reimbursement to the insurer based on the recovery in the suit.

Third-party coverage will cover the insured for claims by third parties of infringement, including defense costs, settlements, judgments, and other expenses, such as pre-judgment interest. Coverage is subject to the garden variety of exclusions typically found in third-party coverage policies, as well as any other exclusions that may be in a particular policy. These policies are claims made policies, meaning they provide coverage for claims made by plaintiff during the policy period and properly reported.

Any company with valuable intellectual property to protect from infringers and potential claimants should purchase specialty intellectual property coverage. Experienced coverage counsel can readily determine whether coverage exists for intellectual property infringement claims or counterclaims brought against your company under your CGL or other specialty insurance and if your company has appropriate first-party enforcement litigation insurance.

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