

***NEW OPPORTUNITIES FOR CGL COVERAGE OF
PATENT INFRINGEMENT LAWSUITS:
ASSERTION OF PATENTS RIGHTS IMPLICATING
COVERAGE FOR DEFAMATION AND
DISPARAGEMENT***

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I. INTRODUCTION

Insurance coverage might arise within a patent infringement context even if the policy at issue has express patent infringement exclusions so long as the policy (like virtually all CGL policies) includes "personal injury" coverage for 'defamation,' (assuming the state courts at issue recognize that companies can defame one another and that this conduct can be true libel as well as trade libel) under such circumstances a defense may be triggered where disputes accompany patent infringement litigation.

II. CASE LAW IN CALIFORNIA AND ILLINOIS

A. Aurafin-OroAmerica

In a recent decision by the Ninth Circuit Court of Appeals, *Aurafin-Oroamerica, LLC v. Federal Insurance Co.*, No. 04-56681, 9th Circuit (Cal.) June 26, 2006, an appellate panel reversed the federal district Judge Matz's denial of a defense which he had reaffirmed after hearing oral argument on Aurafin's motion for reconsideration. It found that both a business reputation and product might be injured where an insured contacts an insurer third party where a defendant is sued for intellectual property infringement.

The panel which included Judge Schwarzer (sitting by designation) reasoned:

The facts alleged in D&W's counterclaims, taken together, could potentially allege a claim for true libel because an allegation that D&W was a patent infringer - a pejorative allegation of shady business practices - was implicit in OroAmerica's statement to QVC that D&W's gold chains infringed its patents. *See Atlantic Mut. Ins. Co. v. J. Lamb Inc.*, 123 Cal. Rptr. 256, 269 (Cal. App. 2002).

Id. at p. 2

In *J.Lamb Inc.*, Judge Croskey, cited with favor a New York case applying Illinois law, *Amerisure Ins. Co. v. Laserage Tech. Corp.*, 2 F. Supp. 2d 296, 304 (W.D.N.Y. 1998), "It seems

obvious to this Court that wrongfully asserting that a competitor's product infringes patents clearly defames the competitor and disparages his product."

B. Nvidia

In *Nvidia Corporation v. Federal Insurance Company*, No. 04 C 7178, 2005 WL 2230190 (N.D. Ill. Sept. 6, 2005), Judge Filip, applying California as well as Illinois law, found that Federal had a duty to defend claims for defamation nested with claims for trade libel as is true here. It rejected Federal's argument that the underlying lawsuit could only be construed to state a claim for trade libel and not defamation.

The underlying complaint's allegations that Nvidia and Sessel falsely stated that VisionTek was selling pirated or unlicensed goods would appear to fit within the broad bounds of such a definition [of defamation].

Id. at *8.

The underlying suit alleged that the false publications harmed VisionTek's "reputation and ability to conduct its business," were part of a campaign to "disparage ... the Debtor" (as opposed to its products), and that the false statements caused irreparable damage. . . . The claims are within the plain meaning of the defamation tort as defined in the California statute, and doubts in this area of the law go to the insured. Under California law, Federal breached its duty to defend.

Id. at *11.

The court's decision was based on a 7th Circuit authority holding that identifying a competitor as an infringer in the marketplace was defamatory where it led their potential customers to not do business with them. *See Nvidia* at *12:

For example, Illinois caselaw teaches that allegations that a company is infringing the intellectual property rights of another entity can state viable claims for defamation. *Republic Tobacco Co. v. North Atlantic Trading Co.*, 381 F.3d 717, 728-29 (7th Cir.2004) (affirming judgment against defendant for defamation under Illinois law where defendant falsely claimed that plaintiff was violating its patent and trademark rights); *Peaceable Planet, Inc. v. Ty, Inc.*, 362 F.3d 986, 993-94 (7th Cir.2004) (teaching that, under Illinois law, false claims that a

competitor "pirated" a product can state a successful claim for defamation if they harm plaintiff in its business).

The court found Illinois and California law indistinguishable on these facts. It reasoned that:

Illinois caselaw teaches that allegations that a company is infringing the intellectual property rights of another entity can state viable claims for defamation. . . . Here, [defendants] . . . falsely stated that VisionTek did not have the legal right to sell its inventory . . ., which subsequent discovery has indicated relates to allegations that products were being sold without appropriate software licenses. . . . These accusations . . . impugn the seller's integrity, honesty, and business ethics, are seen as putative defamation claims under Illinois law.

Id. at *12.

III. AURAFIN AND NVIDIA COURTS REJECTED A NUMBER OF INSURER ARGUMENT WHICH THEY DID NOT FIND IT NECESSARY TO EXPRESSLY ADDRESS

A. Libel, Which Depends on an Attack on the Integrity of the Provider of Goods, Is Often Joined with Trade Libel, an Attack on the Nature of Goods Provided

A business may sue another business for true libel in most states including California and Illinois. Such a claim is not one for trade libel. Nevertheless, in both *Nvidia, Aurafin* as well as *J. Lamb* and *Laserage*, the same facts can give rise to liability for defamation as well as disparagement. See *Franklin v. Dynamic Details, Inc.*, 116 Cal. App. 4th 375 (2004); *Nam Tai Electronics, Inc. v. Titzer*, 93 Cal. App. 4th 1301 (2001); *Alszezh & Home Box Office*, 67 Cal. App. 4th 1456 (1998).

B. Improperly Asserting Intellectual Property Rights Against a Competitor Based on False Statements Known to Be Injurious to the Competitor's Reputation at the Time Made Constitutes Libel

In *CNA Cas. of Cal. v. Seaboard Sur. Co.*, 176 Cal. App. 3d 598, 608 (1986), the court noted that "[T]he provisions in the INA and Pacific insurance policies for libel, slander, or other defamatory . . . material potentially covered allegations in subparagraph 21 (m) that WSBA misrepresented 'the business, property and rights possessed by [the Salveson] plaintiffs

to persons with whom plaintiffs did business in an effort to disrupt and prevent' the business relationships between those persons and the plaintiffs.” Judge Castillo in *Knoll Pharm. Co. v. Automobile Ins. Co.*, 152 F. Supp. 2d 1026, 1038 (N.D. Ill. 2001) stated that fact allegations of superiority could support claims for disparagement as well as true libel. A Maryland court went further in *Warfield-Dorsey Co. v. Travelers Cas. & Sur. Co.*, 66 F. Supp. 2d 681, 688 (D. Md. 1999), stating that a broker, accused of representing that its competitor broker could not write lines of business for a particular carrier, was libel for disparagement and defamation.

C. Asserted Counts for Interference and Unfair Competition May Depend on Fact Allegations of Libel

As senior Judge Alsop found in *Comsat Corp. v. St. Paul Mercury Ins. Co.*, No. 97-2236, 1998 U.S. Dist. LEXIS 2916, at *15 (D. Minn. Mar. 6, 1998) “ ‘... [In] in many cases interference with contract is not so much a theory of liability in itself as it is an element of damages resulting from the commission of some other tort.’ ”.

This follows because a plaintiff must establish an independent wrongful act, other than interference, in order to prevail on a claim for tortious interference with prospective economic advantage. *Korea Supply Co. v. Lockheed Martin Corp.*, 29 Cal. 4th 1134, 1159 (2003).

As Judge Croskey noted in *J. Lamb*:

Coverage . . . is not determined by the nature of the damages sought in the action against the insured, but by the nature of the claims made against the insured in that action. Under the personal injury policy provision, ‘[c]overage . . . is triggered by the offense, not the injury or damage which a plaintiff suffers.’ ” (emphasis in original) . . . The scope of the duty does not depend on the labels given to the causes of action in the third party complaint; instead it rests on whether the alleged facts or known extrinsic facts reveal a possibility that the claim may be covered by the policy . . . In short, Continental alleged that Lamb had falsely stated to Continental’s customers that Continental’s products were burdened with a prior legal right and their purchase of such products would subject them to litigation. Such allegations . . . amount to coverage for product disparagement and trade libel as well as defamation. (emphasis added)).

Id. at 1032-1035

Another California Court of Appeals panel observed that:

“In California . . . the plaintiff need only plead that the defendant published specified types of defamatory statements; the plaintiff need not specially allege the statements were false. The underlying complaint alleged publication to third persons, and the content of the statements were allegedly disparaging. These allegations sufficed to give rise to a potentially covered claim.” (citation omitted). *Barnett v. Fireman’s Fund Ins. Co.*, 90 Cal. App. 4th 500, 510 n.5 (2001)

Such fact allegations need not be asserted under labeled counts or actions for libel or disparagement. *See also Pension Trust Fund v. Federal Ins. Co.*, 307 F.3d 944, 951 (9th Cir. (Cal.) 2002) (“[R]emote facts buried within causes of action that may potentially give rise to coverage are sufficient to . . . trigger the defense. . . .”).

D. The Theory of Recovery or the Merits of The Underlying Action Are Not Pertinent in Evaluating Potential Coverage

Again the court reasoned in *CNA Cas. of Cal. v. Seaboard Sur. Co.*, 176 Cal. App. 3d 598, 612 n.7 (1986):

[A] policy protects against poorly or incompletely pleaded cases as well as those artfully drafted. Thus the question is not whether the complaint can withstand a motion to dismiss for failure to state a cause of action. Nor is the insured’s ultimate liability a consideration. . . . While in [the federal] case the complaint’s first cause of action was couched in terms of restraint of trade, it went on to allege that those whom it had joined as defendants were engaged in ‘false disparagement’ Albeit the policy speaks in terms of ‘defamation’ rather than ‘disparagement’, we find the tort to which it refers within the scope of the insuring clause’s protection.”)

IV. IN AURAFINA, THE COURT EXPRESSLY FOUND THAT FEDERAL HAS FAILED TO SUSTAIN ITS BURDEN TO PROVE THE APPLICABILITY OF ITS INTELLECTUAL PROPERTY EXCLUSION “IN ALL POSSIBLE WORLDS”

A. Federal’s Intellectual Property Exclusion Provides

This insurance does not apply to bodily injury, property damage, advertising injury or personal injury arising out of or directly or indirectly related to the actual or alleged publication or utterances of oral or written statements, whether made in

advertising or otherwise, which is claimed as an infringement, violation or defense of any of the following rights or laws.

- copyright, other than infringement of copyrighted advertising materials;
- patent
- trade dress;
- trade secrets; or
- trademark or service mark or certification mark or collective mark or trade name, other than trademarked or service marked titles or slogans.

B. Where Exclusions Are Ambiguous or Do Not Allow a Policyholder to Gauge What Is Uncovered, Then Any Doubt Is Resolved in Insured's Favor

As Judge Crosky observed in *J. Lamb, Inc., Id.* at. 1038-40:

An insurer may rely on an exclusion to deny coverage only if it provides conclusive evidence demonstrating that the exclusion applies. . . . Thus, an insurer that wishes to rely on an exclusion has the burden of proving, through conclusive evidence, that the exclusion applies in all possible worlds. . . . That potential was never conclusively negated and obviously cannot be negated short of an actual trial to resolve what is clearly a genuine factual dispute.

Indeed, “If the parties dispute whether the insured’s alleged misconduct is potentially within the policy coverage, and if the evidence submitted does not permit the court to eliminate either party’s view. . . the duty to defend is then established . . .”. *American Cyanamid Co. v. American Home Assurance Co.*, 30 Cal. App. 4th 969, 975 (1994)

C. The Policy Only Excludes “[Libel/Asserted as a Cause of Action for a Defense] or Enumerated Intellectual Property Torts” It Is Not Clear and Conspicuous

A number of cases have found that the infringement or violation elements of the intellectual property exclusion would not bar a defense for distinct defamation claims. A recent, and representative decision from Judge Whyte reasoned, “On their face, these disparaging statements make no mention of any of plaintiff’s patents. . . . Travelers asks the court to infer . . . that plaintiff could only have made these statements in defense of its patent rights. The court will

make no such inferential leap.”). *KLA-Tencor Corp. v. Travelers Indem. Co.*, 2003 U.S. Dist. LEXIS 10456, at *18 (N.D. Cal. April 11, 2003).

In *Aurafin*, Federal sought to rewrite its IP exclusion (under the guise of ‘interpretable), stating “If any claim asserted against the insured arises in connection with the same lawsuit wherein intellectual property claims are asserted then no defense benefits exist.”

However, the Ninth Circuit in *Aurafin* rejected this approach, finding that patent misuse was not an allegation of patent infringement but an equitable defense to a claim of patent infringement. *Mallinckrodt, Inc. v. Medipart, Inc.* 976 F.2d 700 (Fed. Cir. (Ill.),1992.). It stated “. . .Under California law, exclusions to insurance policies must be ‘conspicuous, plain, and clear” *Mackinnon v. Truck Ins. Exchange*, 73 P.3d 1205, 1207 (2003). The intellectual property exclusion at issue in this case did not meet the Mackinnon standard because it is unclear what the exclusion meant when it excluded statements made in the ‘defense’ of intellectual property rights.

V. CONCLUSION

Where market disputes refocus patent litigation on statements made to customers, patent infringement litigation can trigger a defense obligation. Especially where communications to customers causes the parties to assert claims for interference with prospective economic advantage (which is but a remedy for underlying wrongful conduct,) a defense arises where such claims factually assert defamation or disparagement even if not so labeled.

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