

THE POLICYHOLDER ADVOCATE/IP COUNSELOR

NEWSLETTER

Volume 12, Issue 2: Spring 2008

NEVADA FEDERAL DISTRICT COURT PREDICTS THE TEXAS SUPREME COURT WILL FORBID REIMBURSEMENT OF DEFENSE FEES FOLLOWING A UNILATERAL RESERVATION OF THE RIGHT TO REIMBURSEMENT

The Ohio Casualty Insurance Company v. Biotech Pharmacy, Inc. et al. adv.
U.S.D.C., District of Nevada, Case No. 2:05-CV-1214, RLH-PAL (D. NEV. 4-2-2008)

In the first decision nationally to expressly address an issue of Texas law, the Court predicted that the Texas Supreme Court would, consistent with its prior precedent, find that “a unilateral reservation of rights letter cannot create rights not contained in the insurance policy which include the right to seek reimbursement of defense fees where there was no potential for coverage”. In previous cases, the Texas Supreme Court, following *Shoshone First Bank v. Pacific Employers Ins. Co.*, 2 P.3d 510, 515-16 (Wyo. 2000) found that a unilateral reservation of rights letter cannot create a right for an insurer to seek reimbursement of settlement costs based on the logic of the Shoshone case which had expressly found that right extended to seek reimbursement of defense costs.

The Texas Supreme Court reaffirmed its earlier ruling in *Matagorda* finding in *Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc.*, No. 02-0730, ___ S.W.3d ___, 2008 WL 274878, (Tex., Feb., 2008) that in Texas the same rule applied in a excess policy context.

The court denied a concurrent motion for reconsideration under FRCP rule 69 as moot in light of its finding vis-a-vis reimbursement. It had previously concluded that a 56(f) right to conduct discovery arose in determining whether a copyright infringement claim was based sufficiently on advertising to fall within the pertinent “advertising injury” coverage.

Gauntlett & Associates attorneys, David A. Gauntlett and Joseph S. McMillen represented Biotech Pharmacy, Inc.

PROSPECTS BRIGHTEN IN THREE KEY JURISDICTIONS FOR POLICYHOLDERS IN SECURING INSURANCE COVERAGE FOR INTELLECTUAL PROPERTY LAWSUITS (CALIFORNIA/OHIO/TEXAS)

● CALIFORNIA

New case law makes the applicability of California coverage law more likely in a number of circumstances.

First, California will rarely recognize the conflict of interests unless the policy issues behind the distinct rule would necessarily create a different result.

- *Western Int'l Syndication Corp. v. Gulf Ins. Co.*, 222 Fed.Appx. 589, 594, (9th Cir. (Cal.) 2007).

Second, California coverage law will apply if a conflict of law arises where the underlying suit is in California, as this is the place of performance.

- *Frontier Oil Corp. v. RLI Ins. Co.*, 153 Cal. App. 4th 1436, 1461 (Cal. Ct. App. (2d Dist.) 2007)

Third, recent case authority clarifies the right to independent counsel in California. In typical scenarios encountered by litigants in intellectual property disputes, an insurer that asserts an “expected and intended” conduct and knowledge of falsity the “first publication exclusion” creates a conflict entitling the insured to retain independent counsel at the insurer’s expense.

- *J.R. Marketing, LLC v. Hartford Casualty Ins. Co.*, 2007 WL 4217443 at *8 (Cal. Ct. App. (1 Dist.) November 30, 2007)

Fourth, recovery of defense fees precipitated by pursuit of intellectual property lawsuits may elicit counterclaims, which are themselves covered, thereby funding the cost of affirmative litigation.

- *Aurafin-OroAmerica, LLC v. Federal Ins. Co.*, 2006 WL 1880088 (9th Cir. (Cal.) June 26, 2006)
- *Adobe Systems, Inc. v. St. Paul Fire & Marine Ins. Co.*, No. C 07-00385 JSW, 2007 WL 3256492, *9 (N.D. Cal. Nov. 5, 2007)

Fifth, California recently expanded the “genuine dispute doctrine” to permit an award of bad faith damages for reasonable attorney’s fees expended in proving coverage only where insurers withheld benefits.

- *Wilson v. 21st Century Ins. Co.*, 42 Cal.4th 713 (Cal. 2007) (“In the insurance bad faith context, a coverage dispute is not ‘legitimate’ unless it is founded on a basis that is reasonable under all the circumstances.”)

● OHIO

In a trio of recent decisions, Ohio Courts have broadly defined the scope of “advertising injury” coverage in relation to claims for trademark and copyright infringement coverage. These cases abandon the narrow focus on reading the breadth of “advertising” injury coverage for offenses of “misappropriation of advertising ideas or style of doing business” (1986 CGL ISO) and its successor “use of another’s advertising idea in your ‘advertisement’” (1998 CGL ISO).

These courts found that these offenses encompass a range of unfair competition claims, including forms of false advertising, false designation of origin, as well as trade dress and trademark infringement claims.

- *AMCO Ins. Co. v. Lauren-Spencer, Inc.*, 500 F. Supp. 2d 721, *733 (S.D. Ohio (E.D.) 2007) (Copyright/Trade dress infringement)
- *Westfield Ins. Co. v. Factfinder Marketing Research, Inc.*, 168 Ohio App. 3d 391, 401, 860 N.E.2d 145 (Ohio Ct. App. (1st Dist.) 2006) (Trade dress case)
- *Ohio Discount Merchandise, Inc. v. Westfield Ins. Co.*, No. 2006CA00059, 2006 WL 2773245, *5 (Ohio App. (5 Dist.) 2006) (Copyright infringement)

● TEXAS

The Texas Supreme Court clarified that “advertising injury” and “personal injury” coverage cases, like those for “bodily injury” and “property damage”, are subject to the notice/ prejudice rule, placing the burden on the insurer to prove that late notice created prejudice before eliminating possible coverage.

- *PAJ, Inc. v. Hanover Ins. Co.*, -- S.W.3d --, 2008 WL 109071 (Tex., 2008) (Trademark infringement)

In another seminal decision, the Texas Supreme Court, on rehearing, three years after its earlier opinion, reaffirmed the rule that an insurer that paid a settlement could not seek reimbursement of monies paid (absent an agreement to permit such reimbursement) should it be determined that it had no duty to cover its insured. Implicit in this analysis (which depended on the absence of the word reimbursement that was not in the policy) is the rule that defense fees paid are also not subject to reimbursement.

- *Excess Underwriters at Lloyds, London v. Frank Casing’s Crew & Rental Tools*, ___ S.W. 3d ___, 2008 WL 274878, (Tex., February 01, 2008)

Taken together, these cases offer opportunities to revisit improper declinations of coverage under California, Ohio or Texas law.

Where “advertising injury” coverage is typically issued on an “occurrence” basis, and the alleged wrongful acts for which coverage is denied, may go back a number of years, the potential defense fee recovery available to policy holders who pursue “buried treasure” by unearthing improper late notice/independent counsel denials could be significant.

USE OF THE LATEST ADR TECHNIQUE, EARLY NEUTRAL EVALUATION, IN INSURANCE COVERAGE DISPUTES RE: INTELLECTUAL PROPERTY/ANTITRUST AND BUSINESS TORT LITIGATION

Procuring an early neutral evaluation can offer parties a reality check on the viability of their legal positions. In an era of increased litigation expense, where one party believes it is more likely to prevail than the other, selecting an early neutral evaluator is a sign of strength. It requires the other party to submit its position to dispassionate neutral analysis and be prepared to explain any shortcomings of its case to its client before it makes the investment to go forward to trial or continue expensive litigation.

For more information regarding ENE, see John S. Blackman's article, *Neutral Evaluation – An Adr Technique Whose Time Has Come*, <http://library.findlaw.com/1999/Sep/1/128447.html>.

The Benefits of Early Neutral Evaluation of Insurance Coverage Disputes of Complex Business Litigation Matters

I have had occasion to serve as an expert witness and consultant in a number of coverage actions where the underlying lawsuits arose out of intellectual property or antitrust/business tort disputes. Knowledge of both the underlying tort and its intersection with insurance coverage generally offers a number of pertinent insights beyond the experience of many courts who do not routinely address such coverage issues.

As an author of a leading treatise, *INSURANCE COVERAGE OF INTELLECTUAL PROPERTY ASSETS* (Aspen Law and Business 1999) (updated annually), as well as numerous articles on this and related topics and an active litigator of these issues, I have a vantage point about how courts have historically analyzed coverage issues that pertain to intellectual property and antitrust/business tort litigation. The same analysis pertinent to preparation of a thorough expert report may also properly address how courts are likely to construe coverage issues.

Where the litigation has yet to be filed, and choice of law remains undetermined, this early neutral evaluation can include an assessment of the viability of the various forums who may consider coverage in a case and alert parties to choice-of-law-related issues which may not have been the principal focus of the case prior to litigation.

A Number of Issues Might Be Usefully Analyzed by an ENE

- Whether a demand to cease and desist seeking a damage remedy could constitute a potentially covered claim requiring an insurer to defend so that its early involvement in settlement might be properly implicated so that all parties could avoid litigation expenses and determine the viability of the coverage issues up front.
- Evaluating the strength of coverage for an asserted complaint or counterclaim, especially where the jurisdiction whose law would be applicable looks only to the four corners of the complaint and the pertinent policy language. (Where extrinsic evidence is either considered because it is available or known to an insurer, consideration of this information following an insurer's denial of coverage can help evaluate whether an obligation to defend may arise.)
- Evaluating whether a proposed settlement would potentially fall within coverage so as to compel an insurer to reimburse it or whether the risks of proceeding to trial could lead to uncovered claims.

Benefits of ENE in Insurance Coverage Litigation of Intellectual Property/Antitrust and Business Torts

- ENE can be scheduled early in a dispute, thus identifying issues promptly and avoiding litigation and administrative costs.
- ENE can reduce the time executives and key employees are kept away from business matters.
- ENE can illuminate strengths and weaknesses of a case so the parties can negotiate with full knowledge of their absolute and relative positions.

- ENE can be used as an adjunct to mediation where an evaluation of the strengths of legal issues on which parties vociferously disagree can assist a mediator in resolving a dispute rather than requiring the parties to proceed to a determination before a court on cross-motions for summary judgment where the results, once attained, may lead to irrevocable changes in relative position and exposure beyond that deemed acceptable by either party.
- ENE is also appropriate in unusual cases that have complicated legal issues when private resolution and speedy determinations are desirable.

The Relationship of ENE to ADR

- Compared to other engagements, the scope of ENE professional engagements is easier to define, control, and render in a cost-effective manner.
- Mediation can also follow an ENE if the parties are prepared to empower an early neutral evaluator to seek settlement based on his evaluative approach to the legal issues.
- ENE can also be of benefit in the underlying intellectual property and/or antitrust litigation for many of the reasons noted here. See recent article by Kenneth B. Germain, ALI-ABA, February 28-29, 2008 New Orleans, LA Conference, entitled *The Use of Subject-Savvy Early Neutral Evaluators to Suggest Solutions to Significant Trademark/Trade Dress Disputes in an Ex Parte and Inter Parte Situations*.

Manner in Which an ENE Can Be Appointed

- Voluntarily, through pre-dispute agreement, such as an ENE clause in an insurance contract.
- Mandatorily, pursuant to court order, premised on either of the following approaches:
 - The ADR Act of 1998, 28 U.S.C. § 651 *et seq.*, authorizes each U.S. District Court to promulgate and administer local rules requiring litigants to engage in listed types of ADR – which specifically includes ENE. “Congress passed the ADR Act to promote the utilization of alternative dispute resolution methods in federal courts and to set appropriate guidelines for their use.” *In re Atlantic Pipe Corp.*, 304 F.3d 135, 141 (1st Cir. 2002). The ADR Act itself, however, does not authorize any specific court to use a particular ADR mechanism.
 - Some courts have concluded that they can order litigants to engage in non-binding ADR processes. *In re Atlantic Pipe Corp.*, *supra*, at 144-145, distinguishing contrary cases; *In re African-American Slave Descendants Litigation*, 272 F. Supp. 2d 755, 760 (N.D. Ill. 2003). See A. Pew and R. Bales, *The Inherent Power of the Federal Courts to Compel Participation in Forums and Alternative Dispute Resolution*, 42 Duq. L. Rev. 1 (2003).

THE NEW BLOG: www.gauntlettoninsurance.com

Gauntlett & Associates is going “green” and is excited to announce this will be our last newsletter. We have embraced the legal blogosphere and have launched our blog:

www.gauntlettoninsurance.com

David Gauntlett will focus on policy holder recovery issues and current case analysis which are relevant in today's complex insurance markets. The blog will allow us to publish rich content almost daily and provide you the reader the opportunity to comment and ask generalized questions. Please bookmark the link or add it to your RSS feed.

PUBLICATIONS BY DAVID A. GAUNTLETT

David A. Gauntlett is the author of *Insurance Coverage of Intellectual Property Assets* published by Aspen Law & Business. The book and supplements are available for \$160.00 plus tax where applicable; shipping and handling are free when full payment is enclosed with the order. To order, call Aspen Law & Business at **1-800-638-8437**.

UPCOMING PUBLICATIONS BY DAVID A. GAUNTLETT

Mr Gauntlett recently authored an article for the Licensing Journal entitled *Comparative Advertising Claims Often Trigger a Duty to Defend Under Commercial Liability Insurance Coverage* to be published in June 2008.

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NEWSLETTER FACTS

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GAUNTLETT & ASSOCIATES – THE POLICYHOLDER ADVOCATE

Gauntlett & Associates specializes in policyholder insurance coverage and litigation re copyright, antitrust, patent, trademark, trade secret, business and general coverage disputes. Including:

- 1.INSURANCE COVERAGE LITIGATION FOCUSING ON IP, ANTITRUST AND CONSTRUCTION DEFECT CLAIMS
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- 6.CONSULTANT TO CORPORATIONS REGARDING WHAT TYPE OF POLICIES TO PURCHASE TO PROTECT AGAINST IP LITIGATION
- 7.LEGAL MALPRACTICE DEFENSE – AS EXPERT AND PERCIPIENT WITNESS

If you have a topic you would like to see addressed in future issues, please feel free to contact us with your suggestions.

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