

# THE POLICYHOLDER ADVOCATE/IP COUNSELOR

## NEWSLETTER

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### IMPLICIT DISPARAGEMENT CLAIMS NESTED IN FALSE ADVERTISING SUIT TRIGGER A DEFENSE

*E.piphany, Inc. v. St. Paul Fire & Marine Insurance Co.* \_\_\_ F. Supp. 2d \_\_\_, 2008 WL 5396889 (N.D. Cal. 2008)

Following oral argument by David Gauntlett, Judge Ware ruled in *E.piphany's* favor on cross-motions for summary judgment, finding a duty to defend for fact allegations of disparagement that triggered a defense in claims for false advertising and unfair competition under 15 U.S.C. § 1125(a) and California Bus. & Prof. Code §§ 17200, 17500.

In evaluating the duty to defend, the court, citing *Scottsdale Insurance Co. v. MV Transportation, Inc.*, 36 Cal. 4th 643, 655 (2005), noted that “[i]f any facts stated or fairly inferable in the complaint, or otherwise known or discovered by the insurer, suggest a claim potentially covered by the policy, the insurer’s duty to defend arises and is not extinguished until the insurer negates all facts suggesting potential coverage.” *Id.* at \*4.

The pertinent policy covers “personal injury” and “advertising injury” defined as “[m]aking known to any person or organization covered material that disparages the business, premises, products, services, work, or completed work of others.” California courts do not explicitly determine whether a cause of action for disparagement can exist where publications do not expressly identify the disparaged product or business. Precedent suggests a disparagement by implication is actionable. *Blatty v. New York Times Co.*, 42 Cal. 3d 1033, 1042, 1044 n.1 (1986) (“[t]o be referred to specifically, we emphasize, the plaintiff need not be mentioned by name, but may be identified by clear implication.” *Id.* at \*5.).

Pertinent authority included *Knoll Pharm. Co. v. Automobile Ins. Co. of Hartford*, 152 F. Supp. 2d 1026, 1037-38 (N.D. Ill. 2001) (applying Illinois law), where the claimant alleged that the policyholder had advertised its thyroid drug as “more effective than or superior to the other drugs available to treat hyperthyroidism” and had wrongfully claimed that its drug was “not bioequivalent to competing products”; competing manufacturers were deemed disparaged. *Id.* at 1036. This despite the fact that disparagement of specific competitors or products was not referenced.

As the court summarized, “In other words, by claiming that its own product was not bioequivalent to competitor products, the policyholder had, by necessary implication, suggested that competitors’ products possessed different and inferior indicia of biological activity.” *Id.* at \*5. Here, at \*6, the court found that disparagement by implication was appropriate.

The Underlying Complaint alleges that Plaintiff falsely stated that it was the “only” producer of “all Java” and “fully J2EE” software solutions, which was an “important differentiator” between competing products, even though some competitors offered products with these exact features. (Underlying Complaint ¶ 1.) . . . The Underlying Complaint further alleges that Plaintiff and Sigma were direct competitors in this market and that Sigma’s market share, sales, and reputation were damaged as a result of Plaintiff’s allegedly false statements. (*Id.* ¶¶ 1, 43.)

Taken together, these allegations show a claim for disparagement by “clear implication.” Blatty, 42 Cal. 3d at 1044 n.1. . . .The gravamen of the Underlying Complaint, therefore, is that Plaintiff made false claims about the superiority of its own products, which clearly and necessarily implied the inferiority of Sigma’s competing products, resulting in damages to Sigma.

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## COURT ADOPTS BRIGHTLINE RULE – THAT “A PRODUCT CANNOT BE AN ADVERTISEMENT FOR ITSELF” – THAT DOES NOT WITHSTAND SCRUTINY

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*Kreuger Int’l, Inc. v. Federal Ins. Co.*, No. 07-C-0736, 2008 WL 4962669 (E.D. Wis. Nov. 19, 2008)

The underlying suit alleged misappropriation of an Italian company’s furniture design for academic-style furniture, its designated CAMPUS line. See *Studio & Partners v. KI*, No. 06-C-0628, 2007 WL 3342597 (E.D. Wis. Nov. 7, 2007).

In 2003 KI applied for and received patents on an Einstein/Intellect desk and chair which were allegedly misappropriated from S&P’s furniture line. Also among the asserted claims was correction of patent inventorship, as well as misappropriation.

Both Federal and St. Paul initially denied a defense, and thereafter St. Paul reconsidered, though subject to a right to seek reimbursement. The court found that allegations that KI displayed the CAMPUS furniture in its showroom without authorization did not amount to a claim that KI improperly used S&P advertising materials.

The court assumed, without analysis or citation to pertinent case authority, that the wrongful act in the misappropriation suit was limited to a “wrongful taking” and did not also include distinct acts of misuse of the idea. This assumption is directly contrary to settled law. *Atlantic Mut. Ins. Co. v. Badger Med. Supply Co.*, 191 Wis. 2d 229, 238, 528 N.W.2d 486, 490 (Wis. Ct. App. 1995) (“Thus, the essence of the cause of action in misappropriation is the defendant’s use of the plaintiff’s product . . .”), citing *Mercury Record Productions, Inc. v. Economic Consultants, Inc.*, 64 Wis. 2d 163, 175, 218 N.W.2d 705, 710 (1974) (emphasis added)); see also *Blackmon v. Iverson*, 324 F. Supp. 2d 602, 610 (E.D. Pa. 2003) (“[The taking of the idea itself] occurs only when the defendant’s use of the idea deprives the plaintiff of some competitive or financial benefit or causes some other detriment separate from the misappropriation.”). This despite the fact that it is the latter conduct which is the basis for the damages asserted in the underlying lawsuit. This conceptual error influenced the court’s subsequent legal analysis.

The key issue in the court's view was whether the unique aesthetic design of the furniture may be considered, in and of itself, to be an advertising idea or material such that its unauthorized use or display would constitute "advertising injury" under the relevant policy language. *Id.* at \*8.

The court rejected KI's suggestion that the product itself, by virtue of its design, constitutes "advertising," reasoning, at \*9:

It is not the product *per se* that is the advertising, because even the best product can lie dormant in a forgotten cellar somewhere and no one would say its intrinsic qualities alone had "advertised" it. Instead, advertising is communication *about* a product, and as such it cannot logically be the product *itself*. This distinction is implicit in St. Paul's definition: "Advertising means attracting the attention of others [to the product] by any means for the purpose of seeking customers or increasing sales or business." The advertising – the means or act of attracting attention – needs an object; it is not *itself* the object.

The cases the court relies upon are readily distinguishable. They include design patent lawsuits where the court and parties ignored the fact that pursuant to 35 U.S.C. § 259 "exposure for sale" of an infringing product, which can also occur in an advertisement, is a discrete basis for liability. Similarly, in copyright infringement coverage lawsuits "display" of a "copyrighted work publicly" under the federal Copyright Act, 17 U.S.C. § 106(5) can create liability for copyright infringement. Having failed to ask the proper question – how liability could create a covered claim in the underlying suit – the courts' analyses in these cases, which assume that a product cannot be an advertisement for itself, do not justify the broad statements articulated by the courts and relied on by the *Kreuger* court. See *Gonzales v. Department of Homeland Security*, 508 F.3d 1227, 1235 (9th Cir. 2007) ("We have held that issues that are not raised or discussed are ' . . . not precedential holdings binding further decisions.' ").

Contrary to the court's assumption, a number of thoughtful cases addressing analogous trade secret misappropriation claims which, like common law misappropriation, make misuse of technology (whether or not it was improperly procured) actionable, find both wrongful taking and wrongful distribution can create liability, as either could independently create a potential defense duty.

In *Aselco, Inc. v. Hartford Ins. Group*, 28 Kan. App. 2d 839, 21 P.3d 1011 (2001), the court found, at 842 and 849, that Aselco

1) misappropriated SOS' advertising ideas or styles of doing business ... f) [A]s part of defendant's advertising and marketing activities, defendant created marketplace confusion as to SOS, its goods and services, and its ability to provide those goods and services." . . . The evidence obtained in discovery indicated that Aselco had copied SOS's line card and put its letterhead in place of that of SOS. Line cards are used to inform potential purchasers of the products that suppliers sell, essentially functioning as catalogs.

While a "product card" is distinguishable from the product itself, where, as here, the product (furniture) is visceral and has visually observable qualities including product information, style, and composition, it also necessarily functions as would a product catalog, such that the display of furniture in a showroom creates potential coverage.

Two other cases are also instructive. In *King Constr., Inc. v. Continental Western Ins. Co.*, 123 S.W.3d 259, 265 (Mo. Ct. App. 2003), a copyright infringement claim, the issue was whether the offense was linked to advertising so as to create liability. There, a custom home builder displayed the product, which was allegedly infringing of copyrighted

architectural plans, by making its homes available for tour. The home was thus a physical manifestation of the architectural drawing and the way such product was advertised was by permitting prospective home buyers to tour it in addition to simply seeing pictures of the home or its appearance from the street. Thus, the product – the house – was an advertisement for itself.

The same result attended where slightly more specific 1998 ISO CGL policy language was at issue in *Bear Wolf, Inc. v. Hartford Ins. Co.*, 819 So. 2d 818, 820 (Fla. Dist. Ct. App. 2002), where display at a trade show of a cigar holder to cigar retailers potentially created copyright infringement such that the mere physical display of the cigar holder created liability under the applicable copyright statute.

Also analogous is *Amazon.com, Inc. v. Atlantic Mutual Ins. Co.*, No. C05-00719RSM, 2005 WL 1711966, at \*3, \*7 (W.D. Wash. July 21, 2005), where an advertising technique was patented and the use of an Internet connection to obtain, by one click, product through the website was deemed an infringement by use of the advertising idea at issue so as to constitute both misappropriation of an advertising idea as well as use of another's advertising idea in your "advertisement" under later policy language pertaining to a series of similar patent claims.

When the *Kreuger* court stated, "Where its meaning is clear, the policy must not be 'rewritten by construction to bind an insurer to a risk it never contemplated or was unwilling to cover, and for which it was never paid'" (2008 WL 4962669, at \*7), it adopted a rule of law that has no factual application here and indeed requires a reverse construction from that adopted by the court. The *Kreuger* court added words of limitation not set forth in the policy by requiring that the advertisement not be of the product itself. Such a limitation, however, could easily have been included by the insurer as subsequent ISO policy forms have done in analogous circumstances. Thus, the mere display of product on a website is not deemed an advertisement unless that display permits an order of the product and indicates its pricing and availability. The insurer had to add these limitations in order to assure that the presumption of mere display on a website, in and of itself, was not deemed sufficient to be an advertisement.

The court's order rewarded an insurer who could have crafted more limited language by presuming an intent that was not supported by an objective reading of the policy's language. See *Fireman's Fund Ins. Cos. v. Atlantic Richfield Co.*, 94 Cal. App. 4th 842,852, 115 Cal. Rptr. 2d 26, 33 (2001) ("[A]n insurance company's failure to use available language to exclude certain types of liability gives rise to the inference that the parties intended not to so limit coverage.").

Again, the court's error is in not focusing on how liability could arise for acts of wrongful use of the furniture product as a distinct form of misappropriation. The court does not envision the circumstance where indemnity could arise for this conduct, irrespective of whether the product idea was purportedly and initially stolen. It fails to appreciate that there are distinct grounds for asserted liability, some of which might not fall within indemnity, others of which would. Where that potential for indemnity is not eviscerated by the complaint's allegations, a defense duty is compelled, as here. The court's reliance on simplistic slogan-like statements that "a product cannot be an advertisement for itself" is not supported by reference to the pertinent policy language and fails to appreciate how a particular product might in fact function as an advertisement in a given case.

The court also left open the issue of reimbursement. The majority of courts, including the Illinois Supreme Court, have found that words of limitation should not be added to a policy, and if there is no reimbursement provision therein, the court cannot imply it. *General Agents Insurance Co. of America, Inc. v. Midwest Sporting Goods Co.*, 828 N.E.2d 1092, 1103 (Ill. 2005) (If there is no right to reimbursement in the policy it should not be implicated by a court, following a number of prior decisions.). See David A. Gauntlett, *Limitations on the Right to Reimbursement: Where an Insurer Provides a Defense It Did Not Owe and Seeks Its Money Back*, 28 Licensing Journal, Oct. 2008.

## MULTIPLE INSURERS MUST REMEDIATE STRINGFELLOW HAZARDOUS WASTE SITE

State of California v. Continental Ins. Co., \_\_\_ Cal. Rptr. 3d \_\_\_, 2009 WL 18696  
(Cal. Ct. App. (4th Dist.) 2009)

In a case addressing cleanup of a hazardous waste site, the State may recover beyond limits of any one liability insurance policy period. David A. Gauntlett and James A. Lowe for the Center for Community Action & Environmental Justice and United Policyholders as Amici Curiae on behalf of Plaintiff, Cross-Defendant, and Appellant.

In reversing the trial court, the appellate court explained the applicability of the policy's "all sums language," stating, "The insurers are not jointly liable on each other's policies; rather, each insurer is severally liable on its own policy. . . . [W]hen there is a continuous loss spanning multiple policy periods, **any** insurer that covered **any** policy period is liable for the **entire** loss, up to the limits of its policy. The insurer's remedy is to seek contribution from any other insurers that are also on the risk." *Id.* at \*8. It also concluded "the State was entitled to stack the policy limits of all applicable policies across all applicable policy periods." *Id.* at \*20.

### 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

- ◆ *Intellectual Property Due Diligence in Corporate Transactions*: § 12A (West 2007) (contributor)
- ◆ *Assets & Finance: Audits and Valuation of Intellectual Property - Internal Controls, Materiality and Investment* (West/Thompson Reuters) (Westlaw AFAVIP) (contributor)
- ◆ Also soon to be published are three books:
  - *A Primer on Insurance Coverage Law, and Intellectual Property Claims Under Commercial General Liability Policies* (Insurance of IP assets) (contributing authors for Chapter 7) (Tod Zuckerman, Bob Chesler, Mary Hildebrand and Christopher Keegan)
  - *Free and Open Source Software and Content Desk Reference: A Legal and Risk Management Guide* (Browntree Publications) (contributing author of chapters on F/OSS and F/OC adoption and corporate risk management policies and procedures)
  - *Intellectual Property Practitioner's Handbook on Insurance Coverage* (ABA 2009)
- ◆ *The Licensing Journal* regularly features articles written by Mr. Gauntlett, the latest entitled *Damages Recoverable Against Insurers Who Refuse to Pay All Attorneys' Fees Incurred in Responding to Potentially Covered Intellectual Property Litigation* (West/Thompson Reuters 2009) (*publication pending*)
- ◆ *TIPS-ICLC 2009 Annual Survey* will also feature an article by Mr. Gauntlett on latest developments in Insurance Coverage Litigation.

## UPCOMING SEMINARS ON INSURANCE COVERAGE AND INTELLECTUAL PROPERTY WHERE DAVID A. GAUNTLETT IS SPEAKING OR ATTENDING

Mr. Gauntlett was recently named a *Super Lawyer* (Southern California) for the following practice areas:  
**Insurance Coverage, Intellectual Property and Antitrust Litigation**

- February 4, 2009** American Intellectual Property Lawyers Association Monthly Online Meeting - Presenting - "Procurement and Use of Insurance to Address Intellectual Property Lawsuits"
- February 26-29, 2009** TIPS 2009 ICLC Midyear Meeting: California Coverage Dreaming on a Winter's Day - Attending
- March 5-6, 2009** Third Annual IP Law Institute for the Pennsylvania Bar Institute (PBI) - Presenting
- March 5-7, 2009** 2009 American Bar Association Insurance Coverage Seminar - Tucson, AZ - Presenting - "The Right to Independent Counsel and How It Impacts the Defense of Business Tort Claims in All Its Manifestations"
- April 19-23, 2009** Risk and Insurance Management Society, Inc. Annual Conference - Orlando, FL - Attending

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For more information, contact our **Director of Business Development, Richard A. Beserra, at (949) 553-1010 x 208**  
Email: [marketing@gauntlettlaw.com](mailto:marketing@gauntlettlaw.com) to be added to our newsletter circulation list, or to be removed.

## 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 Business Tort Claims
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5. Expert Witness on Insurance Coverage Issues, Including Fee Disputes
6. Counsel to IP Case-in-chief Counsel for Insurance Coverage, Including: Choice of Forum, and Negotiation
7. Consultant to Corporations Regarding What Type of Policies to Purchase to Protect Against IP Litigation

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

David A. Gauntlett, Editor • Telephone: (949) 553-1010 • Email: [marketing@GauntlettLaw.com](mailto:marketing@GauntlettLaw.com)

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