Knobbe IP+
PODCAST

Insurance Coverage for Intellectual Property Lawsuits

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JCB Welcome to this episode of Knobbe IP+ Podcast. I'm your host of today's episode, Jared Bunker, an IP litigation partner at the law firm of Knobbe Martens. Today I'll be speaking with David Gauntlett, Principal of Gauntlett & Associates. David is an attorney who specializes in insurance law. We'll be discussing insurance coverage for intellectual property lawsuits. This is going to be an informative conversation, so let's jump right in. David, welcome to the podcast.

DAG Thank you. Happy to be here.

JCB I'd like to start with a few questions about commercial general liability or CGL policies. If my company is sued, and the complaint has only a claim for patent infringement, will there be coverage under common CGL policies?

DAG Well common policies can refer to insurance service officer "ISO" policies, and they tend to be broader than those issued by, whom I refer to as, "the gang of four". Avoid Hartford, Traveler's, Great American, and Evanston, and you'll save yourself bundles of money. They have very narrow coverages and you do not want to go there. Even if they're priced better, there's a reason they're less expensive. The first thing I'd like to know is what the plaintiff is: nonpracticing entity, competitor, someone who claims licensing relationships or is anxious to tell your customers that you are, in fact, an infringer and they should not buy from you? All of those make a difference as to how I might suggest you look at the issue. Typically patent infringement is not covered by CGL policies. You have to go to a specialty insurer, like IPISC, Intellectual Property Services Corporation out of Lexington, Kentucky, as an example for domestic version of patent coverage. You could also go to the London market for product there as well.

Unfortunately, there is coverage for a lot of IP claims in media coverage often sold as part of a package with cyber, but there's no coverage for patent, trade secret, or antitrust in that space.

So, what can you do if all you have is a patent claim? Well, it's likely that many defendants will have a counterclaim: declaratory relief, no patent infringement. Let's say the competitor is suing, you might also add a declaratory relief action stating that

the conduct you're engaging is not tortious interference, not causing injury to any of their customers, and that you have a full right to participate in the market, perhaps even have claims to licenses. The denial to that might implicate coverage beyond the patent.

JCB Can you tell us a little bit about trademark infringement and CGL policies? What should we know above coverage for complaints that identify trademark infringement claims?

DAG The CGL policy typically excludes trademark and doesn't cover it at all. If it's a trade dress claim, however, that's specifically covered. Problem is a lot of trade dress claims are not so labeled so insurance representatives, claims representatives, often miss the possibility of coverage because they don't look at the nature of the facts. They're kind of drawn initially to labels, even though that's not the test to establish potential coverage. Media policies expressly cover them. That's the place to look. And media coverage is now sold as part of cyber packages as part of the errors and omissions coverage that's now available from carriers, usually as an adjunct from a different carrier that's sold in combination by more astute brokers that deal with malpractice exposures for not just lawyers but all sorts of professions.

JCB Let me follow up on one thing you mentioned, and I've also heard you say this in the past. I've heard you say that assessing a claim for purposes of determining this type of coverage, depends on all the relevant facts and inferences, and is not limited to a claim or a claim that may be expressly identified in a complaint. Could you tell us a little bit more about that concept?

DAG Yah. There's a really thoughtful decision that's from the Supreme Court of California called *Hartford v. Swift*. It came out in 2014, and it's addressing whether the fact allegations evidence implicit disparagement. And it goes through the test that you look to, to see if that's the kind of claim you have at issue before you. And it was basically what you would think of as a passing off claim –maybe there was more, maybe there wasn't – the court ultimately defined it as not enough to trigger implicit disparagement. But it went through the test of the Supreme Court of California in case called *MB v. Scottsdale*. And it said, not only is it the fact allegations, inferences from the facts, but extrinsic evidence, which can be discovery, can be letters exchanged between the parties, and inferences on the extrinsic evidence and, my favorite, facts of evidence of potential for amendment. There's a lot of patent infringement claims as they proceed to a pretrial conference order, which supersedes the pleadings as a matter of law, that may evidence liability claims beyond patent infringement, as the case develops. The problem is that if you were to look at the case as it goes to trial, tender that claim, there might be coverage, but you don't get to do that in advance. The potential for amendment helps you prefigure what's going forward, and with careful discovery as well as communications between the parties, that can be elucidated in a way that can clarify why coverage may actually exist downstream.

JCB You mentioned discovery and communications. So if I'm understanding correctly, some possible approaches if I'm facing an accusation or I'm facing a lawsuit, trying to gather some of this extrinsic evidence to help my coverage claim, you're talking about a letter

writing campaign or letter writing back and forth with the accusing party or the opposing counsel, or interrogatories – is that the type of stuff you're talking about?

DAG I'm not a big fan of interrogatories. Those are usually answered by lawyers. But depositions after document production can be great to sort of trap parties. "Well, aren't we eating your lunch in the marketplace by this competitive product that looks very close to yours? Do you think that's causing any injury and damages to you?" And if you get the right people in the marketing department or the CEO, they may be very thoughtful in their responses, and helpful. We've had that experience on a couple of occasions, and it really turned the case around. You can also do a Starbuck's mediation where, under privilege of mediation, you can explore the coverage implications of the litigation at a particular phase. This is usually done later in the case where the parties know there's no easy exit and they're looking for money to solve the problem.

Commented [OE1]: Jared and/or David, could you confirm this is what was said?

JCB Tell us a little bit more about that in sort of a mediation or a discussion with the other side. Are we talking about discussing potential additional claims to add through an amendment?

DAG Perhaps. That's a requisite in about 20 states. You actually have to have an amendment of the pleadings, they control coverage. California isn't among those, nor is New York. And in those jurisdictions, you can just basically clarify what the facts are that is the basis for the asserted claim. It can be in response to discovery, doesn't have to be. It can just be in response to letter writing. Or it can follow a mediation experience where there is clarification of the nature of the claims. Amendments are simpler, easier for the carrier to digest, because there's what the law requires and the way the carriers view the law, and they have a very restricted view. And so if you meet their restricted view, it can minimize transaction costs in getting to the results you want to get.

JCB I see. So having it in a pleading, having it some kind of formal court document certainly helps the carrier understand what they're facing, a little bit more than if it were absent.

DAG Yeah, remember that the claims representatives probably just finished an auto accident case. This may be the first personal advertising injury coverage case under GL policy that they've had all month. They don't have the background. They're designed to be efficient, effective, move forward, and so you have to give them a lot of help. And a lot of what I do is write helpful letters to claims reps to give them the background and knowledge. And sometimes they have to intern it to internal coverage counsel or outside. But the more they know the less work they have to do, the least resistance they'll have to recognizing that duty.

JCB Let me follow up on something else you mentioned. You mentioned media policies, cyber… can you talk about, outside of CGL policies, some of these maybe less common or exotic policies, that might provide coverage for defending intellectual property lawsuits?

DAG Yeah, I don't think media is terribly exotic – it just isn't purchased a lot. The broker community doesn't understand them well, and to help them get sold they started marrying them to cyber coverage which people are starting to actually buy because they're worried about social engineering fraud problems. And so – and you should also buy crime with the cyber because a lot of the cyber doesn't cover social engineering fraud that crime does – and so if you have that package, they just throw in the media for no extra cost because the premium for the cyber was enough to cover the float. So because of that, they're more readily available than they used to be and, like I said, they're covering straight up trademark and copyright, various forms of unfair competition, false advertising, and so it's a really great and affordable product. I've seen them priced for $1 million and about $15,000 a year or less for smaller companies, and it's something worth exploring. As are D&O policies for privately held companies that can be a better price than they are for bigger corporations.

JCB Tell us how D&O polices get implicated, or can be implicated, in an intellectual property lawsuit situation.

DAG Well they cover wrongful acts which is incredibly broad. Then they exclude virtually everything else. And if you're not an officer or director and an officer or director is not sued, the likelihood is you pretty much are only getting securities violations coverages. But suddenly if you have an officer or director named in the lawsuit, there's no exclusions for patent infringement or any other IP claim. So it's the inexpensive way to get patent coverage, is to have an officer or director. Not all officers and directors are enthusiastic about being named in lawsuits, so there's some issues that have to be addressed in that space. But potential for amendment can get you a good space to deal with too.

JCB So switching gears and looking at this from the perspective of somebody who's asserting a patent infringement claim, if one is interested in triggering coverage, they may be looking at a director or officer to include in a lawsuit?

DAG Yes. And often that is something that happens after mediations are unsuccessful and having coverage available to pay settlements becomes a prime interest to all parties and at that point an amendment can be more easily suggested. And it could be that you have the officer or director named in the complaint to start with and it's just a matter of making them a party.

JCB A reminder, listeners, that I am Jared Bunker and we are here today talking with David Gauntlett about insurance coverage for intellectual property lawsuits. David, let's say a policy does require a carrier to cover my defense of an intellectual property lawsuit, and I already have IP counsel – counsel that I trust, counsel that knows the situation, knows the dispute, knows my business. Do I have to go with insurance counsel, or do I have any options to select my own counsel?

DAG Well, it depends what law applies. And the law of various different forms may be applicable. Just because a case is pending in California, the parties, the insurance issuance, the brokers, all of that may influence what law may apply. California is 25th on my list. It's not my favorite jurisdiction. There's a lot of better places to go. And so

you should be very open to considering other options that are a place where coverage can be pursued. One of my favorite jurisdictions is, of all places, South Carolina. Why is that? All insurance companies are out of state. They're considered Yankees. There's a fabulous case called *Episcopal Church v. Church Insurance Co.* Imagine it's a conservative version of the Episcopal church, they're fighting over right of who has the church property. A local federal judge is asked to decide if they should help this company out and get the insurance company to pay for the cost in defending the lawsuit. I was a consultant, and let us just say that our briefs flowed into the order. There's no better way to understand what a policy holder dreams of getting, in any case, than *Episcopal Church v. Church Insurance Co.*, 53 F. Supp. 3d 816. Highlights: coverage fees awarded, control of counsel awarded, right to recover pursuit of a prosecution claim awarded, all pretender costs awarded. So this is sort of the wish list, that case, and you can use it as a template as what you'd like to see in any particular matter.

JCB So this issue, and many others I would imagine, can be very venue specific. Can you talk a little about how venue is decided, about how one might push for one venue versus another inside of these coverage cases?

DAG Well, there's two ways to control the right to independent counsel. One is to accept no for an answer. Get all the evidence you need before the carrier, and then present the bill at the end of the case and point out that there's 10% prejudgment interest from the date of invoice under California, 9% New York, 12% Massachusetts, 18% Texas. A lot of good places to go. Sometimes if the company can afford the litigation, later is better. But they have to not wait to use extrinsic evidence where it's permitted because if they do there's this case called *Basalite* that says "Sorry, too late. Would've helped, but not now." The other thing to bear in mind is if you are seeking to argue for independent counsel you may have to bring a declaratory relief action in your favorite forum to get their choice of law rules to control what law applies.

JCB Let me ask you a little bit more about the situation where coverage is denied. What are some best practices when coverage is denied and you think they got it wrong?

DAG Well first you have to figure out if they got it wrong because they're not properly applying the law. A typical example would be the carrier relying on proof of all the elements to assert a tortive commercial disparagement, when in fact, the legal standard only required to show implicit disparagement or some facts sufficiently. The *Vitamin Energy* case from the 3rd Circuit Court of Appeals, reversing the district court a couple of years ago, in which I'm an expert witness on bad faith, is a good example of that. And basically the Court of Appeals said just read the policy in the complaint. It's obvious. But they applied the standard and said no you have to prove commercial disparagement. In the *Winklevoss* case, involved Howard Winklevoss, the father of the twins in the Social Contract movie [Editor's note: The movie being referenced is the 2010 film *The Social Network*], we represented him there in Illinois. Judge Castillo, a very brilliant judge in the Northern District, came up with a couple of very thoughtful orders early on pointing out there's nothing about this that says the tort of commercial disparagement is the *sine qua non* of getting any coverage. So that hasn't been

applied by a lot of courts, but just getting the carrier to follow the rules correctly can be the first stroke. Second, they may have varied position views about things that are wrong, but maybe you want to wait to see if there's enough at stake so the cost of litigating a coverage case is really the sensible approach. And so the timing may be later.

JCB Any help to be gained by involving the broker? Anything helpful there?

DAG Well it's always good to let the broker know about the case. Don't let them be the only one tendering it because they may not. But they may have advice as to who to send it to. Because first you have to make sure you have all the right entities insured, and sometimes you can talk to the broker about fixing things that hadn't been done correctly. And that happens a lot that there's not enough communication between the people who are doing the formation of entities for the business and the folks that show up as insureds on the policies they're relying on. But once the broker gets notice they're supposed to give it to the insurer, but you have to make sure that's been done.

JCB You mentioned some of your work as an expert witness. Can you tell us a little bit more about that in these coverage disputes, these coverage lawsuits, what is your role as an expert witness and what does that entail?

DAG Well I just had one in Santa Barbara where my role was to point out that when the insurer decided to immediately hire a coverage attorney to keep all communications cloaked and nondisclosed, that there might be some hiding of the ball. And the jury came out with the full amount of an award of compensatory damages for a million and $15 million for punitive because they decided that the carrier was not following the proper procedures. And my job was to explain what custom and practice looks like for a carrier who's properly following the rules and point out when they weren't weighing both sides of the scale as they needed to do to fairly adjust claims.

JCB Let me ask you another question about triggering coverage and avoiding triggering coverage. We spoke about a couple of strategies that a plaintiff may take for either increasing the chance of triggering coverage and also the strategies for increasing the chance of avoiding the defendant being able to have coverage. We talked about carefully asserting specific claims and not others. We talked about involving potentially directors and officers in your claims. Any other strategies that a potential plaintiff might have for increasing the chance of triggering insurance or avoiding it?

DAG Well basically if you're looking to a commercial general liability policy, you just avoid claiming damages of any kind. Pure injunctive relief is fine. No attorneys' fees. You can't ask for attorneys' fees. There's a brilliant decision by Judge Curiel of the Southern District, going at great length to describe the circumstances in which attorneys' fees are considered damages for purposes of the CGL policy. Very thoughtful. And so there's ways that you can make that not happen. And you can always change your mind. As you get closer to settlement, you can decide, okay now I'm seeking an amendment to add them. Because of that, carriers will often be asked, by folks like me, to defend a case where there are no damages claimed and they haven't been expressly waived or a potential for amendment exists. So if you really

want to assure yourself of being within the envelope of protection, you might have to get a waiver. That's going to require some in-depth conversations with the client about why and the purposes and extent of those should be well documented.

JCB Let me ask you one more question about some of these IP-specific policies. I'm aware of some policies that are specifically tailored for patent infringement disputes and lawsuits. What can you tell us about those policies? What's your impression? Any best practices or tips in that area?

DAG Well there's not a lot in the market outside of London. IPISC is the most vigorous participant. We've actually helped – I've represented IPISC in suing Hartford where they stepped up in a trademark case for the insured, Skechers, and had to sue Hartford to get the money they had advanced back because as a specialty carrier they were supposed to be backup, not the first string. We also had a case wherein they agreed to defend patent case one, and another patent in the same family they said no. We had to write a 25-page, single-spaced letter explaining they were not reading their policy correctly, and they backed down and agreed to send a second case. So, they're educable but they sometimes need to be brought around. Also, sometimes a policy application materials can suggest that they reserve rights to change their mind, so you have to negotiate sometimes the provisions that they're offering you. You know, it requires careful representation through the process of policy procurement. It's not like just buying a CGL policy through a broker. And frankly there are not a lot of brokers that even interact with entities like that. So it's pretty much you and the insurer. And that's why we spend a lot of time helping folks buy policies of insurance in all sorts of domains – media, cyber, you can imagine.

JCB David, before we wrap up here, any other big points, big take-home messages that our audience might need to know or should understand about insurance coverage for intellectual property lawsuits?

DAG Well, although this case wasn't an IP case, it involved a D&O policy, whistleblower issues, and an ex-employee. The *Legion* cases out of Delaware, following California law, point out why other lawsuits than the one you're involved in, where they have related issues that are strategically defensive of the suit you're defending, may come within the obligation of the insurer to fund. And that could be prosecution or the defense of a case. We had one in which we had six related lawsuits we were able to get all covered within the envelope of the insurer's obligation. And remember a CGL policy often doesn't have a limit on defense fees – it's unlimited. In a case we had for Hewlett-Packard, we had an international policy which we got them $54 million in defense fees on, because there was no limit.

JCB That wraps up today's episode. A big thanks to our guest, David Gauntlett, for joining us today. Be sure to visit knobbe.com to listen to or view written transcripts of this and other episodes of Knobbe IP+. Thanks for listening.

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