I Know What You Mean

Recent Decisions Construing "Personal and Advertising Injury" Coverage for False Advertising and Deceptive Trade Practice Claims

By Thomas W. Arvanitis

Rapid developments in technology and the regulatory environment have spawned significant changes in the breadth and complexity of claims liability insurers face. In this ever-evolving landscape, it is vital for insurance law practitioners to be aware of how courts are defining the contours of "personal advertising injury" coverage in the context of both traditional and 21st century claims, because these claims are often high-stakes, "bet the company" exposures. Business disputes between aggressive competitors that spare no expense give rise not only to potentially massive damage awards, but skyrocketing litigation costs. Faced with these new and significant exposures, insureds are looking to their "personal and advertising injury" coverage more than ever for a defense and indemnity. And this is particularly true where an insured faces false advertising and deceptive trade practice claims.

But under what circumstances will these claims implicate the "personal and advertising injury" coverage? And when? This article will discuss a couple of recent decisions that illustrate the different approaches courts have taken in evaluating an insurer's obligations under the "personal and advertising injury" coverage in the context of false advertising and deceptive trade practice claims.

Recent Decisions Assessing the Application of the Disparagement Offense in the Context of False Advertisement Claims

For an insurer's duty to defend a lawsuit to exist under the "personal and advertising injury" liability coverage, the insured must establish (among other things) that the lawsuit at least potentially seeks damages that are within the scope of one of the enumerated "personal and advertising injury" offenses. Oftentimes, these offenses include injury arising out of oral or written publication of material, in any manner, of material that slanders or libels a person or organization or disparages a person's or organization's goods, products or services ("disparagement offense").

To potentially implicate the disparagement offense, the insured must allegedly: (1) publish material, either in writing or orally, (2) that disparages the claimant's goods, products, or services. To constitute "disparagement," the statement must be made about a competitor's goods; it must be untrue or misleading; and it must be made to influence or tend to influence the public not to buy those goods or services. *Pekin Ins. Co. v. Phelan*, 799 N.E.2d 523, 526 (Ill. App. Ct. 2003).

Over the past several years, there has been a steady rise in the number of cases addressing coverage under the disparagement offense, despite no express claim against the insured for slander, libel, or disparagement. These cases often emanate from disputes in which the insured is alleged to have falsely advertised its products, infringed a competitor's intellectual property, or made "knock-offs" or inferior versions of the competitor's products. The question becomes whether these allegations involve a statement that implicitly references the competitor and, if so, whether the statement says something false or derogatory. If so, some courts have found a potential claim for implied disparagement sufficient to trigger an insurer's duty to defend.

For example, in *Jar Laboratories, LLC v. Great American E&S Insurance Co.*, 945 F. Supp. 2d 937 (N.D. Ill. 2013), the insured was sued for false advertising based on statements it made about its over-the-counter pharmaceutical product, LidoPatch, that allegedly caused the distributor of a competing prescription product, Lidoderm, to suffer damaged goodwill and lost profits. The insured's false advertising allegedly included statements that its product would provide the same benefits as the "prescription brand" and had the "same active ingredient as leading prescription patch." Although the insured never mentioned Lidoderm by name, the court found that its statements were clear references to the insured's competing product. Because the insured implicitly equated the competitor's product with the insured's allegedly inferior product, the court found the underlying complaint alleged a potential claim for implied disparagement, triggering a duty to defend.

That is not to say that false advertisement claims necessarily involve implied disparagement for purposes of "personal and advertising injury" coverage, however.

Take *Albion Engineering Co. v. Hartford Fire Insurance Co.*, No. 1:17-cv-3569, 2018 WL 1469046 (D.N.J. Mar. 26, 2018) (New Jersey law), in which the insured was sued by a competitor for falsely advertising its caulking guns as made in the U.S.A., when they were actually made in Taiwan. The competitor alleged that it distinguished its competing caulking guns based on their manufacture in the United States, and that the insured's false advertising resulted in lost sales and damage to the competitor's reputation.

In analyzing whether the disparagement offense was triggered, the *Albion* court found that an action for product disparagement or trade libel requires: (1) a publication; (2) with malice; (3) of false allegations concerning the plaintiff's property or product; and (4) special damages. The insured's alleged false representation that its products were made in the U.S.A. contained no statement that referenced the claimant, explicitly or implicitly. The court therefore concluded that the underlying complaint failed to allege a potential claim under the disparagement offense.

Albion is in line with other recent decisions finding that an insured's false statements about its own products, which do not necessarily refer to and derogate a competitor's product or clearly imply the inferiority of the competitor's product, do not give rise to a potential claim for disparagement by implication, and thus do not implicate the disparagement offense. *See*, *e.g.*, *Vitamin Health, Inc. v. Hartford Cas. Ins. Co.*, 685 Fed. App'x 477 (6th Cir. 2017) (Michigan law); *Charter Oak Ins. Co. v. Maglio Fresh Foods*, 629 Fed. App'x 239 (3d Cir. 2015) (Pennsylvania law).

Even when an insured is alleged to have made a false statement that expressly references the claimant, there may be no coverage under the disparagement offense absent a claim for damage to the claimant's reputation. For example, in *Cincinnati Insurance Co. v. Zaycon Foods, LLC*, No. 2:17-cv-140, 2018 WL 847247 (E.D. Wash. Feb. 13, 2018) (Washington law), the insured, Zaycon Foods LLC, faced claims for violations of securities laws, fraud, negligent misrepresentation, breach of fiduciary duty, and others related to the ouster of Zaycon's CEO. Zaycon argued there was a duty to defend allegations that it falsely represented the former CEO's position on a deal to obtain votes from Zaycon members for his removal. The court found that, under Washington law, defamation is concerned with compensating the injured party for damage to reputation. Although Zaycon allegedly made a false statement about the claimant, nowhere was it alleged that the claimant suffered reputational harm, or that the claimant sought damages for any such injury. Therefore, the court found the insurer did not have a duty to defend under the disparagement offense.

Recent Decisions Construing Policy Exclusions in the Context of False Advertisement and Deceptive Trade Practice Claims

Even if a lawsuit's false advertisement or deceptive trade practice allegations can be construed as potentially seeking damages that implicate the disparagement offense, exclusions applicable to Coverage B. could limit or possibly exclude coverage with respect to such damages.

For example, in *Scott, Blane, and Darren Recovery, LLC v. Auto-Owners Insurance Company*, No. 17-12945, 2018 WL 1611256 (11th Cir. April 3, 2018) (unpublished), the Eleventh Circuit, applying Florida law, found the "quality of goods" exclusion precluded a duty to defend allegations that the insured falsely advertised the quality of its tuna meat.

The insured, Anova Food, Inc., advertised that it preserved its sashimi-grade tuna using a natural wood smoking process, without the use of additives or chemicals. King Tuna, Anova's competitor, alleged the insured was actually using synthetic carbon monoxide to give its tuna the bright red color favored by consumers. King Tuna also alleged that Anova falsely advertised its tuna meat as "superior to its competitor's offerings" based on its wood chip smoking process. King Tuna filed two suits against Anova for false advertising under the Lanham Act and unfair trade practices.

Anova's insurer, Auto-Owners Insurance Co., declined a duty to defend. After incurring over $3.5 million to defeat King Tuna's claims, Anova sued Auto-Owners for breach of contract and bad faith. Anova sought coverage under the disparagement offense.

The district court found the disparagement offense was not triggered because Anova's statements were directed generally to its competition, not specifically to King Tuna, and therefore did not support a claim for express or implied disparagement.

After a detailed summary of the parties' positions, the Eleventh Circuit declined to rule on the issue. The court found that, even if King Tuna alleged a potential claim for implied disparagement, coverage was nevertheless precluded by the exclusion for "advertising injury" arising out of the "failure of the insured's goods, products or services to conform with advertised quality or performance." The Eleventh Circuit reasoned that the underlying lawsuits

accused Anova of misrepresenting the nature, characteristics and qualities of its tuna products by claiming they were prepared in a manner different from Anova's actual methods of preparation. The court therefore concluded the suits "arose from the alleged failure of Anova's products to conform to their advertised quality," and were excluded from coverage.

The Scott decision is a reminder of the key role the "quality of goods" exclusion may play in limiting coverage for potential claims of implied disparagement, particularly when the insured's advertised claims of superiority are based solely on false statements concerning the quality of its own goods, products or services.

In contrast, the recent decision captioned *West Bend Mutual Ins. Co. v. Ixthus Medical Supply, Inc., et al.*, No. 2017AP909, 2018 WL 1583124 (Wis. Ct. App. Mar. 28, 2018) (unpublished), illustrates the reluctance courts exercise in applying policy exclusions predicated on an insured's intentional conduct. In *West Bend*, the Wisconsin Court of Appeals found West Bend had a duty to defend its insured against allegations of willful misconduct and fraud, because the underlying complaint included causes of action that did not require proof of intentional wrongdoing.

The insured, Ixthus Medical Supply, was sued by Abbott Laboratories for deceptive business practices, unfair competition, trademark and trade dress infringement, and fraud. Abbott sold blood-glucose test strips for international use that did not comply with U.S. regulations, and were cheaper than their domestic counterpart. Abbott alleged that Ixthus illegally conspired to pass off Abbott's test strips as domestic test strips that qualified for Medicare and Medicaid reimbursement. Ixthus then allegedly falsified rebate claims submitted to Abbott. Ixthus allegedly knew its diversion of the test strips was illegal, and constituted criminal mail, wire, and insurance fraud.

West Bend denied a duty to defend based, in part, on the exclusion for "personal and advertising injury" "caused by or at the direction of the insured with the knowledge that the act would violate the rights of another and would inflict 'personal and advertising injury.'" The trial court agreed with West Bend, finding the exclusion applied because the underlying complaint alleged only willful misconduct by Ixthus.

The insurer's victory, however, was short-lived. On appeal, Ixthus and Abbott successfully argued that, regardless of whether a complaint alleges a policyholder knowingly committed a wrongful act, an insurer has a duty to defend if the policyholder could face liability without a showing of intentional conduct. Abbott's complaint included strict liability claims for trademark dilution and deceptive trade practices under the Lanham Act and New York law. Because Ixthus could face liability under these causes of action regardless of its intent, the court found Ixthus faced potential liability for which the exclusion would not apply.

West Bend argued on appeal that, because the duty to defend is determined by the facts alleged rather than the theories of liability, coverage for Abbott's lawsuit was excluded because the complaint alleged only a fraudulent, criminal scheme. The West Bend court was not persuaded by the argument. It noted that, although some of the counts included allegations of intentional misconduct, others did not. The court also rejected West Bend's argument that the exclusion nevertheless applied because each count incorporated by reference the allegations of willful misconduct and criminal fraud set forth in the body of the complaint.

The *West Bend* decision thus serves as a reminder of the challenges insurers face in some jurisdictions when relying on Coverage B's intent-based exclusions to deny a duty to defend.

Conclusion

This article, which expresses the opinions of the author and does not necessarily reflect the views of Nicolaides Fink Thorpe Michaelides Sullivan LLP or its clients, demonstrates the different approaches courts have recently taken in construing the circumstances in which a false advertisement or deceptive trade practice claim may implicate a liability policy's "personal and advertising injury" coverage. Each claim requires a fact-specific inquiry, to be sure. Even so, given the potential exposure that "personal and advertising injury" claims present, insurance law practitioners will want to be mindful of the ever-evolving, developments in case law construing the scope of "personal and advertising injury" coverage in the context of false advertisement and deceptive trade practice claims.

Thomas W. Arvanitis is a partner of Nicolaides Fink Thorne Michaelides Sullivan LLP in Chicago, where he focuses his practice in insurance coverage counseling and litigation. He has significant experience advising insurers on coverage issues with respect to personal and advertising injury coverage, including intellectual property claims, privacy claims, defamation claims, false imprisonment and malicious prosecution claims. *The author would like to thank associates Meaghan Sweeney and Emily Steinberg for their assistance in the development of this article.*