

California Supreme Court Defines Scope of Advertising Injury Coverage

Hartford v. Swift imposes “specificity” requirements that may provide comfort to companies facing disparagement claims while requiring careful navigation to trigger CGL policies.

The California Supreme Court recently issued a ruling that may serve as a classic “double-edged sword” for companies whose alleged competitors attempt to bring disparagement claims. In *Hartford Casualty Insurance Co. v. Swift Distribution, Inc.*, No. S207172 (June 12, 2014),¹ the Supreme Court clarified and limited the circumstances in which an implicit “disparagement” claim can trigger an insurer’s duty to defend under the “advertising-injury” component of comprehensive general liability (CGL) insurance policies. Importantly, however, in doing so the court also provided businesses with a potential reprieve from an onslaught of future disparagement lawsuits.

As a result of the ruling in *Swift*, California businesses facing intellectual property rights or advertising law litigation risk should carefully evaluate their coverage portfolios to accurately assess their available insurance benefits, and consult with experienced coverage counsel before interpreting *Swift* hastily.

Swift Delineates the Scope of “Disparagement” Claims

In *Swift*, a transport-cart manufacturer, Gary-Michael Dahl (Dahl) sued Swift, d/b/a Ultimate Support Systems (Swift), which sold a competing transport cart, for patent and trademark infringement, unfair competition, misleading advertising and breach of contract. Although Dahl did not expressly allege disparagement as a cause of action, Dahl’s allegations arguably could be construed to imply such a claim; Dahl asserted that Swift’s similarly named cart misled the public into believing that Swift’s products were the same as or affiliated with Dahl’s products (the “consumer confusion” theory). Moreover, Dahl contended that Swift’s advertisements included allegedly “false statements of superiority,” which arguably could be construed to imply the inferiority of Dahl’s cart (the “superiority” theory).

Swift sought a defense against Dahl’s lawsuit under the advertising-injury provision of its CGL policy issued by Hartford.² Determining whether Hartford’s defense obligation was triggered turned on whether the court agreed Dahl’s claims could be construed to allege disparagement. The California Supreme Court sided with Hartford, holding that standard CGL policy language only covers a “disparagement” claim when a false or misleading statement: (1) *specifically refers* to the underlying plaintiff’s product or business and (2) *clearly derogates* that product or business. Both of these requirements “must be satisfied by *express mention* or by *clear implication*.”³

Applying its newly announced principles to Dahl's underlying allegations against Swift, the Supreme Court rejected both Swift's "consumer confusion" and "superiority" theories of coverage. First, the Court found that no potential disparagement claim existed due to alleged consumer confusion between the carts. Contrary to the contention that Dahl's allegations implied the Swift cart was an inferior quality "knockoff," Dahl repeatedly alleged as a key aspect of its patent and trademark infringement claims that the two carts were "nearly indistinguishable."

Second, the Court rejected Swift's argument that claims of superiority and puffing constitute a coverage-triggering disparagement claim. Swift's allegedly false marketing statements lauding its cart as "innovative," "unique" and "unparalleled" extolled Ultimate's cart without demeaning Dahl's product. The mere fact that Swift allegedly falsely described its cart as "patent pending" did not "suggest that it ha[d] any unique feature that [was] an 'important differentiator' between [the] competing products."⁴ The Court held that mere claims of superiority and puffing are not sufficiently specific to support a disparagement claim, and therefore did not trigger Hartford's duty to defend.⁵

Implications for Policyholders

Swift establishes a new set of rules for advertising injury coverage that policyholders must navigate carefully. To satisfy the *Swift* "specificity" requirements, defendants seeking coverage should focus on allegations and evidence of false and misleading statements that specifically or clearly are derogatory towards the opposing party's product or business.

Although the *Swift* court may have set a higher bar to trigger coverage, *Swift* may also offer a silver lining for policyholders seeking to minimize the risks of potential disparagement claims. The court predicated its ruling in part on the policy rationale that Swift's "superiority" theory, in particular, could transform almost any advertisement touting the superior quality of a company or its products into fodder for "disparagement" litigation. Proliferation of such litigation would interfere with "the free flow of commercial information" and "the informational function of advertising," which are "essential to informed choice in our free enterprise economy." The specificity limitations articulated in *Swift* should "narrow the range of publications in the marketplace that may rise to the level of a legally actionable injurious falsehood" and help to "forestall[] 'vexatious lawsuits' over perceived slights that do not specifically derogate or refer to a competitor's business or product."⁶ In other words, the specificity requirements should "significantly limit the type of statements that may constitute disparagement, especially since advertisements and promotional materials often avoid express mention of competitors."⁷

On the reverse side, companies intending to **assert** disparagement claims against competitors should also consider *Swift* when drafting complaints. If triggering the defendant's policies is a strategic goal for the plaintiff, then a well drafted complaint may better position such triggering of coverage. Although *Swift* arguably narrows the circumstances in which a plaintiff's lawsuit will trigger CGL coverage, the decision does not eliminate the possibility entirely. Conversely, if triggering the defendant's coverage would be strategically counterproductive, then the plaintiff should think carefully about how to plead the infringing conduct, and follow the guidance provided in *Swift*.

The *Swift* decision adds another layer of complexity to the already nuanced litigation at the intersection of advertising and intellectual property. Before filing patent or trademark infringement lawsuits, companies should contact sophisticated counsel to fully discuss their options and analyze how best to frame their allegations in a way that ensures the best chance of successfully resolving the case. Similarly, because *Swift* imposed a difficult but not insurmountable obstacle for policyholders to trigger CGL policies, companies seeking to obtain coverage should enlist experienced coverage counsel to assist in navigating the Court's "specificity" requirement.

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Endnotes

¹ *Hartford Cas. Ins. Co. v. Swift Distrib., Inc.*, No. S207172, 2014 WL 2609753, at *1 (Cal. Jun. 12, 2014) (publication forthcoming) (*Swift*).

² The California Supreme Court outlined the duty-to-defend standard in *Horace Mann Ins. Co. v. Barbara B.*, 4 Cal. 4th 1076, 1081 (1993):

[A] liability insurer owes a broad duty to defend its insured against claims that create a potential for indemnity....[T]he carrier must defend a suit which *potentially* seeks damages within the coverage of the policy....The determination whether the insurer owes a duty to defend usually is made in the first instance by comparing the allegations of the complaint with the terms of the policy. Facts extrinsic to the complaint also give rise to a duty to defend when they

reveal a possibility that the claim may be covered by the policy....Any doubt as to whether the facts give rise to a duty to defend is resolved in the insured's favor.

³ The *Swift* ruling required the Court to repudiate a Court of Appeal's reasoning in *Travelers Prop. Cas. Company of America v. Charlotte Russe Holding, Inc.*, 207 Cal. App. 4th 969 (2012) (*Charlotte Russe*). In *Charlotte Russe*, the court concluded that a clothing retailer's low pricing of a supplier's products could imply low quality, which supports an implied disparagement claim. The *Swift* Court disagreed, because "[d]isparagement by 'reasonable implication' requires more than a statement that may conceivably or plausibly be construed as derogatory to a specific product or business." A "reasonable implication" in this context "means a clear or necessary inference." *Charlotte Russe's* prices "did not carry an implication clear enough to derogate [the supplier's] product for purposes of a disparagement claim." *Swift*, at *10.

⁴ *Id.* at *9-10 (citing *E.piphany*, 590 F. Supp. 2d at p. 1253) (internal quotations omitted).

⁵ Although mere claims of superiority of the defendant's product are not sufficiently specific, if a defendant has made a false statement that its product is the "only" one to offer certain features, the specificity requirement may be met because the false statement about the product's superiority "clearly and necessarily" implies that competitors' products are inferior. *Id.* at *9-13 (citing *E.piphany, Inc. v. St. Paul Fire & Marine Ins. Co.*, 590 F. Supp. 2d 1244, 1252-54 (N.D. Cal. Dec. 16, 2008)).

⁶ *Id.* at *13, *9 (quoting *Blatty v. New York Times Co.*, 42 Cal. 3d 1033, 1044 (1986)).

⁷ *Id.* at *9, *13 (quotations omitted).