

**SURVEY OF INSURANCE CONTRACTS OF MICHIGAN COMPUTER
AND SOFTWARE FIRMS - WILL THEY COVER SOFTWARE-RELATED
INTELLECTUAL PROPERTY LITIGATION ?**

By

**Proprietary Rights Committee
Computer Law Section
State Bar of Michigan**

Chairperson

**David R. Syrowik
Brooks & Kushman P.C.
Southfield, Michigan**

Committee Members

**Maria Franek
Mitchell A. Goodkin
William M. Hanlon
Ronald M. Nabozny**

**State Bar of Michigan
61st Annual Meeting
September 18, 1996**

THE SURVEY

Objectives and Background

The Proprietary Rights Committee of the State Bar of Michigan's Computer Law Section conducted a survey to determine whether the insurance contracts of Michigan computer and software firms would cover software-related litigation expenses and damages if and when such companies are sued for patent, trademark, copyright or trade secret infringement.

Typically, coverage, if found, will be found under the insured's commercial general liability (CGL) insurance policy. The operative language which most frequently triggers coverage for patent, copyright and trademark infringement and unfair competition claims is the "advertising injury" provision found within the "Broad Form Endorsement" riders. The insured's excess or umbrella policy, as well, may also be relevant.

The trend has been that computer companies are seeking and enforcing their intellectual property rights in response to increasing competitiveness in the worldwide computer industry. Insurance companies, underwriters, claims adjusters and even attorneys, are oftentimes unfamiliar with insurance exposure for intellectual property claims. The significant cost of defending infringement suits has led many computer and software manufacturers and companies that serve the computer industry, to scrutinize more carefully their standard form insurance policies. The article of Appendix A attached hereto discusses the above-noted trends in some detail.

Survey Design

The Michigan Technology Counsel maintains a database of Michigan computer and software firms entitled "Michigan Computer Directory." Each firm listed in the database was requested to provide copies of their current CGL policy, together with any excess or umbrella policies. The Committee promised to maintain the confidentiality of their policies and further allowed them to delete any confidential terms from their policies.

Results

Based on the mass mailing to the firms located in the Michigan Computer Directory, the Committee received 20 CGL policies and 1 umbrella policy. A common definition of "advertising injury" was as follows:

Injury arising out of one or more of the following offenses committed in the course of advertising your goods, products or services:

1. Oral or written publication of material that slanders or libels a person or organization or it disparages a person's or organization's goods, products or services;
2. Oral or written publication or material that violates a person's right of privacy;
3. Misappropriation of advertising ideas or style of doing business; or
4. Infringement of a copyright, title or slogan.

Another "advertising injury" definition is as follows:

Advertising injury means injury, other than bodily injury or personal injury, arising solely out of one more of the following offenses committed in the course of advertising of your goods, products or services:

1. Oral or written publication of advertising material that slanders or libels a person or organization;
2. Oral or written publication of advertising material that violates a person's right of privacy;
3. Infringement of copyrighted advertising materials or infringement of trademark or service marked titles or slogans.

Still another definition of "advertising injury" is as follows:

Advertising injury offense means any of the following offenses:

1. Libel or slander;
2. Making known to any person or organization written or spoken material that belittles the products, work or completed work of others;
3. Making known to any person or organization written or spoken material that violates an individual's right of privacy;
4. Unauthorized taking or use of any advertising material, slogan or title of others.

In the same policy in which this "advertising injury" definition appeared, the following was included under "exclusions":

1. Intellectual Property. We won't cover injury or damage that results from the actual or alleged infringement or violation of any of the following rights or laws:
 - a. copyright,
 - b. patent,
 - c. trade dress,
 - d. trade name,
 - e. trade secrets,
 - f. trademarks,
 - g. other intellectual property rights or laws.

But we won't apply this exclusion to bodily injury or property damage that results from your products or completed works.

Consequently, as noted above, while the definition of "advertising injury" can vary from policy-to-policy, the definition of "advertising injury" generally tracks or follows the 1986 definition of "advertising injury" as set forth on page 3 of the article of Appendix A. As noted therein, the terms "piracy" and "unfair competition" were deleted from the 1986 definition.

There also seems to be some effort to specifically exclude intellectual property litigation from insurance policies.

Legal Update

As noted in the article of Appendix A, 35 U.S.C. § 271(a) of the Patent Statute was amended to provide:

. . . Whoever without authority makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent therefor, infringes the patent.

Pub. L. 103-564 § 533(a) which expanded the definition of infringement under § 271(a) to include offers to sell patented inventions became effective as of Jan. 1, 1996.

In the case, *Everest & Jennings, Inc. v. American Motorists Insurance Co.*¹, the Court explained the rationale for its denial of the defense or indemnity to claims of direct patent infringement under advertising injury provisions covering "misappropriation of advertising ideas or style of doing business" by stating that there was no causal connection between the alleged infringement and the insured's advertising. The Ninth Circuit affirmed the District Court's holding that the insurance company had no duty to indemnify or defend the case stating that the plaintiff failed to demonstrate even a potential causal connection between its "advertising activities" and another's patent infringement claim.

In another recent case, *Simply Fresh Fruit, Inc. v. Continental Insurance Co.*², the Court similarly allowed an insurer to refuse to defend actions for misappropriation of trade secrets and patent infringement. The court stated again that there was no causal connection between the "advertising injury" and the insured's "advertising activities" and, consequently, there was no coverage. In other words, for there to be coverage, the "advertising injury" must be committed in the course of the insured's advertising of its goods, products, or services.

¹ 23 F.3d 226 (9th Cir. 1994).

² 84 F.3d 1105 (9th Cir. 1996).

However, as noted above, the amendment to § 271(a) of the patent statute now provides a distinct and independent basis for liability which, in many fact scenarios, will have a clear nexus to the insured's advertising activities at least with respect to patent infringement.

Finally, in the case *Sentex Systems, Inc. v. Hartford Accident & Indemnity Co.*,³ the Court held that a trade secret misappropriation suit which related to marketing such as customer lists, sales and marketing techniques and other inside information was covered by liability insurance. In particular, such trade secrets misappropriation fell under the "misappropriation of advertising ideas" clause of the "advertising injury" provision of the CGL policy.

Miscellaneous

By letter dated June 26, 1996 (Appendix B), the Chairperson of this Committee supplied information regarding intellectual property infringement insurance coverage. In the materials enclosed with the letter, the insurance industry's position with respect to CGL policy coverage for patent infringement became abundantly clear:

Doesn't my Company's Comprehensive General Liability (CGL) Policy Include Coverage for Patent Infringement?

Most likely not. There have been recent cases in which this coverage has been tested. The majority of these cases have been adjudicated with a determination that there is *not* coverage for patent infringement under the CGL policy. Insurance companies generally maintain that the CGL policy was never intended to cover patent infringement liability. A number of insurers are revising their policy language to make it more clear that the CGL policy *does not* cover patent infringement claims. If you are relying on the CGL policy for intellectual property coverage, you should consider these questions:

- ☞ Is my CGL limit of liability adequate to cover my intellectual property exposure?

³ 52 BNA's PTCJ 466 (9th Cir. 1996).

- 👉 Am I diluting my CGL coverage so that it will not be available for the primary risks it is intended to cover?

CONCLUSION

If one is sued for patent infringement based on allegedly wrongful conduct engaged in after January 1, 1996, the insured should promptly tender claim for coverage of such patent infringement law suit. Any prior denial of coverage for such claims should be revisited and a re-tender of such claims should be made for patent violations that are alleged to continue after January 1, 1996.

Until case law in this area becomes better developed, the effort to establish the right to a defense of patent or other intellectual property infringement claims will continue to encounter stiff opposition from the insurer's coverage counsel.

Also, counsel for the insured will have to be creative in that the words "piracy" and "unfair competition" have been eliminated from the definition of "advertising injury" as noted by the survey.

APPENDIX A

APPENDIX B

C:\DRS\SURVEY.96 -- KATHY 6/24/96
9/11/96
9/13/96