



THE NEXUS REQUIREMENT AND THE FATAL INJURY:  
DOES AN OFFER TO SELL AN INFRINGING PRODUCT  
GIVE RISE TO A DUTY TO DEFEND UNDER A CGL?

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Abstract

Case law in the area of patent infringement has held that patent infringement cannot occur in the course of an insured's advertising activities as a matter of law. In 1996, the United States added "offer to sell" as one of the enumerated offenses of direct patent infringement to 35 U.S.C. §271(a). Since that time, there has been little deviation or fluctuation from the above mentioned principle, especially in litigation where a patentee's search for insurance coverage from their CGL policies "Adverting Injury" provision. This Comment discusses the necessity of the court system to reexamine the modification to 35 U.S.C. §271(a), specifically, the impact of the addition of "offer to sell" as an enumerated offense of patent infringement. Additionally, this Comment proposes that courts should acknowledge that when offering for sale a potentially infringing device is the act of patent infringement, alleged infringers should be entitled to secure financial assistance from their CGL policy issuers for the costs associated with the duty to defend their infringement claims.

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INTRODUCTION

Imagine Ernie Entrepreneur pursuing the American dream of economic freedom and corporate independence by opening his own manufacturing business. He intends to “re-design” the wheel in the saw-blade industry. The young entrepreneur believes *his* saw-blade design can cut through anything without ever dulling the blade. After a “good-faith” search of issued patents to ensure that his blade does not infringe another’s invention, Ernie manufactures a single prototype to determine the saw blade’s acceptance among the saw-blade community. Traveling from city to city, Ernie finds that his new saw blade has exceptional appeal among commercial contractors. While in the City of Atlantis, Ernie is confronted by a representative of a company who alleges that Ernie’s saw-blade design infringes the company’s patent. Subsequent litigation ensues and in a timely fashion, Ernie enlists the help of his insurance carrier for his defense. To his disappointment, Ernie’s insurance company informs him that his Commercial General Liability (“CGL”) policy does not expressly include or implicitly provide coverage for lawsuits alleging patent infringement.

The above scenario has left young Ernie Entrepreneur to adjudicate and pay any legal expenses and judgments for which he may be found liable. This is typically the case for instances of direct patent infringement. The judicial system views the action that triggers the infringement of a patent as the same action that triggers the injury for purposes of insurance indemnification.<sup>1</sup>

This Comment examines the modern judicial rulings that constitute the recent judicial trend, which has been to deny insurance coverage to alleged patent infringers who look for litigation and damage cost coverage from their CGL policy. This Comment also seeks to expose the illogical holdings that are at the root of this trend. Recent modifications to the Patent Act seemingly broaden an insurer’s duty to defend a policyholder accused of committing patent infringement. Thus, under such modifications to the Patent Act, Ernie may find that certain acts of advertising his “infringing” invention entitle him to turn to his CGL policy provider for the costs of defending his claim. This Comment suggests that a liability-incurring injury should be recognized as occurring once an infringing device or process is advertised for commercial purposes by the alleged infringer. Arguably, once such an injury occurs, a patentee would incur damages, i.e., lost profits.

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<sup>1</sup> See DAVID A. GAUNTLETT, INSURANCE COVERAGE FOR INTELLECTUAL PROPERTY ASSETS § 10.02, at 10-12 (2000).

This Comment provides the following background material necessary to understand fully the current state of the law, as well as proposed changes that uncover and expose existing insurance coverage for defendants in patent infringement actions who hold CGL policies. Part I outlines some basic, foundational principles of Patent, Insurance, and Contract law. Part I.A introduces the concept of patent grants; Part I.B analyzes ways in which one may infringe a patent; Part I.C explains the high cost of patent litigation; and Part I.D illustrates different methods—some conventional and others non-traditional—by which parties to patent infringement actions fund the escalating costs of litigation. Part II begins with an analysis of the “advertising injury” provision of a standard CGL policy. Part II.B illuminates the necessity of a “nexus” between the infringement injury and the advertising activity, and Part II.C explores the maxims of contract interpretation that are the beginnings of exposing insurance coverage for patent litigation. Parts II.D through II.G not only expose the fallibility of the current decision making process but also discuss three unique approaches that can be applied to different factual scenarios to ensure that an insurer has a duty to defend an underlying allegation of patent infringement. Parts II.D through II.G also highlight some inclusive indicators that exist within the current insurance policy that affirmatively demonstrate that insurance coverage for patent infringement exists within current CGL policies. Finally, Part III proposes that because certain advertisements may be equated with an offer for sale, insurers should fund the defense of post-GATT allegations of patent infringement, so long as the insured has a standard Insurance Services Offices CGL policy with an “advertising injury” provision.

## I. PATENTS, INFRINGEMENT, AND HOW TO COVER THE COSTS OF LITIGATION

### A. *What Is a Patent?*

A patent is “a grant . . . of the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States.”<sup>2</sup> The United States patent system is rooted in the Constitution.<sup>3</sup> The Patent Clause of Article I, Section 8 provides that “Congress shall have Power . . . To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the

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<sup>2</sup> 35 U.S.C. § 154(a)(1) (2000).

Every patent shall contain a short title of the invention and a grant to the patentee, his heirs or assigns, of the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States, and, if the invention is a process, of the right to exclude others from using, offering for sale or selling throughout the United States, or importing into the United States, products made by that process, referring to the specification for the particulars thereof.

*Id.*; see also 5 DONALD S. CHISUM, CHISUM ON PATENTS § 16.02, at 16-6 (2000) (stating that the issuance of a patent by the United States Patent Office includes the right to exclude others from infringing on that which the patent is sought to protect).

<sup>3</sup> *In re Bergy*, 596 F.2d 952, 958 (C.C.P.A. 1979), *vacated in part sub nom. Diamond v. Chakrabarty*, 444 U.S. 1028 (1980), *aff'd sub nom. Diamond v. Chakrabarty*, 447 U.S. 303 (1980).

exclusive Right to their respective Writings and Discoveries.”<sup>4</sup> A patentee’s “right to exclude” others from his patented inventions was formally codified in 1790 when Congress enacted the first Patent Act.<sup>5</sup> The grant of a patent confers upon the patentee tremendous power to prevent others from infringing his patent rights during the term of the patent.<sup>6</sup>

Since the enactment of the Patent Act of 1790, Congress has amended the Act several times,<sup>7</sup> modifying the protections conferred upon patentees.<sup>8</sup> Today’s current statutory definition of a patentee’s rights was amended in 1996 to include protection against infringers who offer to sell a patented invention.<sup>9</sup> It follows statutorily<sup>10</sup> that “whoever without authority makes, uses, offers to sell, or sells a patented invention” commits direct patent infringement.<sup>11</sup>

### B. Infringement and How It Occurs

The statutory definition of direct patent infringement grants to a patentee the “right to exclude”<sup>12</sup> others from “making, using, selling, or offering to sell” a “process, machine, manufacture, or composition of matter”<sup>13</sup> that infringes the patentee’s patent.<sup>14</sup> Substantive statutory law states that liability for infringement attaches when one “makes” a patented device or invention.<sup>15</sup> Generally, it is the mere making

<sup>4</sup> U.S. CONST. art. I, § 8, cl. 8.

<sup>5</sup> See GAUNTLETT, *supra* note 1, § 10.01[B], at 10-3 (stating that the Patent Clause of the United States Constitution “has been interpreted to allow Congress to regulate patents”).

<sup>6</sup> *Id.* § 10.01[C][3], at 10-9 n.41. In accordance with the TRIPS Agreement, each patent term runs for 20 years from the application filing date. *Id.*

<sup>7</sup> See Patent Act of July 4, 1836 ch. 357, § 6, 5 Stat. 117; amended by Act of March 3, 1891, ch. 517, 26 Stat. 826; amended by 35 U.S.C. § 120 (1952) (current version 35 U.S.C. § 271 (2000)).

<sup>8</sup> 35 U.S.C. § 271 (2000); see GAUNTLETT, *supra* note 1, § 10.01[C], at 10-4. All of Congress’ subsequent revisions to the Patent Act have been in an effort to “simplify the laws and also to give the courts direction in handling patent cases.” *Id.*

<sup>9</sup> 35 U.S.C. § 271(a); see CHISUM, *supra* note 2, § 16.02[5][g], at 16-58. An amendment to 35 U.S.C. § 271 was effective on January 1, 1996 which added “offer to sell” as an exclusive right conferred to a patentee. *Id.*

<sup>10</sup> See 35 U.S.C. § 271(a).

<sup>11</sup> See CHISUM, *supra* note 2, § 16.02 at 16-6 n.2 (citing Griffin v. Keystone Mushroom Farm, 453 F. Supp. 1283, 1285 (E.D. Pa. 1978)).

[T]he patentee has a certain bundle of rights—*i.e.* to exclude others from making, using or selling the patented invention, and to control at the first stage the exceptions to that exclusion by the granting of licenses. Infringement of that right ‘is essentially a tort’ against the patentee and ‘implies invasion of some right of the patentee’ under the patent.

*Id.*

<sup>12</sup> 35 U.S.C. § 271(a); see *Coakwell v. United States*, 372 F.2d 508, 510 (1967). Whoever without authority goes against the express terms enumerated in 35 U.S.C. § 271(a) is liable to the patentee for patent infringement. *Id.*

<sup>13</sup> 35 U.S.C. § 101 (2000).

<sup>14</sup> 35 U.S.C. § 271.

<sup>15</sup> See *Coakwell*, 372 F.2d at 511. There is nothing more required for direct patent infringement than what is outlined in 35 U.S.C. § 271(a). *Id.*; see also *Neff Instrument Corp. v. Coahuilecs, Inc.*, 269 F.2d 668, 673 (stating that the mere manufacture of a single device protected by a patent is an infringement even though the device is neither used nor sold); see also CHISUM, *supra* note 2, § 16.02[3][a], at 16-34 (stating that careful statutory dissection reveals the use of the

of a patented invention which likely gives rise to the patentee's right to exclude and collect damages.<sup>16</sup>

A patentee may allege three different types of patent infringement: direct infringement; contributory infringement; or actual inducement.<sup>17</sup> Focusing the discussion on direct infringement, there are two possible types—literal infringement<sup>18</sup> and infringement under the doctrine of equivalents.<sup>19</sup> Literal infringement exists where “each limitation in the asserted claims [is] present in the accused device.”<sup>20</sup> However, some accused devices may fall outside the scope of the patent claims. The doctrine of equivalents applies where the differences between the patented device and the accused device are insubstantial, or where the equivalent element in the accused device performs substantially the same function in substantially the same way to achieve substantially the same result as the claimed element.<sup>21</sup> Thus, under the doctrine of equivalents, an alleged infringer can still be found liable for patent infringement.

### C. *Why the Need for Insurance Coverage?*

Since the creation of the United States Court of Appeals for the Federal Circuit (“CAFC”) in 1982, the number of patent infringement cases filed has increased over one hundred percent.<sup>22</sup> Not only is the number of cases increasing, but the cost of trying infringement cases is increasing as well. The cost of patent infringement

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disjunctive “or” in both 35 U.S.C §§ 154, 271 between the list of enumerated rights conferred to the patentee). “This codifies the long-standing rule that making a patented product without the use or sale will constitute infringement.” *Id.*

<sup>16</sup> *Id.* § 16.02[3][a], at 16-34 (citing *Whittemore v. Cutter*, 29 F. Cas. 1120, 1121 (C.C.D. Mass. 1813) (No. 17,600)). The court held that for every instance of patent infringement, “the legislature intended to make every one of the enumerated acts a substantive ground of action.” *Id.* Therefore, the manufacture of a single patented device “justified the award of at least nominal damages.” *Id.*

<sup>17</sup> See GAUNTLETT, *supra* note 1, § 10.01[C][2], at 10-5.

<sup>18</sup> See CHISUM, *supra* note 2, § 18.04[4][a], at 18-392 (noting some court decisions that have referred to an act of patent infringement as one of literal infringement “if the literal terms of the claim read on the accused product or process, [then] infringement is established without further inquiry into equivalence”).

<sup>19</sup> See CHISUM, *supra* note 2, § 16.02, at 16-4; see also BLACK'S LAW DICTIONARY 496-97 (7th ed. 1999) (defining the Doctrine of Equivalents as “[a] judicially created theory for finding patent infringement when the accused process or product falls outside the literal scope of the patent claims” and noting that “[t]he doctrine evolved to prevent parties from evading liability for patent infringement by making trivial changes to avoid the literal language of the patent claims”).

<sup>20</sup> *N. Am. Vaccine, Inc. v. American Cyanamid Co.*, 7 F.3d 1571, 1574 (Fed. Cir. 1993).

<sup>21</sup> *Warner-Jenkinson Co. v. Hilton Davis Chem. Co.*, 520 U.S. 17, 39-40 (1997); see also *Graver Tank Mfg. Co. v. Linde Air Prods. Co.*, 339 U.S. 605, 608-10 (1950) (stating that the doctrine of equivalents is a judge-made doctrine developed to allow the courts to not only deal with “devices that did not read upon the patent claim, but also to deal with infringers who do little more than minor modifications to existing patented devices or processes in an attempt not to have their infringements exposed”). “The theory is that ‘if two devices do the same work in substantially the same way, and accomplish substantially the same result, they are the same even though they differ in name, form, or shape.’” *Id.* at 608.

<sup>22</sup> See Jeffrey Dunsavage, *Insuring Intellectual Property Remains a Niche, Despite Rapidly Growing Need*, BUS. WIRE, Aug. 4, 1997 (stating that “the number of patent infringement lawsuits has more than doubled” from 1982 to 1997).

litigation from the time of filing of a complaint to the entry of final judgment can amass an expense budget for both parties in the seven-figure dollar range.<sup>23</sup> Recent studies indicate that the defense costs of patent infringement litigation can amount to over two million dollars.<sup>24</sup> The extreme cost of defending against a claim of patent infringement makes it difficult for most persons to adequately defend themselves in such suits. The high cost of patent enforcement litigation also prevents many persons, especially many small start-up companies,<sup>25</sup> from protecting (as well as defending) their most valuable assets—issued U.S. patents.<sup>26</sup> An unfortunate result of the high cost of litigation is that “most individuals or small businesses either turn a blind eye to what’s going on or come to some less-than-beneficial arrangement with the infringer.”<sup>27</sup>

#### *D. Litigation Funding Strategies*

Because “the intellectual property . . . of a company is now more valuable than its buildings, machinery, and fixed assets,”<sup>28</sup> the exorbitant costs of safeguarding and defending those intellectual property rights may force many companies to seek alternative forms of funding, rather than entirely absorb those costs themselves.<sup>29</sup> Some of the possible funding mechanisms for the “sport of kings”<sup>30</sup> include: (1) contingent fee arrangements;<sup>31</sup> (2) Alternative Dispute Resolution methods (e.g., arbitration);<sup>32</sup> (3) investors;<sup>33</sup> or (4) insurance.<sup>34</sup>

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<sup>23</sup> See James G. Gilliland, Jr., *The Use of ADR in IP Disputes*, INTELL. PROP. TODAY, February 1997, at 34.

<sup>24</sup> Audio tape: IP & Tech Law Monitor: The New New Media, THE RECORDER, held by American Lawyer Media, L.P. (March 26, 2001) (transcript on file with author).

<sup>25</sup> See *Deciding When And How To Enforce Your Patent—General Patent Corporation*, MONDAQ BUSINESS BRIEFING, LEXIS, Nexis Library, Mondaq Ltd. File; David Fanning, *Intellectual Property: Patently Obvious*, POST MAGAZINE, May 25, 2000, at 21. “Three recent cases in the US incurred defen[s]e costs ranging between \$11m and \$28m, and typical intellectual property insurance policies there limit individual claims to a maximum of \$1m.” Fanning, *id.*, at 21.

<sup>26</sup> See John Leming, *Lawsuits Prompt Need for Insurance Protection*, J. COM., June 7, 1999, at 12. “Patents can be a company’s most valuable intellectual property.” *Id.* “But protecting them can be costly.” *Id.*

<sup>27</sup> See Fanning, *supra* note 25, at 21.

<sup>28</sup> Melvin Simensky & Eric C. Osterberg, *The Insurance and Management of Intellectual Property Risks*, 17 CARDOZO ARTS & ENT. L.J. 321, 321 n.1 (1999) (citing J. Donald Francher, *How Insurance Can Reduce Intellectual Property Risks*, NAT’L UNDERWRITER, February 24, 1997, at 9).

<sup>29</sup> See Leming *supra* note 26, at 12 (suggesting that since 1988, patent insurance is now available to protect both the patentee from infringement of his patent as well as protect companies from allegations of infringement if that infringement is unintentional).

<sup>30</sup> See Frederic P. Zotos, *Unlocking the Potential for Innovation: Walk Softly and Carry a Big Stick*, INTELL. PROP. TODAY, LEXIS, Nexis Library, Intell. Prop. Today File (suggesting that given these astrological costs, patent litigation has duly earned the nickname “the sport of kings”).

<sup>31</sup> *Id.*

<sup>32</sup> See Scott H. Blackmand & Rebecca M. McNeill, *Alternative Dispute Resolution in Commercial Intellectual Property Disputes*, 47 AM. U.L. REV. 1709, 1710 (Aug. 1998) (“While ADR has become more prevalent in other areas of the law, many intellectual property attorneys do not regularly consider ADR as one of their options.”); Gilliland, *supra* note 23, at 34.

<sup>33</sup> See Zotos, *supra* note 30, at 26.

<sup>34</sup> See Simensky, *supra* note 28, at 321.

Similar in form and function to personal injury contingency-fee arrangements,<sup>35</sup> the patent bar is moving towards an acceptance of contingency-fee agreements as an alternative to the more traditional methods of fee payment to cover the astronomical costs of litigation.<sup>36</sup> The increasing number of patent infringement cases with award amounts exceeding the \$100-million mark have enticed and lured patent attorneys to take infringement cases on a contingent-fee basis. The reason is that the amount of money an attorney can recover may well surpass the amount he would have recovered had he taken the case on an hourly basis.<sup>37</sup> But all too often, many attorneys and firms balk at contingent-fee cases, due in large part to the enormous amount of time, effort, and expense involved in a patent case.<sup>38</sup>

Arbitration is a second option for “[p]eople with problems, like people with pains, [who] want relief, and they want it as quickly and inexpensively as possible.”<sup>39</sup> A noteworthy benefit of electing arbitration over conventional courtroom justice is that arbitration, when conducted with skill and experience, should cost no more than fifty percent of what a traditional courtroom proceeding would cost.<sup>40</sup> The lower out-of-pocket costs of arbitration, in conjunction with potentially high awards in patent infringement suits, lures more attorneys to reach an accord in a patent infringement dispute through the process of arbitration.<sup>41</sup>

A third option to funding the sport of kings is to solicit investors.<sup>42</sup> In some instances, an investor may decide to put forth a portion of the funding capital after evaluating the case’s potential for yielding a satisfactory return on that investor’s investment.<sup>43</sup> Alternatively, a patentee may agree to give a potential investor an interest in the patent royalties at the conclusion of the litigation.<sup>44</sup>

A final option is the availability of insurance coverage. There are two prevalent insurance coverage options—patent insurance coverage<sup>45</sup> or coverage within the “advertising injury” provision of a CGL policy.<sup>46</sup> Patent insurance attempts to fill a

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<sup>35</sup> See *Zotos*, *supra* note 30, at 26 (stating that “the patent bar is increasingly looking to the time-honored practices of the personal injury bar for a solution” to combat the rising cost of patent litigation).

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> See *Blackmand & McNeill*, *supra* note 32, at 1723.

Even when the case has a good chance of a favorable outcome, many lawyers and firms simply are not in a position to commit to an extensive outlay over a lengthy period of time. For this reason, individual plaintiffs often have a great deal of trouble finding representation on a contingent-fee basis.

*Id.*

<sup>39</sup> *Id.* at 1711 (quoting former Chief Justice Burger).

<sup>40</sup> *Id.* at 1725.

<sup>41</sup> *Id.* at 1723-25.

<sup>42</sup> See *Zotos*, *supra* note 30, at 26; see also *PEARL to Acquire Interest in LAN Technology Lawsuit*, CANADIAN CORP. NEWS, Feb. 24, 2000 [hereinafter *PEARL*].

<sup>43</sup> See *Zotos*, *supra* note 30, at 26.

<sup>44</sup> See *PEARL*, *supra* note 42 (stating that Intellectual Property Resource Corporation (IPRC) of Louisville, Kentucky “has been investing in patents and enforcing litigation since 1992” and has subsequently received a “10.5% carried interest in any proceeds from a patent issued in 1987 covering critical aspects of the local area network technology”).

<sup>45</sup> See *Simensky*, *supra* note 28, at 329-32 (discussing patent insurance policies, what is covered, what is not covered, scope of policies, and cost, as well as special considerations).

<sup>46</sup> *Id.* at 331-34 (outlining the “advertising injury” provision of a standard ISO issued CGL insurance policy).



need within the insurance industry. Corresponding to a large increase in intellectual property litigation, insurance companies, such as American International Group, Inc. (“AIG”) and Lloyd’s of London, have recently begun to offer insurance policies that cover losses due to alleged patent infringement.<sup>47</sup> Specifically, AIG’s policies can cover the majority of costs incurred in defending a suit, including damage awards, attorney costs, and settlement payments.<sup>48</sup> However, such policies do not encompass litigation costs associated with determining whether a person has willfully infringed another’s patent.<sup>49</sup> On the downside, the cost to a corporation to have such a policy can amount to over \$3,000 annually.<sup>50</sup>

The other source of insurance coverage for a corporate defendant in a patent infringement action can be found in the “advertising injury” provision of a CGL policy.<sup>51</sup> An in-depth examination of the current CGL “advertising injury” provision merged with an examination of the post-1996 change to the definition of direct patent infringement warrants a complete reversal in the judicial trend of denying coverage for the defense of patent infringement actions.

## II. OH COVERAGE, OH COVERAGE, WHEREFORE ART THOU?

### A. An “Advertising Injury”

Commercial enterprises looking to protect their investment with an insurance policy usually find that a CGL<sup>52</sup> policy provides the necessary protection that they desire.<sup>53</sup> Broad-form CGL policies are a form of liability insurance.<sup>54</sup> The purpose of these policies is to provide broad coverage for a range of risks that may befall the policyholder.<sup>55</sup>

Not until the second half of the twentieth century did insurance policy language standardize within the insurance industry.<sup>56</sup> The standardization of wording among insurance-industry contracts has become even more uniform in the area of

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<sup>47</sup> *Id.* at 329.

<sup>48</sup> *Id.*

<sup>49</sup> *Id.*

<sup>50</sup> *Id.* at 330.

<sup>51</sup> *Id.* at 331-32.

<sup>52</sup> See 2D ERIC MILLS HOLMES & MARK S. RHODES, HOLMES’ APPLEMAN ON INSURANCE § 1.15, at 65 (2d ed. 1996).

<sup>53</sup> *Id.*

<sup>54</sup> See BLACK’S LAW DICTIONARY 806 (7th ed. 1999) (defining liability insurance as “an agreement to cover a loss resulting from one’s liability to a third party . . . [t]he insured’s claim under the policy arises once the insured’s liability to a third party has been asserted”).

<sup>55</sup> See 2D HOLMES & RHODES, *supra* note 52, § 1.15, at 65. The insurance industry has divided available insurance policies to encompass two different forms of coverage—policies that afford coverage for a specific type of risk or injury and those that can encompass a wide range of risks or injuries. *Id.*

<sup>56</sup> See *id.* “Prior to 1940, each insurance company drafted its own CGL policy and considerable confusion resulted from the diverse language adopted by different insurers.” *Id.* “Consequently, the insurance industry voluntarily set about to standardize the CGL contract language.” *Id.*

property/casualty policies with the help of the Insurance Services Offices (“ISO”).<sup>57</sup> In 1976, the ISO included for the first time in their broad-form CGL Endorsements a provision for “advertising injury” liability coverage.<sup>58</sup> This “advertising injury” provision is the means by which many corporations have sought to find coverage for the costs of defending against IP actions initiated against them.<sup>59</sup>

Since the inclusion of this provision in 1976, the ISO’s CGL provision affording coverage for advertising injuries was changed once in 1986.<sup>60</sup> While the language of today’s policy<sup>61</sup> differs from that which emerged in 1976, the coverage afforded is still the same. An example of a typical “advertising injury” provision reads:

The company will pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages because of personal injury or advertising injury to which this insurance applies . . . arising out of the conduct of the named insured’s business.

‘Advertising injury’ means injury arising out of one or more of the following offenses:

. . . .

c. Misappropriation of advertising ideas or style of doing business; or

d. Infringement of copyright, title or slogan.<sup>62</sup>

. . . .

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<sup>57</sup> *Id.* at 66. (noting that the ISO is a “service organization whose membership consists exclusively of property/casualty insurers.”); *see also* GAUNTLETT, *supra* note 1, § 1.02[B], at 1-9 n.4 (“The ISO is an association of insurers that develops standard forms of policies.”).

<sup>58</sup> *See* CLARANCE E. HAGGLUND ET AL., CGL POLICY HANDBOOK § 10.01 at 10-3 (2001).

<sup>59</sup> *See* Simensky, *supra* note 28, at 331 (stating that while there was a period of years where intellectual property specialists based their assumption on case law that intellectual property suits were not covered by CGL policies, recent court decisions have found that many IP suits are covered within the “advertising injury” provision of a CGL policy).

<sup>60</sup> *See* GAUNTLETT, *supra* note 1, § 1.02[B], at 1-9. The language of the 1976 ISO policy provision encompassing advertising injuries “provided for coverage of ‘piracy [or] unfair competition’ committed or alleged to have been committed during the policy period.” *Id.* That phrase preceded the 1986 ISO policy language, which covers offenses of “misappropriation of advertising ideas or style of doing business.” *Id.*

<sup>61</sup> *See* HAGGLUND ET AL., *supra* note 58, § 10.01 at 10-4. While the ISO’s CGL policy has been updated since 1986, in 1998, 1992 and 1996, those updates have had no effect on the advertising injury provisions since the language has remained the same with regard to the sections affecting advertising injury coverage. *Id.* “[T]he 1998 policy narrows somewhat coverage for ‘advertisement’ and for intellectual property claims.” *Id.*; *see also* GAUNTLETT, *supra* note 1, § 1.01[D], at 1-8 (explaining that a more recent amendment to the ISO’s CGL policy regarding advertising injury coverage greatly modifies the wording of the of the 1986 policy). This 1998 ISO CGL policy (CG 00 01 07 98) has been approved by most Department of Insurances throughout the United States. *Id.* “[T]he ISO has stated that the language changes between the two policies were not intended to change the scope of coverage.” Simensky, *supra* note 28, at 332.

<sup>62</sup> *See* GAUNTLETT, *supra* note 1, § 1.01[B], at 1-4 n.2. “Commercial General Liability Coverage Form CG 00 01 (ed. 11-85).” *Id.*

[T]his insurance applies to “advertising injury” only if caused by an offense committed . . .

(2) in the course of advertising your goods, products or services.<sup>63</sup>

For CGL policyholders to find coverage within the advertising injury provision of their policy, the insured’s pending action must satisfy a three-part advertising injury test: “(1) [t]he insured must be engaged in an advertising activity; (2) the underlying allegations must fall within the scope of the named offense; and (3) the injury must arise out of an offense committed in the course of the policyholder’s advertising activity.”<sup>64</sup> Of the aforementioned parts of the test, the third prong, namely the establishment of a nexus between the “insured’s advertising activities and the offense charged,”<sup>65</sup> has been the most problematic for policyholders.<sup>66</sup>

### *B. The Question of Proximity or “Nexus” Requirement*

The ISO CGL advertising injury provision requires that the injury for which insurance coverage is sought “arise out of” the insured’s advertising activity.<sup>67</sup> A review of the principles of tort law reveals that the phrase “arise out of” is not the language of direct causation.<sup>68</sup> While there is great disparity among the federal district courts as to how close the nexus must be,<sup>69</sup> it is clear that there must be some “causal relationship” between the patent infringement and the advertising activity.<sup>70</sup> Without a reasonable nexus requirement, an argument could be made that “any harmful act, if it were advertised in some way, would fall under the grant of coverage merely because it was advertised.”<sup>71</sup> So long as one’s “direct patent infringement occurs in the course of the insured’s advertising activities, the causal nexus

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<sup>63</sup> See *id.* § 1.01[B], at 1-4 n.3. “Courts have held that the phrase ‘arising out of’ contained in most policies means ‘connected with,’ ‘growing out of,’ and other very broad, general and comprehensive terms.” *Id.* “To qualify as an ‘advertising injury’ which ‘arises out of’ a covered offense, the offense need only bear a ‘casual relationship’ to the advertising.” *Id.*; see also GAUNTLETT, *supra* note 1, § 10.05[A][1], at 10-34 (stating that the “term ‘arising out of’ means ‘incident to or having connection with’”). “As long as the direct patent infringement occurs in the course of the insured’s advertising activities, the causal nexus requirement of the ‘occur in the course of’ language is satisfied and coverage may properly arise.” *Id.*

<sup>64</sup> See GAUNTLETT, *supra* note 1, § 10.02, at 10-11.

<sup>65</sup> See *id.* § 10.05[A], at 10-34 (“Advertising injury coverage requires that the injury ‘arise out of’ an offense committed during the policy period in the course of the named insured’s advertising activities.”). “The causal nexus must be between the enumerated offense and the advertising activity.” *Id.* at 10-35.

<sup>66</sup> *Id.*

<sup>67</sup> *Id.* at 10-34.

<sup>68</sup> See GAUNTLETT, *supra* note 1, § 10.05[A], at 10-34. “California insurance coverage law, as well as that of the vast majority of states is clear: the term ‘arising out of’ is not language of direct causation.” *Id.*

<sup>69</sup> See *id.* § 2.04[A], at 2-13.

<sup>70</sup> See *id.* § 10.02, at 10-11.

<sup>71</sup> See *Bank of the W. v. Superior Court of Contra Costa County*, 833 P.2d 545, 559 (Cal. 1992).

requirement of the ‘occur in the course of language is satisfied and coverage may properly arise.’<sup>72</sup>

### *C. Issue to Defend in Light of Insurance-Contract Ambiguities*

Courts addressing issues of whether an insurance company must defend a policyholder’s action turn to basic principles of contract construction.<sup>73</sup> These principles direct the courts to look to the wording of the insurance contract to determine the parties’ intent.<sup>74</sup> The starting point for any question of contract interpretation is the language and words of the policy.<sup>75</sup> Comparison of the “intent” of the policy to the allegations of the complaint will determine if the insurer has an obligation to defend the insured’s claim.<sup>76</sup>

When determining the availability or lack of coverage for the insured’s claim, courts construe the insurance contract’s policy provisions “as a layperson would read them.”<sup>77</sup> Ambiguities arising during the interpretation of an insurance policy shall be construed against the insurer and in favor of the insured.<sup>78</sup> If an ambiguity persists while interpreting the policy’s provisions, ample case law,<sup>79</sup> as well as

<sup>72</sup> See GAUNTLETT, *supra* note 1, § 10.05[A][1], at 10-34.

<sup>73</sup> See 3 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 24.3 n.8 (Lexis 2001).

<sup>74</sup> See *Gray v. Zurich Ins. Co.*, 419 P.2d 168, 172 n.7 (Cal. 1966) (stating that “[c]ourts have . . . applied the doctrine of reasonable expectation to the interpretation of insurance contracts”) (citing *Atl. Nat’l. Ins. Co. v. Armstrong*, 416 P.2d 801, 809 (Cal. 1966)). “In interpreting an insurance contract we must consider the intent and reasonable expectations of the parties in entering into the agreement.” *Id.*

<sup>75</sup> See 4 ROWLAND H. LONG, THE LAW OF LIABILITY INSURANCE § 16.03 (Release No. 68 2001).

<sup>76</sup> See *Copart, Inc. v. Travelers Ins. Co.*, Nos. 99-17380, 99-17470, 2001 U.S. App. LEXIS 6140, at \*2-\*3 (9th Cir. Apr. 3, 2001) (citing *Peerless Lighting Corp. v. Am. Motorists Ins. Co.*, 98 Cal. Rptr. 2d 753, 759 (Cal. Ct. App. 2000)). An insurer must defend an action for the insured when the facts in the complaint disclose a bare potential for coverage. *Id.*; see also *Montrose Chem. Corp. of Cal. v. Canadian Universal Ins. Co.*, 861 P.2d 1153, 1157 (Cal. 1993) (“[A] liability insurer owes a broad duty to defend its insured against claims that create a potential for indemnity.” (citing *Horace Mann Ins. Co. v. Barbara B.*, 846 P.2d 792, 795 (Cal. 1993))).

<sup>77</sup> See *Peerless*, 98 Cal. Rptr. 2d at 759 (stating that the “clear and explicit” meaning of the ambiguous contractual provisions shall be interpreted by the court in their “ordinary and popular sense”); see also *Atlantic*, 416 P.2d at 809 (stating that courts must “evaluate not only [the insurer’s] contract form, but also [the insured’s] knowledge and understanding as a layman and his normal expectation of the extent of coverage of the policy”) (emphasis added); GAUNTLETT, *supra* note 1, § 10.04[B][3], at 10-30. It is the law of many jurisdictions of the country that the courts therein must interpret and give meaning to the words of an insurance policy as a “layman would read them and not as they might be analyzed by an attorney or an insurance expert.” *Id.* This may include using a dictionary to find the plain meaning associated with the terms of the insurance policy contract. *Id.*

<sup>78</sup> *Green Mach. Corp. v. Zurich Am. Ins. Group*, No. 99-3048, 2001 U.S. Dist. LEXIS 13378, at \*8 (E.D. Pa. Aug. 24, 2001).

<sup>79</sup> See *Westchester Resco, L.P. v. New England Reins. Corp.*, 818 F.2d 2, 4 (2d Cir. 1987) (“[A]mbiguities in an insurance policy are to be construed strictly against the insurer”); see also *Semmes Motors v. Ford Motor Co.*, 429 F.2d 1197, 1207 (2d Cir. 1970) (stating that “the rule of ‘construction against the draftsman’ . . . applies with particular force . . . ‘in cases where the drafting party has the stronger bargaining position’”); *Indiana Comprehensive Health Ins. Ass’n v. Dye*, 531 N.E.2d 505, 507 (Ind. App. 1988) (“When interpreting an insurance contract, and all other contracts of adhesion, . . . in cases of ambiguity where more than one reasonable interpretation is possible and

judicial maxims of contract interpretation,<sup>80</sup> provide support for the proposition that ambiguities should be construed against the insurer.<sup>81</sup> The existence of ambiguities in contractual provisions providing coverage for offenses which amount to advertising injuries has been the “source” or starting point for policyholders finding coverage for IP suits.<sup>82</sup>

It is well established that a duty to defend an action not only arises before an insurer’s duty to indemnify,<sup>83</sup> but also is broader than the duty to indemnify.<sup>84</sup> It follows that “if the underlying complaint alleges multiple claims, some of which are covered under the policy and some of which are not, the duty to defend arises if at least one of the claims in the complaint is within the policy’s coverage.”<sup>85</sup> Therefore, determining whether an insurer’s duty to defend has arisen, courts “line-up” the four corners of the insurance policy with the four corners of the complaint looking for *any* overlap.<sup>86</sup> If the court does establish any overlap, this alone gives rise to an insurer’s duty to defend and pay for an insured’s litigation expenses.<sup>87</sup> The action of the court pairing up the claim with the insured’s insurance policy, known as the “eight-corners rule,”<sup>88</sup> is the point where examination of coverage for patent infringement begins to emerge.

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especially where a coverage exclusion is involved, then the court must adopt the interpretation most favorable to the insured.”).

<sup>80</sup> See CORBIN, *supra* note 73, § 24.27.

<sup>81</sup> See *Atlantic*, 416 P.2d at 808; see also CORBIN, *supra* note 73, § 24.27 (“The ‘contra proferentem’ device is intended to aid a party whose bargaining power was less than that of the draftsman.”). The maxim of *contra proferentem* spells out a “general rule that an ambiguity will be resolved against the one who prepared the document.” *Id.* Also, since a “[d]isparity of bargaining power is likely to exist when a person applies for an insurance policy, . . . ambiguities in an insurance policy are generally to be construed strictly against the insurer.” *Id.*

<sup>82</sup> See William P. Kelly, *Insurance Law Annual: Scope of Advertising Injury Under Iowa Law in Commercial General Liability Policies*, 48 DRAKE L. REV. 625, 625-26 (2000) (stating that within the context of insurance law, advertising injury is a type of liability insurance, and due to the judicially determined ambiguous nature of the term “advertising injury,” corporations have sought to find coverage for there Intellectual Property suits within the provision).

<sup>83</sup> *Id.* at 627.

<sup>84</sup> See *Montrose Chem. Corp. of Cal. v. Canadian Universal Ins. Co.*, 861 P.2d 1153, 1157 (Cal. 1993).

<sup>85</sup> See *Ryland Group, Inc. v. Travelers Indem. Co. of Ill.*, NO. A-00-CA-233 JRN, 2000 U.S. Dist. LEXIS 21412, at \*12 (W.D. Tex. Oct. 25, 2000).

<sup>86</sup> *Id.* at \*11-12.

<sup>87</sup> See *Montrose*, 861 P.2d at 1157. “The determination whether the insurer owes a duty to defend is made in the first instance by comparing the allegations of the complaint with the terms of the policy.” *Id.* “For an insurer, the existence of a duty to defend turns not upon the ultimate adjudication of coverage under its policy of insurance, but upon those facts known by the insurer at the inception of a third party lawsuit.” *Id.* “Hence, the duty ‘may exist even where coverage is in doubt and ultimately does not develop.’” *Id.*

<sup>88</sup> See *Ryland*, 2000 U.S. Dist. LEXIS 21412, at \*12-13 (“[W]here the complaint does not state facts sufficient to clearly bring the case within or without the coverage, the general rule is that the insurer is obligated to defend if there is, potentially, a case under the complaint within the coverage of the policy.”). “Stated differently, in case of doubt as to whether or not the allegations of a complaint against the insured state a cause of action within the coverage of a liability policy sufficient to compel the insurer to defend the action, such doubt will be resolved in the insured’s favor.” *Id.*

*D. Progression from Coverage—to No Coverage—Back to Coverage*

Judicial decisions of the past decade mirror case precedent and the growing trend,<sup>89</sup> which avoids stretching the reach of CGL policies to policyholders sued for acts of alleged patent infringement.<sup>90</sup> One case that is alleged to have initiated the trend in favor of insurers is *Bank of the West v. Superior Court of Contra Costa County*.<sup>91</sup> Even though *Bank of the West*<sup>92</sup> involved insurance coverage for petitioner's unfair business practices,<sup>93</sup> the court in dicta outlined maxims of CGL advertising injury coverage afforded for IP suits. These maxims have been at the foundation of the judicial decision-making process in the area of advertising injury coverage for IP suits. In addition to spelling out an IP injury's nexus requirement,<sup>94</sup> one sentence of this heavily cited 1992 case ruled out all possibility that future litigants would find coverage for patent infringement litigation within an insured's CGL policy advertising injury provision.<sup>95</sup> The sweeping statement by the justices of the Supreme Court of California is just one of a limited number of fact-specific decisions that insurers have relied on to preclude coverage for most patent infringement claims.<sup>96</sup>

The *Bank of the West* holding was furthered and strengthened by a Ninth Circuit decision less than two years later in *Iolab Corp. v. Seaboard Surety Co.*<sup>97</sup> Unlike *Bank of the West*, the underlying litigation of *Iolab* involved indemnification for a settlement paid for a prior act of patent infringement.<sup>98</sup> Although *Iolab* and

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<sup>89</sup> See Jason A. Reyes, Note, *Patents and Insurance: Who Will Pay for Infringement?* 1 B.U. J. SCI. & TECH. L. 3 (1995) (outlining a linear progression of increasing denial of coverage afforded to insured's by the courts interpreting the insured's CGL policy for coverage in patent litigation). The trend began in the year 1988 with the case *Aetna Casualty v. Watercloud* granting coverage for a patent issue and culminates in 1994 with *Intex Plastics v. United National Insurance* denying coverage within the CGL policy. *Id.*; see also David A. Gauntlett, *Patents and Insurance: Who Will Pay for Reimbursement?* 4 B.U. J. SCI. & TECH. L. 6 para. 1 (1998) (introducing the article with the proposition that up until 1996, many of the patent infringement cases that were litigated in the United States were not decided in favor of the policyholder).

<sup>90</sup> See *Simply Fresh Fruit v. Cont'l Ins. Co.*, 94 F.3d 1219, 1223 (9th Cir. 1996) (holding that the defendant insurer was not obligated to defend the plaintiff policy holder in actions of patent infringement); see also *St. Paul Fire & Marine Ins. v. Advanced Interventional Systems*, 824 F. Supp. 583, 586 (E.D. Va. 1993) (holding that "patent infringement does not fall within the scope of 'advertising injury,' . . . even though the insured advertises the infringing product, if the claim of infringement is based on the sale or importation of the product rather than its advertisement").

<sup>91</sup> 833 P.2d 545, 551 (Cal. 1992) (holding that insurance policies covering advertising injuries provide coverage only for claims that arise out of common law unfair competition actions).

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at 560 (holding "that 'advertising injury' must have a causal connection with the insured's 'advertising activities' before there can be coverage").

<sup>95</sup> *Id.* at 561 (holding that patent infringement "does not 'occur in the course of . . . advertising activities' within the meaning of the policy even though the insured advertises the infringing product, if the claim of infringement is based on the sale or importation of the product rather than its advertisement" (citing *Nat'l Union Fire Ins. Co. v. Siliconix Inc.*, 729 F. Supp. 77, 80 (1989))).

<sup>96</sup> See Gauntlett, *supra* note 89, at 6 (stating that much of the recent decisions which have found against the interests of the policyholders were based on decisions that have "factually narrow precedents which fail to foreclose coverage for a variety of plausible scenarios").

<sup>97</sup> 15 F.3d 1500 (9th Cir. 1994).

<sup>98</sup> *Id.* at 1502. The plaintiff-appellant *Iolab* was sued in an original action by Dr. Ronald P. Jensen, a patent owner on an intraocular lens designed to replace a human's natural lens. *Id.* The

plaintiff Jensen settled on a figure lower than the court-assessed damages,<sup>99</sup> Iolab initiated a third-party action against Seaboard (their insurer) for compensation and indemnification<sup>100</sup> under the advertising injury provision of their CGL policy.<sup>101</sup>

As in *Bank of the West*, the Ninth Circuit held that “unless Dr. Jensen’s claim was that Iolab infringed his patent in its advertising, *in a manner independent of its sale* of the . . . lens, the Jensen” injury does not arise out of advertising.<sup>102</sup> Therefore, the court backed and strengthened its holding that “patent infringement cannot constitute an advertising injury,”<sup>103</sup> since patents are not infringed by advertising but instead by the enumerated acts of 35 U.S.C. § 271(a).<sup>104</sup> Under *Bank of the West*, Iolab’s advertising activity need only violate one of the enumerated acts that statutorily define patent infringement in order for coverage to be afforded.<sup>105</sup> The *Iolab* court emphasized that for an insured to find insurance coverage within a CGL’s advertising injury provision, the insured must show that the advertising activity caused the patent infringement.<sup>106</sup>

A final case emphasizing the trend followed by the judicial community regarding questions of CGL insurance coverage for patent infringement actions is *Simply Fresh Fruit v. Continental Insurance Co.*<sup>107</sup> The Ninth Circuit held true to form and followed the precedent spelled out five years earlier in *Bank of the West*. The court

Iolab/Jensen action culminated in August 1990 with a verdict for Jensen and the court finding that Iolab committed patent infringement. *Id.* The court awarded damages would have amounted to excess of \$33 million. *Id.* at 1503.

<sup>99</sup> *Id.* at 1503.

<sup>100</sup> See GAUNTLETT, *supra* note 1, § 10.04[A], at 10-24. “*Iolab*, however, is distinguishable as it is limited to direct patent infringement claims arising out of sale of infringing products.” *Id.* “The *Iolab* decision only involved the question of the insurer’s duty to indemnify for the sums the insured paid to settle the underlying direct infringement claims.” *Id.* “The *Iolab* court did not address the duty to defend the underlying direct infringement claim.” *Id.* “[T]he carrier must defend a suit which *potentially* seeks damages within the coverage of the policy.” *Montrose Chem. Corp. of Cal. v. Canadian Universal Ins. Co.*, 861 P.2d 1153, 1157 (Cal. 1993). “Implicit in this rule is the principle that the duty to defend is *broader* than the duty to indemnify; an insurer may owe a duty to defend its insured in an action in which no damages ultimately are awarded.” *Id.*

<sup>101</sup> See *Iolab Corp.*, 15 F.3d at 1503. The opinion lists all fifteen insurers of Iolab; four primary and eleven “excess insurers.” *Id.* Of the four primary insurers, Seaboard provided the longest term of coverage, spanning over eight years. *Id.*

<sup>102</sup> *Id.* at 1505-06 (emphasis added) (asserting that this conclusion was reached following the logic outlined in *Bank of the West*, which requires that the advertising injury have a causal connection to the “insured’s advertising activities” before a CGL policy’s advertising injury provision will offer coverage).

<sup>103</sup> *Id.*

<sup>104</sup> 35 U.S.C. § 271(a)(1994) (“[W]hoever without authority makes, uses, or sells any patented invention . . .”).

<sup>105</sup> *Id.*

<sup>106</sup> See *Iolab*, 15 F.3d at 1507 (dictating when the court explained that “Iolab’s claim with regard to the relationship between its advertising activities and the Jensen loss does not establish the causal nexus required by *Bank of the West*”). “Iolab fails to show that the Jensen loss was caused by its advertising rather than its infringement of Dr. Jensen’s patent.” *Id.* It was not the advertising that “caused” the infringement, because “advertising” is not one of the three enumerated forms of patent infringement listed in the Patent Act. *Id.*

<sup>107</sup> 94 F.3d 1219 (9th Cir. 1996). The underlying action for which Simply Fresh was attempting to have Continental Insurance indemnify it was a case of alleged patent infringement. *Id.* at 1220. The original action was commenced by Reddi-Made corporation against Simply Fresh Fruit for their alleged infringement of Reddi-Made’s patents for a fruit-cutting device. *Id.* at 1221.

held that as a matter of law, an insured's patent infringement cannot occur in the course of its advertising activities.<sup>108</sup> Again the court reasoned that because a patent infringement injury "could have occurred independent and irrespective of any advertising"<sup>109</sup> by the insured, the causal nexus requirement of *Bank of the West* was not satisfied.<sup>110</sup>

### *E. Coverage, Where Are You NOW?*

On January 1, 1996, an amendment to 35 U.S.C. § 271(a) added "offer to sell" as one of the enumerated ways in which an individual could infringe a patent.<sup>111</sup> This addition to 35 U.S.C § 271(a) was the result of U.S. codification of the General Agreement on Tariffs and Trade ("GATT").<sup>112</sup> It has been argued that with the addition of "offer to sell" as a fourth enumerated offense of direct patent infringement, "the nexus required between the alleged infringing activities and 'advertising' under Advertising Injury Coverage now should easily be met."<sup>113</sup> Reflective of the post-1996 change to the Patent Act,<sup>114</sup> Judge Conti held that the insured in *Everett Associates v. Transcontinental Insurance Co.*<sup>115</sup> had a reasonable expectation to assume insurance coverage for direct patent infringement, stating that the issued "CGL policy could reasonably be construed to cover claims for patent infringement."<sup>116</sup>

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<sup>108</sup> *Id.* at 1222.

<sup>109</sup> *Id.*

<sup>110</sup> See *Simply Fresh Fruit*, 94 F.3d at 1223 (It "is now the clearly established law in California . . . that the injury for which coverage is sought must be caused by the advertising itself." (citing *Microtech Research, Inc. v. Nationwide Mut. Ins. Co.*, 40 F.3d 968, 971 (9th Cir. 1994))).

<sup>111</sup> See *3D Sys., Inc. v. Aarotech Lab. Inc.*, 160 F.3d 1373, 1378 (Fed. Cir. 1998).

The amendment to § 271(a) represents a distinct change to the bases for patent infringement, because liability arose previously only as the result of an actual sale. . . . Little interpretation of this change as it relates to direct infringement under § 271(a) has been given, and no guidance on whether state law applies when determining if an 'offer to sell' has occurred.

*Id.*; *Everett Assoc., Inc. v. Transcontinental Ins. Corp.*, No. C-97-4308 SC, 1999 U.S. Dist. LEXIS 11792, at \*15-\*16 (N.D. Cal. June 28, 1999) (explaining that Congress' change to 35 U.S.C. § 271(a) may have changed the "landscape" of case law on which the defendant relies). The defendant in *Everett* was relying on *Bank of the West*, which was decided and adhered to up to this point. *Id.*

<sup>112</sup> EUGENE R. ANDERSON ET AL., *INSURANCE COVERAGE LITIGATION* § 16.05[c] (2d ed. 2000) (explaining that the adoption of GATT effectuated the changes in the Patent Act which increased the number of enumerated direct patent infringement violations from three to four).

<sup>113</sup> *Id.* Anderson et al. state that the case law decisions and precedent which hold that direct patent infringement cannot arise within the "advertising activities" of the insured and consequentially did not fall within the scope of the advertising injury provision of the insured's CGL policy should be revisited and questioned. *Id.* The pre-1996 litigation's holdings may have little value to new litigation involving alleged patent infringement since the "nexus" gap seems to have been minimized. *Id.*; see Kelly, *supra* note 82, at 630-31. "[T]he explanation that [an] injury must merely 'arise out of the advertising activities 'suggests a minimal, tangential connection between the injury and the advertising.'" *Id.* "Courts gave 'advertising,' 'arise out of,' and 'offense' a fairly broad construction allowing many claims to be defended under the language of the 1973 form." *Id.*

<sup>114</sup> 35 U.S.C § 271(a) (2000).

<sup>115</sup> No. C-97-4308 SC, 1999 U.S. Dist. LEXIS 11792 (N.D. Cal. June 28, 1999)

<sup>116</sup> *Id.* at \*7.



In the underlying action,<sup>117</sup> Everett Associates was sued for patent infringement.<sup>118</sup> Subsequently, Everett sought the costs of its defense against the underlying action from its insurance carrier, Transcontinental. Transcontinental, however, denied that it had a duty to defend Everett or indemnify Everett for the patent infringement action.<sup>119</sup> The court held that “whether the policy language can be interpreted to cover patent infringement claims depends on a two-step analysis.”<sup>120</sup> First the court must determine if the language of the policy is ambiguous. Second, the court must look to the objectively reasonable expectations of the insured and determine if there was an underlying intent that the policy would cover the costs of defending against a patent infringement action.<sup>121</sup>

The first prong of the test has its origins in the California Supreme Court’s *Bank of the West* decision, which outlined the analysis and criteria that some courts currently use in determining the presence of ambiguities in the insurance policy language.<sup>122</sup> Grounding *Everett’s* decision on both the holdings of *Bank of the West* and *Lebas Fashion Imports*,<sup>123</sup> the court held that the insured’s advertising injury provision of its CGL policy was ambiguous.<sup>124</sup> The policy’s ambiguity was with respect to the coverage afforded by a “misappropriation of advertising ideas or style of doing business” because several of the terms, “from the point of view of a layman,”<sup>125</sup> could be assigned two or more reasonable definitions.<sup>126</sup>

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<sup>117</sup> Clark v. Everett Assoc., No. SA CV 97-351-GLT, 1998 U.S. Dist. LEXIS 22259 (C.D. Cal. Oct. 26, 1998).

<sup>118</sup> See *Everett*, 1999 U.S. Dist. LEXIS 11792, at \*2. The defendant *Everett* in the underlying action was sued by the plaintiff who alleged that defendant had “advertised, offered to sell, manufactured, and sold portable massage tables that infringed a patent owned” by the plaintiff Clark. *Id.*

<sup>119</sup> *Id.* at \*2-\*3.

<sup>120</sup> *Id.* at \*9. The court outlined the two-step analysis; first, if the insurance policy in question does not provide the coverage that the insured expressly seeks in its claim to the insurer, the court must determine if the language of the policy is ambiguous. *Id.* Secondly, if the language of the policy is found by the court to be ambiguous, then “the court must look to the objectively reasonable expectations of the insured to determine if the policy could be construed to cover patent infringement claims.” *Id.*

<sup>121</sup> *Id.*

<sup>122</sup> *Id.* at \*9-\*10 (“[A] court that is faced with an argument for coverage based on assertedly ambiguous policy language must first attempt to determine whether coverage is consistent with the insured’s objectively reasonable expectations. In doing so, the court must interpret the language in context, with regard to its intended function.” (citing *Bank of the W. v. Superior Court of Contra Costa County*, 833 P.2d 545, 551 (Cal. 1992))).

<sup>123</sup> *Lebas Fashion Imps. of USA, Inc. v. ITT Hartford Ins. Group*, 50 Cal. App. 4th 548 (1996). The *Lebas* court was forced to decide whether the provision of the insured’s CGL policy covering “advertising injuries” could encompass a non-enumerated tort of trademark infringement if it was found to have ambiguous language. *Id.* The plaintiff relied on the provision of his CGL policy that afforded coverage for offenses committed in the “misappropriation of advertising ideas or style of doing business.” *Id.* The *Lebas* court held that the “misappropriation” clause was in fact ambiguous to the insured and “could reasonably be construed to include claims for trademark infringement, another significant and expensive tort which is not specifically enumerated as an advertising offense.” *Id.*

<sup>124</sup> *Everett*, 1999 U.S. Dist. LEXIS 11792, at \*15.

<sup>125</sup> *Id.* at \*13. When analyzing the terminology of an insurance policy, the court should give the terminology its plain meaning and not the meaning that an attorney or an insurance expert would give to them. *Id.*

After concluding that the first part of the test was satisfied, the *Everett* court moved to the second prong of the test, attempting to resolve the ambiguity by “looking to the objectively reasonable expectations of [the insured].”<sup>127</sup> Prior case law examining this question has held that patent infringement “could not reasonably be construed to be an ‘advertising injury’ for purposes of a CGL policy.”<sup>128</sup> Litigation that involves an allegation of patent infringement must consequently be reexamined for a potential of coverage due to the addition of the infringing act of “offer[ing] to sell” to the Patent Act in 1996.<sup>129</sup> Since the complaint of the underlying *Clark* action went so far as to stipulate and charge that the defendant “offered to sell . . . products infringing [Clark’s patent],”<sup>130</sup> the court determined that the “[p]laintiff had an objectively reasonable expectation that the CGL policy would cover patent infringement claims for advertising a patented product.”<sup>131</sup>

*F. If It Was Never Excluded . . . It Must Be Included . . .*

Contained within a standard ISO-format CGL Insurance policy, a policyholder can expect to find five basic components or sections, one of which should be entitled “Exclusions and Exceptions.”<sup>132</sup> Standard coverage parts do not mean identical coverages that cannot be customized to meet the individual policyholder’s needs.<sup>133</sup>

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<sup>126</sup> *Id.* at \*13-\*14. The *Lebas* court found that the coverage stipulation in question contained three ambiguities: (1) misappropriation, (2) advertising idea, and (3) style of doing business. *Id.*

<sup>127</sup> *Id.*

<sup>128</sup> *Id.* at \*15.

<sup>129</sup> *Id.* at \*16. The mere fact that the litigation in taking place after the January 1, 1996 amendment of 35 U.S.C. § 271(a) does not automatically determine that the amended version of the statute is the applicable and controlling rule. *Id.* The amendment to the statute is applicable in this case because the underlying accusation of alleged patent infringement took place after January 1, 1996. *Id.*; see also GAUNTLETT, *supra* note 1, § 11.03[B], at 11-17 (noting that the decision in *Bank of the West* held that a patent infringement claim could not occur in the course of advertising activities because the infringing activity was based on the sale of the product rather than its advertisement; it is now worth noting that “[b]y virtue of the amendment to the Patent Act, the claim [of patent infringement] is based, at least in part, on the advertisement of the patented product”).

<sup>130</sup> See *Everett*, 1999 U.S. Dist. LEXIS 11792, at \*16.

<sup>131</sup> *Id.* at \*22. The court went on to hold that “the advertising injury provisions in the CGL policy could reasonably be construed to cover claims for patent infringement.” *Id.* The court reached this conclusion by finding that the “offer to sell” language in the Patent Act, which may permit claims of patent infringement based on advertising alone, could create the required causal connection [to] permit coverage of patent infringement claims under a CGL policy.” *Id.* at \*20.

<sup>132</sup> See HOLMES & RHODES, *supra* note 52, § 117.1 (explaining that the same five essential elements create a pattern within most standard form insurance contracts used today: (1) the *Declarations Page* (or “DEC” sheet); (2) *Insuring Agreements*; (3) *Exclusions and Exceptions*; (4) *Conditions*; and (5) *Definitions*).

<sup>133</sup> See HOLMES & RHODES, *supra* note 52, § 117.1.

For example, ISO maintains five basic coverage parts, 73 countrywide endorsements, and 118 state-specific endorsements for the Homeowners line alone. With this variety of standard coverage parts, insurers can write Homeowners insurance for an apartment renter in Brooklyn who owns a large collection of art, a condo owner in Duluth who has installed a sauna and burglar alarm and wants high levels of liability coverage, or a homeowner in Palo Alto who has a swimming pool and tennis courts—all using ISO coverage parts.

The exclusion section's purpose is to eliminate "certain events or conditions from coverage" of the insurance policy's coverage.<sup>134</sup> As aforementioned, in the 1930's, the CGL policy was developed and written as a liability policy to provide coverage for a wide-range<sup>135</sup> of "accidents" or "occurrences."<sup>136</sup> It is in the exclusion's provision of the ISO's CGL form contract that an insurer may amend or customize coverage for the individual insured.<sup>137</sup>

With that in mind, "if the insurers desired to avoid any potential for coverage of patent infringement lawsuits, they could have sought to expressly exclude patent infringement actions."<sup>138</sup> *Industrial Molding Corp. v. American Manufacturers Mutual Insurance Co.*<sup>139</sup> supports the proposition that if an insurer meant to omit an area from the coverage of a CGL policy, then the insurer would enumerate any deletions within the Exclusion section of the issued policy.<sup>140</sup>

*Union Insurance Co. v. Knife Co.*<sup>141</sup> provides additional support for the proposition that a CGL policy is all encompassing with the exception of the enumerated exceptions. After the defendant corporation was sued in the underlying action for trademark infringement, the plaintiff sought a declaratory judgment as to whether it had a duty to defend under terms of the CGL insurance policy.<sup>142</sup> The court held that:

If the drafters of this insurance policy wanted to limit their exposure to 'suits arising under the common law tort of misappropriation' or to exclude exposure for 'actions involving trademarks,' it would have been a simple

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*Id.*

<sup>134</sup> BLACK'S LAW DICTIONARY 586 (7th ed. 1999).

<sup>135</sup> See Kelly, *supra* note 82, at 630-31 (stating that the addition of the advertising injury provision to the CGL policy "was originally sold to 'many thousands of policyholders with the promise of providing even 'broader' coverage than already provided by 'comprehensive' general liability insurance policies'").

<sup>136</sup> See HOLMES & RHODES, *supra* note 52, § 117.1.

Whereas insurance coverage generally can be written to cover all risks or only specified risks, all liability insurance by custom in the insurance industry provides all-risk coverage. In the 1930s, the insurance industry developed comprehensive liability insurance coverage to prevent overlapping of the specified risk approach and to minimize gaps in coverage.

*Id.*

<sup>137</sup> *Id.* § 6.5 n.16. The "[p]urpose of liability insurance contract is to provide protection against liability claims, and policy terms must be given interpretation consistent with that purpose, with limitations and exclusions strictly construed." *Id.*

<sup>138</sup> See GAUNTLETT, *supra* note 1, § 10.04[A], at 10-20; see also Simensky, *supra* note 28, at 333-34 (listing the following exclusion clause from an actual policy as representative of how to properly ensure that a policy does not cover patent infringement suits; "[T]his policy does not apply to any claim against the [insured] based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged infringement of patent . . ."); Gauntlett, *supra* note 89 (questioning the need for the addition of IP exclusions to the advertising injury provision of a CGL policy if the policy was never drafted to encompass IP suits in the first place).

<sup>139</sup> 17 F. Supp. 2d 633 (N.D. Tex. 1998).

<sup>140</sup> *Id.* at 637.

<sup>141</sup> 897 F. Supp. 1213 (W.D. Ark. 1995).

<sup>142</sup> *Id.*

matter to do so. In fact, previous policies apparently did expressly exclude actions for trademarks.<sup>143</sup>

While this Comment has focused on patent infringement, it naturally follows that broad-form CGL policies can be (and should be) “tailor-made.” This is accomplished through careful use and crafting of a policy’s Exclusions and Exceptions section because most often the specific torts<sup>144</sup> listed in the language of a CGL policy will contain an ambiguity that may be overly exploited.<sup>145</sup>

### *G. Money Is the Root of All That is Evil . . .*

In the preceding discussion of the cases mentioned in this Comment, it was noted that the underlying actions (which preceded the accused infringers’ claims for defense cost coverage) comprised more than just a claim for patent infringement.<sup>146</sup> The causes of action brought against alleged infringers suggest that the true injury suffered as a result of patent infringement is not in the mere “mak[ing], us[ing], offer[ing] for sale, or sell[ing]” the invention.<sup>147</sup> The true injury does not seem to arise until a patentee is deprived of lost profits, an injury more offensive than replication of a patented invention. It is worth repeating that “the intellectual property capacity of a company is now more valuable than its buildings, machinery, and fixed assets.”<sup>148</sup> The explicit and implicit value of a patent is too great to ignore—as evidenced by the fact that a number of patent litigation suits have involved sums in excess of \$100 million.<sup>149</sup> Implicitly, the monetary value of intellectual property, patents especially, can be deduced by an examination of the amount of money that companies are either willing to expend to protect patents from infringement, or if need be, to fund expensive lawsuits to stop others from infringing their patents.<sup>150</sup> A deviation from the substantive law of patents as the

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<sup>143</sup> *Id.* at 1216.

<sup>144</sup> See Kelly, *supra* note 82, at 630-31 (“[N]early all of the enumerated torts are intentional, and there is no indication the words used in the definition of advertising injury are words of limitation.”).

<sup>145</sup> See *Everett Assoc., Inc. v. Transcontinental Ins. Corp.*, No. C-97-4308 SC, 1999 U.S. Dist. LEXIS 11792, at \*8-\*13 (N.D. Cal. June 28, 1999) (explaining that just because coverage for a tort that is not listed within the enumerated torts in a CGL policy does not preclude the insurer’s duty to defend).

<sup>146</sup> See *Simply Fresh Fruit v. Cont’l Ins. Co.*, 94 F.3d 1219, 1220 (9th Cir. 1996) (stating that of the three claims filed by Reddi-Made, the claim filed in state court “contained allegations of: (1) misappropriation of trade secrets, (2) breach of contract, (3) violation of the Uniform Trade Secrets Act, and (4) intentional interference with economic advantage”); *Iolab Corp. v. Seaboard Sur. Co.*, 15 F.3d 1500, 1506 (9th Cir. 1994) (stating that Iolab was held liable in the underlying Jensen patent infringement action based and calculated on the corporation’s for-profit *sales* of the infringing lens); *Tradesoft Techs., Inc. v. Franklin Mut. Ins. Co.*, 746 A.2d 1078, 1083 (N.J. Super. Ct. App. Div. 2000) (stating that one of the underlying actions against Tradesoft Technologies Inc. was for unfair competition).

<sup>147</sup> 35 U.S.C. § 271(a) (2000).

<sup>148</sup> See Simensky, *supra* note 28, at 321.

<sup>149</sup> See Zotos, *supra* note 30, at 26.

<sup>150</sup> *Id.*

determinative factor for when a patent infringement injury arises is not even required.

Therefore, the judicial community needs to reevaluate the distinction it has established between the mere advertising of a patented device or process and an offer for sale.<sup>151</sup> “Many of the decisions against policyholders have primarily relied on factually narrow precedents which fail to foreclose coverage for a range of scenarios.”<sup>152</sup>

### III. CONCLUSION

Analogous to the question of whether a falling tree in the woods makes a sound is the question of when does patent infringement *really* injure the patentee? If one suggests that a patentee is truly not injured until an alleged patent infringer is about to commercialize a patentee’s invention, every altruistic patentee will scream that a patent is worth much more to them than its weight in gold.

Both the Congressional beginnings of the patent statutes and the history of the Constitutional Convention in Philadelphia in 1787 reveal that our founding fathers “properly intended to encourage *economic* progress when they wrote into the U.S. Constitution the basis for the patent system.”<sup>153</sup> Therefore, remaining consistent with the intent of our founding fathers, the judiciary should recognize as well that another entrepreneur’s efforts in making a profit from a patentee’s invention is the *true* injury that should give rise to an insurer’s duty to defend.

The “fatal injury” which fulfills the nexus requirement, giving rise to an insurer’s duty to defend an insured against a patent infringement action, should be recognized as the mere act of advertising an infringing good. The reason for this is because an offer for sale is now an enumerated infringing act in the Patent Act. “Advertising an invention constitutes an offer for sale when it creates in the purchaser’s mind a reasonable belief that the invention is being offered for sale.”<sup>154</sup> A prerequisite to such cases will require courts to engage in a fact-specific determination of whether an alleged infringer’s advertising activity led to a reasonable belief that a device is being offered for sale;<sup>155</sup> creation of such a belief helps complete the causal-nexus analysis, triggering an insurer’s duty to defend.

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<sup>151</sup> 35 U.S.C. § 271(a).

<sup>152</sup> See Gauntlett, *supra* note 89, at 6.

<sup>153</sup> See Mondaq, *supra* note 25.

<sup>154</sup> See *Envirotech Corp. v. Westech Eng’g Inc.*, 904 F.2d 1571, 1576 (Fed. Cir. 1990) (“While there is no requirement that the purchaser have actual knowledge of the invention to invoke the on sale bar, what the purchaser reasonably believes the inventor to be offering is relevant to whether, on balance, the offer objectively may be said to be of the patented invention.”).

<sup>155</sup> See *generally* *Rotec Indus., Inc., v. Mitsubishi Corp.*, 215 F.3d 1246 (Fed. Cir. 2000). In determining what “constitutes an ‘offer[]’ as the term is used in §271(a),” the court looked to the common law of the United Kingdom for guidance; the “common law of contract does not limit the meaning of ‘offer for sale’ in the context of patent infringement.” *Id.* at 1251 (citing *Gerber Garment Tech. Inc. v. Lectra Sys. Ltd.*, 13 R.P.C. 383, 411-12 (United Kingdom Patents Court 1995)). Unlike the United Kingdom which has “held that mere advertising activities could infringe, even if the activities do not meet the common law definition of offer,” the Federal Circuit in *Rotec* “define[d] § 271(a)’s ‘offer to sell’ liability according to the norms of traditional contractual analysis.” *Id.* at 1252-53. Therefore, where an advertisement “is clear, definite, and explicit, and leaves nothing open

If an enumerated offense is alleged to have occurred in the course of advertising activity, and the offense occurred during the policy period, then the insurer may have a duty to defend so long as there is not a modified endorsement or definitional change contained within the policy that clearly excludes such coverage.<sup>156</sup>

Courts should put a stop to the trend of denying insurance coverage to innocent insureds in patent infringement actions. The advertising injury provision of Ernie Entrepreneur's CGL policy should cover his litigation costs.

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for negotiation, it constitutes an offer, acceptance of which will complete the contract." *Lefkowitz v. Great Minneapolis Surplus Store, Inc.*, 86 N.E.2d 689, 691 (Minn. 1957). Furthermore, "[w]hether in any individual instance a[n] . . . advertisement is an offer rather than an invitation to make an offer depends on the legal intention of the parties and the surrounding circumstances." *Id.*

<sup>156</sup> See P. L. Skip Singleton, Jr., *Justice for All: Innovative Techniques for Intellectual Property Litigation*, 37 IDEA 605, 617-18 (1997).