HUNTON& WILLIAMS

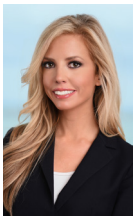
Lawyer Insights

March 27, 2017

The Disparagement Dilemma: Insurance Coverage for the Defense and Indemnity of Product Disparagement Claims

by Syed Ahmad, Andrea DeField and Katherine Miller

Published in Corporate Counsel


For decades, retailers and all other kinds of companies have faced suits alleging breach of contract, unfair trade practices or tortious interference. Typically, these companies are left to defend these suits and incur substantial defense costs without the benefit of insurance coverage because the claims are generally not covered under their commercial general liability policies. For some lucky insureds, however, courts have found coverage for these lawsuits where they include allegations of product disparagement—a covered "personal and advertising injury" under typical commercial general liability policies. For example, the Ninth Circuit recently affirmed a district court's ruling that a liability insurer had a duty to defend its insured based on only two to three isolated allegations of conduct that could be considered product disparagement even though the rest of the claims dealt with different theories of liability. See Millennium Laboratories, Inc. v. Darwin Select Ins. Co., No. 15-55227 (9th Cir. Jan. 27, 2017).

In Millennium, the Ninth Circuit relied on well-established insurance law requiring a liability insurer to defend a suit, if the allegations in the complaint could potentially be covered under the policy. The Court explained that the insurer should have realized that Millennium faced potential disparagement claims because the insurer knew that Millennium's sales team had allegedly told customers that a competitor's business was illegal and because it knew that Millennium's general counsel gave a presentation to sales representatives, which included a slide depicting the plaintiff and its compliance officer in body bags with the sounds of gunshots. Accordingly, the Ninth Circuit affirmed that the insurer was required to defend two lawsuits, notwithstanding that one of the complaints failed to include any allegations of disparagement.

Even where an insurer provides a defense based on the potential for coverage, however, it may reevaluate coverage at the time of settlement or judgment based on the facts established at trial or prior to settlement. In Rass Corp. v. Travelers Cos. , 90 Mass. App. Ct. 643 (Mass. Ct. App. 2016), the insurer did just that. While the insurer had provided a defense to its insured because of the potential for coverage, the insurer refused to contribute to settle the claim before trial. After the insured was forced to settle the case on its own, it filed suit against the insurer. The trial court held in favor of the insured, finding coverage for the settlement where the disparagement claim was based on the insured's email to a customer warning the customer that the plaintiff may attempt to illegally circumvent him and sell directly to the customer. The Massachusetts intermediary appellate court affirmed.

Other corporate insureds, however, have not been so lucky as courts across the country wrestle with the fact-specific analysis to determine whether product disparagement is alleged and covered by insurance. For example, in Wireless Buybacks, LLC v. Hanover Am. Ins. Co., CV CCB-16-0328, 2016 WL 7178299

(D. Md. Dec. 8, 2016), allegations that the insured was infringing its competitor's product were found to lack the requisite wrongful comparison so as to constitute disparagement.

In other cases, courts have relied on various exclusions that barred coverage. In Great Lakes Beverages, LLC v. Wochinski, No. 2016-AP-386, 2017 WL 218407 (Wis. Ct. App. Jan. 18, 2017), the insured sought coverage from its liability insurer based on allegations that it tortuously interfered with the plaintiff's business relationships by telling actual and prospective customers that a noncompete was in effect when it was not. The court found it was unnecessary to address whether the allegations amounted to disparagement because the breach of contract exclusion applied to defeat coverage. Similarly, in One Beacon American Insurance Co. v. City of Zion , 119 F. Supp. 3d 821 (N.D. Ill. 2015), the court likewise denied coverage based on the breach of contract exclusion. There, the city argued that coverage was triggered because the plaintiff alleged that a city representative made false statements regarding when a stadium would be built and that it was owed money from the plaintiff, slowing down construction. The court disagreed and held that the insurer did not owe coverage because all of the allegations arose out of the alleged breach of contract to build the stadium.

In Selective Way Insurance Co. v. Crawl Space Door System , 162 F. Supp. 3d 547 (E.D. Va. 2016), the court relied on a different exclusion, the policy's "failure to conform" exclusion, to likewise preclude coverage. That exclusion barred coverage for "personal and advertising injury" arising out of an insured's false statement about its own product. While the complaint did not include any direct allegations of disparagement, the insured argued that coverage for product disparagement was triggered by allegations that it advertised that its flood vents were "unparalleled" and provided more space for less money than the plaintiff's flood vents. The court found it unnecessary to determine whether these statements were disparagement because the "failure to conform" exclusion applied.

While these recent decisions provide some guidance on what allegations and factual circumstances may trigger coverage, it is clear that judicial treatment of coverage for product disparagement is far from uniform. Where a claimant has not alleged the tort of disparagement, corporate policyholders should still review each complaint for any allegations that may constitute disparagement—particularly allegations of unfair comparison. Allegations of disparagement, no matter how few, may trigger the insurer's duty to defend the entire lawsuit, saving the corporate defendant, and its counsel, from the expense of providing its own defense.

Syed Ahmad is a partner in Hunton & Williams LLP’s insurance coverage practice in Washington. He represents clients in connection with insurance coverage, reinsurance matters and other business litigation. He can be reached at (202) 955-1656 or sahmad@hunton.com. Andrea DeField and Katherine Miller are Miami-based associates in the firm’s insurance coverage practice. Their practice focuses on complex business litigation with an emphasis on insurance coverage and related coverage disputes. DeField may be reached at (305) 801-2465 or adefield@hunton.com, and Miller may be reached at (305) 801-2525 or kmiller@hunton.com.