

“Implied Disparagement” Triggers Coverage Under CGL Policy

By Peter Selvin¹

What constitutes “disparagement” of another’s products sufficient to trigger coverage under the personal injury of advertising injury portions of a CGL policy?

The Court of Appeal in *Travelers Property Casualty Company of America v. Charlotte Russe Holding, Inc.*, __ Cal.App. __ (2012) addressed that question in a decision issued by the Court on June 21.

In that case, Travelers’ insured, Charlotte Russe, was the exclusive sales outlet for Versatile’s “People’s Liberation” brand of apparel. According to Versatile, Charlotte Russe had promised to provide the investment and support necessary to “promote the sale of premium brand denim and knit products in order to encourage [its] customers to purchase such premium products at a higher price point at [its] stores.”

Versatile brought a lawsuit against Charlotte Russe claiming that Charlotte Russe had marketed Versatile’s products in a “fire sale” manner and at “close-out” prices. Versatile alleged that Charlotte Russe’s marketing practices not only violated the parties’ agreement but also would result in damage to and diminution of the People’s Liberation brand and trademark.

Charlotte Russe tendered the claim to Travelers, its CGL carrier. In support of that tender Charlotte Russe pointed to the fact that Versatile’s discounting claim was based on “public display of signs in store windows and on clothing racks announcing that People’s Liberation brand jeans were on sale” as well as on their “written mark-downs on individual People’s Liberation clothing items.” Charlotte Russe also supported its tender by pointing to an apparel industry expert affidavit (presumably offered by Versatile in the underlying litigation) to the effect that such markdowns and “dramatic price reductions[s] promoted in such a manner had the potential to have a *disparaging effect* on the People’s Liberation brand.” (emphasis added)

The Travelers’ policy contained both “personal injury” and “advertising injury” liability coverage. Both provide broad offense-based coverage for claims alleging injury arising out of “oral or written...publication of material that ... disparages a person’s or organizations goods, products or services...”

The trial court granted summary judgment to Travelers, finding no coverage under the policy. The trial court reasoned that in order to be covered Versatile’s claims must amount to actionable claims of trade libel.

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The Court of Appeal reversed, holding that Charlotte Russe's marketing practices could constitute an "implied disparagement" of Versatile's products and further that such a disparagement claim need not rise to the level of trade libel in order to be covered.

At the threshold, the Court held that for purposes of coverage analysis "disparagement" may be implied and that Charlotte Russe's marketing practices (which could have suggested to consumers that Versatile's products were lower-end merchandise) satisfied this requirement. As the court explained, "the question here ... is not whether the underlying claims expressly allege that the Charlotte Russe parties disparaged Versatile's products, but whether the allegations may be understood to accuse the Charlotte Russe parties of statements and conduct 'that ...disparages a person's or organization's goods, products or services...'"

This language reflects a growing trend of the appellate courts to find that the "disparagement" offense may be triggered even where the underlying plaintiff does not directly accuse the insured of such conduct in those terms.

This decision is the latest in a series of appellate decisions which have continued to expand the scope of what may be covered under the "disparagement" offense in CGL policies. In this regard several recent cases have found that disparagement may be implied for insurance coverage purposes where, for example, a vendor claims that it was the "only producer" a certain software product (*E.piphany, Inc. v. St. Paul Fire & Marine Ins. Co.*, 590 F. Supp. 2d 1244 (N.D. Cal. 2008)) or where it claims that its products are "more effective" or "superior" to those made by others (*Knoll Pharmaceutical Co. v. Automobile Ins. Co. of Hartford*, 152 F.Supp.2d 1026, 1036 (N.D.Ill. 2001)). More recently, the Court determined that there was "disparagement" and hence insurance coverage where a complaint alleged that the insured had "implied to the marketplace" that it had a superior right to use a certain trademark and thus by implication represented that the underlying plaintiff did not have the rights to that trademark. *Burgett, Inc. v. American Zurich Insurance Company*, 2011 U.S. Dist. LEXIS 135449 (E.D.Cal. 2011).

Although not cited in the *Charlotte Russe* decision, a recent federal court decision underscored essentially the same points. In *Michael Taylor Designs, Inc. v. Travelers Prop. Cas. Co. of Am.*, 761 F.Supp.2d 904 (N.D.Cal. 2011), the insured was sued by a former supplier for trade dress infringement. The former supplier alleged that the insured had improperly offered for sale "cheap synthetic knock-offs" of the supplier's wicker furniture products. The essence of the supplier's claim was damage to the reputation of its products that would result from consumers encountering the alleged knockoffs marketed by the insured and believing them to be products manufactured by the supplier.

The insured's liability carrier had declined to cover the insured until the supplier, in an amended complaint, had expressly alleged that the insured's conduct amounted to disparagement of the supplier's goods. The question presented in the case was whether the factual allegations of the original complaint were sufficient to give rise to a duty to defend, despite the claims having been couched in language of trade dress infringement rather than in terms of disparagement.

The court concluded that because the trade dress claim "raised the possibility of a disparagement claim" (761 F.Supp.2d at 904), the duty to defend was triggered. In this regard, the court noted that the plaintiff-supplier had essentially alleged damage to the reputation of its

products that would result from consumers encountering “cheap synthetic knock-offs” and believing them to be products manufactured and marketed by the supplier. 761 F.Supp.2d at 911.

The bottom line is that coverage opportunities are increasing for parties who may be sued by competitors, distributors or suppliers where the gravamen of the complaint speaks expressly or by implication to “disparagement”. As that term continues to be given expanded scope by the appellate courts, insureds should continue to press for coverage in these sorts of cases.