

Company's Prior Knowledge of Trademark Dispute Relieves E&O Insurer of Duty to Defend

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A California intermediate appellate court, applying California law, has held that an E&O policy provided no coverage for a lawsuit filed during the policy period when the suit arose from circumstances that occurred prior to inception of the policy and that the insured objectively should have known could lead to a claim. *American Int'l Specialty Lines Ins. Co. v. Continental Cas. Ins. Co.*, 2006 WL 2361451 (Cal. Ct. App. Aug. 16, 2006).

The insured company entered into a partnership to market certain online services using a logo that allegedly infringed on a trademark used by the underlying plaintiff. The plaintiff demanded that the company's partner cease and desist using the allegedly infringing mark in a December 1998 letter. The company admitted that its partner notified it of the matter in mid-January 1999. The parties subsequently entered into negotiations to resolve the matter, but were unsuccessful. The underlying plaintiff filed suit against the company and its partner on February 18, 1999.

The company later submitted an application for a specialty E&O policy to the insurer. The company initially answered in the negative an application question as to whether the company was aware of any circumstance "which may reasonably be expected to result in a claim being made against You." The company later supplemented its answer, informing the insurer of the existence of the trademark infringement case. In its supplement, the company identified the date of the alleged error or occurrence as December 1998.

The insurer subsequently issued a specialty E&O policy to the company with a policy period of February 12, 1999 to January 5, 2000, and a retroactive date of March 19, 1997. The policy stated that it would provide coverage for claims arising from a wrongful act committed between the retroactive date and policy inception date, but only if three conditions were met: (1) the written claim was first made against the company during the policy period, (2) the company did not know prior to the inception date of any circumstance "that could reasonably be expected to lead to the Claim," and (3) there was no other valid and collectible insurance for the claim. The policy also provided that it would treat as a single wrongful act all wrongful acts committed between the retroactive date and the end of the policy period that were "related by common facts,

circumstances, transactions, events and/or decisions."

The court held that the E&O insurer had no duty to defend or indemnify the company against the trademark suit. The court opined that the policy's use of the phrase "could *reasonably* be expected to lead to the Claim" required the application of an objective standard to determine whether the company's pre-policy knowledge of the trademark dispute negated coverage for the later lawsuit. Applying this standard, the court concluded that the complaint in the underlying action demonstrated on its face that coverage was not available because it alleged that the company and its partner began a business that infringed on the plaintiff's trademark and that the plaintiff demanded in December 1998 that the alleged infringement cease. The court determined that these allegations necessarily meant that the company knew of circumstances that could reasonably lead to a claim prior to the February 1999 policy inception date. Furthermore, the court added, the facts subsequently discovered indicated that the parties engaged in negotiations for a business solution to the dispute through February 16, 1999, which meant negotiations must have occurred from December 1998 to that date.

The appellate court rejected the company's argument that the underlying complaint was covered under the policy because it constituted a separate claim made during the policy period. The court reasoned that the lawsuit arose from the same circumstances as the pre-policy cease and desist letter, and that the alleged infringement accordingly constituted a single "wrongful act" under the E&O policy. The court concluded that there could be no coverage for related wrongful acts occurring during the policy period because the single wrongful act was treated as happening at the start of the chain of events, prior to policy's inception.