TRIPLE THREAT TO COVERAGE: THIRD CIRCUIT DEPARTS FROM THREE FUNDAMENTAL RULES IN APPLYING "PRIOR PUBLICATION" EXCLUSION

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Insurance Coverage Alert

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INTRODUCTION

Three well-established rules — (1) that policy exclusions are to be interpreted narrowly, (2) that an insurer has the burden to prove the applicability of an exclusion, and (3) that an insurer has a duty to defend as long as the underlying allegations are potentially within a policy's coverage — took a backseat in a recent decision by the United States Court of Appeals for the Third Circuit involving "personal and advertising injury" coverage.[1] In *Hanover Insurance Co. v. Urban Outfitters, Inc.*, --- F.3d ---, 2015 WL 6405763 (3d Cir. Oct. 23, 2015), the court applied a "prior publication" exclusion broadly and held that because the policyholder could not establish that an underlying complaint for trademark infringement specifically alleged new violations during the policy period, the insurer was relieved of its duty to defend. The decision represents an unfortunate departure from fundamental insurance coverage principles under Pennsylvania law. Had the court followed any one of these rules, the outcome arguably would have been a finding of coverage.

BACKGROUND OF THE *URBAN OUTFITTERS* CASE

The Navajo Nation sued clothing store Urban Outfitters and its affiliates for trademark infringement and other claims, alleging that Urban Outfitters "advertised, promoted, and sold its goods under the 'Navajo' and 'Navajo' names and marks." An insurance policy issued to Urban Outfitters contained a "prior publication" exclusion that provided there was no coverage "arising out of oral or written publication of material whose first publication took place before the beginning of the policy period," which was July 7, 2010. The underlying complaint alleged infringement "[s]ince at least March 16, 2009," but also alleged that "[s]ometime in early 2011, and possibly earlier, Urban Outfitters started a product line of 20 or more items containing the NAVAJO trademark." The underlying complaint also attached examples of allegedly infringing advertisements dated within the policy period. The district judge held that the insurer had no duty to defend Urban Outfitters, based on the "prior publication" exclusion.[2]

THE THIRD CIRCUIT'S DECISION

In affirming the district court's ruling, the Third Circuit departed from established Pennsylvania law in three ways.

Broadening of the "Prior Publication" Exclusion

Pennsylvania law requires that policy exclusions must be construed narrowly.[3] However, the Third Circuit employed a broad interpretation of the "prior publication" exclusion, and one largely detached from the actual language of the exclusion. The court stated, without reference to the policy language or any extrinsic evidence, that the "prior publication" exclusion "serves to limit the coverage for an ongoing course of wrongful conduct." [4] By expanding the inquiry beyond whether the same "material" had its "first publication" before the policy period (i.e., the language of the "prior publication" exclusion), the court impermissibly broadened the policy language in favor of the insurer.

Reversal of Burden of Proof

An insurer asserting a policy exclusion has the burden of proving that the exclusion is applicable.[5] In *Urban Outfitters*, the court implicitly required that a policyholder seeking a defense from its insurer must affirmatively establish that an exclusion does not apply, turning the traditional burden of proof on its head. According to the court's analysis, absent a specific allegation that the pre-publication advertisements were substantially different from advertisements during the policy period, the "prior publication" is presumed to apply. That approach leaves the policyholder vulnerable to losing otherwise valid coverage based on the incompleteness, vagueness, or ambiguity of the underlying complaint, effectively relieving the insurer of its burden of showing that the "prior publication" exclusion is actually applicable.

Narrowing of the Duty to Defend

As long as the underlying complaint alleges facts that are potentially within the policy's coverage, an insurer should be held to have a duty to defend.[6] In other words, the duty to defend is broader than the duty to indemnify.[7] When there is any doubt regarding an insurer's duty to defend, it must generally be resolved in favor of the policyholder.[8]

Notwithstanding these principles, the court resisted the argument that Urban Outfitters' pre-coverage advertisements could be significantly different from advertisements published during the policy period — which would render the "prior publication" exclusion inapplicable — even though the underlying complaint was decidedly vague regarding the content of alleged pre-coverage advertisements. The result is an aberrant scenario in which Urban Outfitters might ultimately be held liable based solely on advertisements during the policy period, such that it would arguably be entitled to indemnity from an insurer who was previously held to have no duty to defend. Such inconsistencies are normally prevented by the principle that the duty to defend survives as long as there is a *potential* for coverage. In *Urban Outfitters*, the mere possibility — based on an incomplete factual record, since the complaint was dismissed on a motion for judgment on the pleadings, prior to discovery[9] — that an exclusion might ultimately preclude indemnity relieved the insurer of its duty to defend a potentially covered claim.

CONCLUSION

Urban Outfitters is a clear departure from longstanding pro-coverage Pennsylvania precedent. It demonstrates that even at the duty to defend stage — where doubts should be resolved in favor of coverage — courts are

sometimes persuaded by insurers' aggressive, exclusion-based arguments. In the event of a claim related to their advertising, policyholders would be prudent to immediately confer with coverage counsel in order to develop strong arguments in favor of coverage.

NOTES:

[1] Courts have held that a variety of intellectual property and related claims — including copyright, trademark, trade dress, patent, trade secret, and misappropriation — may be within the scope of the "personal and advertising injury" coverage found in most commercial general liability policies.

[2] *Urban Outfitters*, 2015 WL 6405763, at *1–3.

[3] *See, e.g.*, *Mut. Benefit Ins. Co. v. Politsopoulos*, 115 A.3d 844, 852 n.6 (Pa. 2015).

[4] *See Urban Outfitters*, 2015 WL 6405763, at *5. The court acknowledged that it was departing from the framework set forth in the leading case on the "prior publication" exclusion, *Taco Bell Corp. v. Continental Casualty Co.*, 388 F.3d 1069 (7th Cir. 2004). *Id.* at *5 n.30.

[5] *See, e.g.*, *Erie Ins. Exch. v. Transamerica Ins. Co.*, 533 A.2d 1363, 1366 (Pa. 1987).

[6] *See, e.g.*, *Am. & Foreign Ins. Co. v. Jerry's Sport Ctr., Inc.*, 2 A.3d 526, 608 (Pa. 2010).

[7] *Id.*

[8] *See, e.g.*, *Roman Mosaic & Tile Co. v. Aetna Cas. & Sur. Co.*, 704 A.2d 665, 669 (Pa. Super. Ct. 1997).

[9] The court declined to consider any extrinsic evidence that might support a finding of coverage, strictly adhering to the Pennsylvania rule that the duty to defend depends only on the language of the policy and the allegations of the underlying complaint. *Id.* at *3–4.

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