WISCONSIN SUPREME COURT
December 11, 2018
9:45 a.m.

2017AP909 West Bend Mutual Ins. Co. v. Ixthus Medical Supply, Inc.

This is a review of a decision of the Wisconsin Court of Appeals, District II (headquartered in Waukesha), that reversed a Racine County Circuit Court decision, Judge David W. Paulson, presiding.

This case presents the question of whether West Bend Mutual Insurance Co. has a "duty to defend" its insured, Ixthus Medical Supply, Inc., in a federal trademark infringement case.

Abbott, a health care company, makes diabetic blood glucose test strips that are sold worldwide. The underlying complaint alleges that test strips intended for international markets were fraudulently diverted, advertised, and passed off as domestic test strips, which are eligible for certain rebates and reimbursement. Test strips intended for international use are not. Abbott thus paid insurers rebates on what it thought were legitimate insurance, Medicaid, or Medicare reimbursement claims. Abbott filed suit against Ixthus and more than 300 other defendants, alleging a number of claims.

Ixthus is alleged to have sold test strips to domestic pharmacies that were wrongfully diverted from international markets. The pharmacies, in turn, allegedly sold the test strips to consumers.

Ixthus tendered defense to its insurer, West Bend. Under the policies, West Bend has a duty to defend for, among other things, claims of "personal and advertising injury." The policies contain an exclusion for coverage for personal and advertising injury under the "Knowing Violation of Rights of Another" provisions, for injury "caused by or at the direction of the insured with the knowledge that the act would violate the rights of another and would inflict 'personal and advertising injury.'"

West Bend disputed coverage and filed this declaratory action in Racine County circuit court, seeking a declaration that it had no duty to defend or indemnify Ixthus. West Bend argued that (1) the policies' "knowing violation" exclusion barred coverage, and (2) that the underlying complaint failed to allege a causal connection between Ixthus's advertising activity and Abbott's injury.

The circuit court ruled in favor of West Bend, noting that no reasonable insured would believe it would have liability insurance coverage for repeated and intentional participation in an illegal scheme to defraud.

The Court of Appeals reversed, concluding that there are claims in the complaint that survive the "knowing violation" exclusion, stating "[s]imply because the complaint alleges intent does not necessarily mean each underlying claim requires proof of intent." For example, certain claims arise under the Lanham Act, which is a strict liability statute, so there need not be an allegation of willfulness to succeed on the issue of liability.

West Bend says that the Court of Appeals improperly focused on Abbott's theories of liability, rather than the specific facts alleged in the complaint. West Bend also maintains that there is no coverage because the complaint does not allege a causal connection between an offense covered under the "advertising injury" provisions of the insurance policy and the insured's actual advertising activity.

Ixthus says that the appellate court properly applied controlling precedent and reached the correct result.

The Supreme Court may provide guidance on the proper interpretation of a "knowing rights" exclusion and the scope of a claim for "advertising injury."

The following issues are presented for review:

1. Do allegations of Ixthus' unlawful diversion to U.S. markets of Abbott's diabetic test strips manufactured for foreign markets, and fraudulent rebate scheme with resultant loss to Abbott, constitute injury caused by advertising so as to invoke "advertising injury" liability coverage and invoke West Bend's duty to defend the underlying lawsuit in federal court in New York, Abbott Laboratories, et al. v. Adelphia Supply USA, et al., No. 15 Civ. 05826 (CBA)(MDG)(E.D.N.Y.)(the "Abbott Suit")?
2. Do allegations of Ixthus' unlawful diversion of test strips and fraudulent rebate scheme constitute a knowing violation of rights of another such that the exclusion for Knowing Violation applies?
3. Do allegations of Ixthus' unlawful diversion of test strips and fraudulent rebate scheme preclude coverage pursuant to the Criminal Acts exclusion?
4. Do allegations that Ixthus intentionally caused damage to Abbott by participating in the unlawful diversion of test strips and fraudulent rebate scheme preclude coverage on the basis of the Doctrine of Fortuity?
5. Do allegations of Ixthus' unlawful diversion of test strips and fraudulent rebate scheme preclude coverage on the basis of an insured's reasonable expectations?
6. Do allegations of Ixthus' unlawful diversion of test strips and fraudulent rebate scheme preclude coverage on the basis of public policy considerations?