

# Life line

CFC Underwriting's **Madeleine Brown** and **Kristian Kolsaker** outline the benefits IP insurance can bring amid the viral pandemic



**The vast majority of businesses today of most sizes and in most industries, will have an intellectual property (IP) risk whether they realise this or not.**

The global pandemic has served as a wake-up call for many; having to lock up their premises and move to a work from home environment has forced them to reassess the importance of their intangible assets and afford them the same level of protection as their bricks and mortar. Those companies who hadn't perhaps realised the value of the IP within their business – whether the IP is their brand, their creativity or their products and services – are now looking at how they can protect it within the new 'norm' in which we find ourselves.

The demand for IP insurance has been increasing as businesses become more aware of the threat not only to their own IP, but also the potential that they may face a claim of infringement by another company.

Another benefit to IP insurance, which has perhaps flown under the radar, is the protection it can provide against affirmative exposures that arise in obligations under contracts. Most businesses do not produce final products these days. They are instead developing solutions and products that form part of a bigger end product, and through this chain, contractual exposures arise.

And there is a further often unrecognised benefit of IP insurance; in addition to a business registering its IP, insuring it can help to secure funding from would-be investors.

To fully understand the full benefit of this valuable insurance, let's look at each area in a little more detail.

## **Contractual obligations**

Large businesses are, on average, more aware and better equipped to identify IP infringement risk than smaller businesses. To a large extent, the reasons are due to depth of expertise in their legal and internal control functions, such as enterprise risk teams but also as a result of experience gained from their own legal disputes, which are more likely

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to occur as companies grow. As a final and important point, larger businesses have deeper pockets and even specific funds dedicated to transfer IP risks and exposures that affect the business. These onerous obligations can have a major impact on a small business.

When small business suppliers begin pitching and contracting with larger corporations, the disparity between the parties' negotiating positions can be material. When it comes to IP infringement, one party has greater awareness of the IP infringement exposure in the first place; has access to a greater sample of contract clauses with an understanding of their implications; and records, monitors and reports on the IP infringement indemnity positions on each of their contracts to comply with their own contract risk management programme. More challenging still, any prospective contract may have greater significance for the small business supplier.

IP infringement warranties and indemnities allocate and transfer infringement liability between contract parties. In the context of IP insurance, there are two key points to consider. These are below.

### **• Limit of liability**

Agreement to provide IP infringement indemnities is one matter, but

limits of liability are financial amounts written into contracts detailing the maximum liability of the indemnitor to their indemnified party. Often the limits can be set as high as £5m or can be without limit. Agreeing to such a liability can far outweigh its affordability for a small business and could be catastrophic if the indemnity was triggered. Such a low frequency but high severity risk profile is well suited to risk transfer to an IP insurer.

#### • Contract insurance requirements

An increasing number of contracts are requiring insurance to be put in place to meet the scope and extent of the agreed indemnities. As a specialised IP infringement product, IP insurance is required specifically and more frequently as it will include cover for any type of IP infringement allegation, including patent infringement. Other insurance products, such as directors and officers liability cover, often limit or exclude IP coverage so only an IP insurance policy will fully comply with the contract insurance requirements.

### A business enabler

Affordability of an IP infringement indemnity is an important consideration for an organisation's robustness, but it can also put them in a stronger position than competitors to win contracts.

Rather than reacting to a request to have such indemnity in place, a business could choose to take a more proactive approach by taking out IP insurance in the first place, with coverage in place for all of their contracts. With strong risk management in place, they are better positioned to negotiate with larger partners and manage indemnity levels from the outset. And larger companies may well be encouraged to enter into an agreement or contract with a smaller supplier if that supplier demonstrates a strong approach to managing their own risks.

An IP policy will cover infringement allegations relating to all IP rights including patents and trade secrets, and it is possible to obtain a global policy covering all territories. This global coverage is important, particularly for companies operating in the US, where patent litigation court filings are on course to be at their highest annual level for five years.

IP insurance is valuable even if the insured receives infringement indemnities for a product. This is because the insurance will pay out by default first, and then seek to recover any costs from the indemnitor, providing the insured peace of mind that they will not lose out financially in any way. This is preferable to the time, expense and uncertainty involved in attempting to trigger an indemnity from a contract party and compelling them to resolve the dispute and cover all the legal costs and compensation.

Based on our experience over the past year, contracts where the potential liability for one party far exceeds that company's affordability are becoming more commonplace. While it is difficult to predict the likelihood of a claim, it is all too easy for a smaller company to unknowingly infringe on a third party's IP rights simply because it is too time consuming and expensive to conduct searches for all relevant registered and unregistered third party rights.

However, it is an inevitable fact that these risks exist and claims instances arising out of contractual indemnity requests are gradually increasing. Reviewing our own claims experience, five years ago less than 10% of notifications to us were contractual indemnity requests, but this has increased over time and they now comprise more than a third of notifications in the last 12 months. This correlates with the increasing amount of IP infringement terms and conditions in contracts.

### Funding

The often unrecognised benefit of IP insurance is how it can help a business to secure funding from would-be investors. This not only enables investors to clearly understand the value of the IP, but also

provide the additional security of knowing that their investment will be protected.

Having a strong patent portfolio is a good start; patents lend credibility, particularly to a start-up business, and can be collateralised to gain further investment. However, a patent portfolio is only an effective deterrent if it can be used. Having IP pursuit insurance in place can reassure investors that a portfolio is no empty threat. Conversely, IP defence insurance can act as balance sheet protection, giving investors' confidence that their money will be spent on actual R&D rather than fighting potential litigation and that company they have invested in won't fold.

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And when it comes to their own patents, companies can spend thousands of pounds on registering and maintaining a patent, but the value to the organisation of that protected technology can be several times this initial outlay. Patent invalidity coverage is available to meet the legal costs incurred in any defence of an invalidity challenge brought against that patent by a third party.

A broad IP insurance policy, covering a range of IP exposures, is a good way to maximise protection in a competitive environment, and investors recognise proactivity in exposure management. Many enquiries we receive for IP insurance are actually investor driven.

### IP insurance as risk management

Insurance policies are often likened to having a safety net or a life buoy in place and that is certainly true when it comes to IP insurance. It sits alongside their current strategies providing security, business development and business enabling.

As awareness of how it can provide protection and risk transfer and so support the growth of a small business, we are seeing a significant uptick in the number of smaller suppliers wanting to insure not only their own IP but also their contractual obligations. And if the worst does happen, they know they can defend a claim with the benefit of an insurer's resources, know-how and financial support putting them in a far stronger position than they would be without it.

### Authors



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