

IP insurance and M&A

Mergers and acquisitions activity (M&A) can involve a buyer acquiring an entire business or simply the acquisition of specific assets. In both cases, M&A will have implications relating to Intellectual Property (IP).

IP can take several different forms, ranging from design rights, trademarks, copyrights and trade secrets, to more complex IP such as patents. IP is highly relevant to companies of all sizes and in all industries.

M&A transactions can often provide the catalyst for buyers of companies to purchase IP insurance as it both supplements and enhances protections obtained from IP representations and warranties in the acquisition agreement, which are typically covered by representations and warranties insurance (R&W insurance).





Understanding representations and warranties

IP will often play a significant role in an acquisition, as for many businesses much of their value lies in their IP which is what makes them unique.

When an acquisition takes place, the buyer will obtain representations (reps) and warranties from the seller regarding the assets being acquired. This is primarily a means of risk allocation, providing the basis for which they can recover damages if those reps and warranties are false. Frequently buyers will purchase R&W insurance to protect themselves against financial loss resulting from breaches of the reps and warranties.

In most cases, these reps and warranties will include statements in relation to the target company's IP. It is common for the seller to represent and warrant that the operation of the target business does not infringe, misappropriate, or violate any other party's IP rights; that no other party is infringing, misappropriating, or violating the target's IP rights; and that there is no litigation or claims covering any of the foregoing that is pending or threatened.

The role of IP insurance

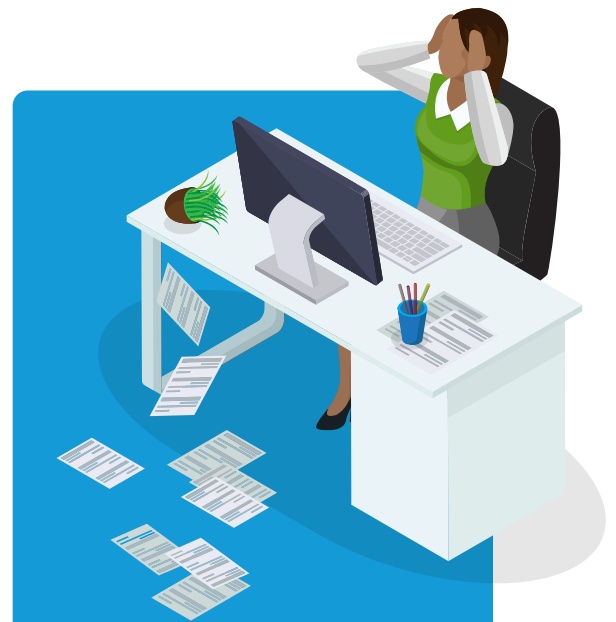
The IP protection under R&W insurance can vary depending on the scope of the IP reps and warranties in the acquisition agreement. For instance, the relevant IP reps and warranties may include knowledge qualifications (i.e. may be subject to seller awareness) and will likely be historic or 'retro' in nature.

On the other hand, IP insurance is designed to cover the legal expenses and damages arising from any allegations of infringement, both historic and prospective, regardless of seller awareness.

With this in mind, IP insurance can be an invaluable tool for a buyer in establishing or enhancing protection against IP associated risk during M&A transactions as the policy will cover infringement allegations that would not be otherwise covered by R&W insurance.

It also provides peace of mind that any IP infringement allegations relating to the target's new business activities will be covered going forward.

In many cases, IP insurance can act as a deal facilitator by helping the buyer avoid protracted IP reps and warranty negotiations, or by acting as a bid differentiator at auction.



Distressed M&A

The global Coronavirus pandemic has created an extremely challenging economic environment for many businesses to navigate. As a result, buyers are preparing for an increase in distressed M&A transactions.

One of the greater risks to a buyer in distressed M&A is the potential for limited contractual recourse under the acquisition agreement. In distressed M&A transactions, a buyer often agrees to purchase a target business on an 'as is' basis, and the seller provides very limited or no representations and warranties regarding the target business. Because of this, it's unlikely that R&W insurance will be available.

In these cases, IP insurance can offer the protection usually provided under the IP representations and warranties in addition to comprehensive cover.



Did you know?

Each year **over 1 million new patents are granted**, and **over 10 million new trademarks are filed worldwide**¹.

¹World Intellectual Property Organization, WIPO Indicators Report



What to consider

There are a number of insurance products that can provide IP cover. The type of IP the target business holds and uses, and the industry the target operates in, will influence the buyer's decision as to what is the most appropriate insurance product to cover the target business. As IP insurance can be provided on both a prospective basis and a retrospective basis, it can be used to provide protection to a buyer for business operations in both the pre and post-close period.

Here are some ways CFC can assist with IP insurance:

- **Stand-alone IP insurance:** Cover provided for claims arising out of the IP of a target's business, which specifically covers for legal expenses and damages arising from IP infringement allegations.
- **Media license agreement liability insurance:** Designed for businesses that use third-party IP (i.e. brands, logos, images, or characters) pursuant to media license agreements like sponsorship or endorsement deals, brand collaborations, or naming rights agreements. This will cover unintentional breaches of those agreements as well as claims alleging infringement from either the licensor or another third-party.
- **Industry-specific package policies:** Defense costs cover provided as part of a package policy for specific industries where IP is a critical asset (such as the life sciences, media & entertainment, professional services and technology industries).

A standalone IP insurance policy is the best way to ensure a business has protection for all IP infringement allegations, including patent infringement, which is frequently excluded from other insurance policies.

Case study

Prospective protection

A manufacturer of engine components was acquired by an engineering research organisation.

CFC provided R&W insurance to the buyer covering the representations and warranties given by the seller, including coverage of the IP representations. Additionally, the buyer purchased a standalone IP insurance policy covering the buyer for retrospective and prospective IP infringement exposures.

Following closing, the business developed and launched a new product to the market with an announcement in the industry press. Later that week, a large competitor emailed the company to allege that the new product was infringing their patent.

The most relevant IP representation – that the seller had not infringed any third-party IP – was not found to be inaccurate because the new product had been developed following the transaction closing, meaning no claim could be lodged under the R&W insurance.

However, the standalone IP insurance responded with legal costs and settlement amounts being covered.

Case study

Enhanced R&W insurance protection

A private equity firm acquired a specialist ventilation manufacturer from a consortium of private owners. The buyer procured R&W insurance as well as a standalone IP Insurance policy.

A month after closing, a third-party competitor sent a cease and desist demand to the target alleging 'passing off' as well as design rights infringement in respect of one of their most popular products: a heat recovery unit. This product had been a best-seller for a number of years.

The seller's non-infringement representation under the acquisition agreement was subject to seller awareness. None of the seller's executives had any awareness of any possible third-party infringement prior to closing. Accordingly, the seller's non-infringement representation was not found to be inaccurate and therefore the R&W insurance policy did not respond.

However, the claim was covered under the IP insurance policy. Legal costs were incurred by the buyer to defend the allegation and after a few months, the parties reached an out-of-court settlement. Both the legal costs and settlement amount were covered under the IP insurance.

Case study

Establishing IP protection

CFC were approached to provide insurance in relation to the acquisition of a business that owned and operated a website providing healthcare products.

The online store was powered by Shopify and the assets being acquired were those connected to the operation of the website, primarily the domain name, brand name, trademarks, designs and social media accounts (the assets connected with marketing the products), along with certain customer / vendor agreements and inventory. As such, the IP of the target represented a large portion of the target value to the buyer.

Because of the operations of the business, CFC's media & entertainment package policies provided comprehensive and industry-relevant coverage of IP, errors and omissions and cyber exposures, both on a prospective and retrospective basis.

For more information on IP insurance, visit [cfcunderwriting.com](https://www.cfcunderwriting.com) or contact IP@cfcunderwriting.com

