Your Coverage Advisor

Reasons to Start Thinking About Intellectual Property Insurance

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WHY DO YOU NEED INTELLECTUAL PROPERTY ("IP") INSURANCE?

IP insurance coverage can be used to protect the insured against third-party infringement claims, allow the insured to pursue potential infringers of their IP, protect the insured against an adverse ruling related to their own IP assets, cover reps and warranties related to IP transactions, and to cover potential contract breaches related to IP assets.

"Google's trademark is worth an estimated $44 billion, or 27% of the corporation's overall value, measured by market capitalization"

However, more generally, IP insurance is used for your typical business reasons, such as to protect the balance sheet, to provide contractual liability protection, and to facilitate business deals. The cost of IP litigation is almost always higher than any other form of litigation, for example, where the plaintiff is seeking damages of $25 million or less, total litigation costs run $600,000–$2 million for cases settled…

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before going to trial, and $1.2 million–$3.5 million if they go through trial and appeal. For cases involving more than $25 million, the AIPLA says pretrial litigation costs are $1.4 million–$4 million and jump to $2.5 million–$6 million if the cases go through trial and appeal.

The prevalence of non-practicing entities ("NPEs"), patent enforcement entities ("PAEs") and patent trolls is becoming increasingly problematic. These entities typically don't practice a patent, but seek to enforce the patent, to which they own enforcement rights, against companies to extract settlements and/or licensing fees. Further, in markets where there are strong competitors, the competition may seek to use their patents to carve out niches, remove competition, or extract royalties. Additionally, when a company enters a new or crowded market, competitors may seek to keep their competition away, or, in a crowded market, numerous patents may already exist. In any case, patent infringement claims against any company can be a significant expense, but may affect the viability of a small or start-up company.

Because the cost of IP litigation can be very costly, enforcing a company's IP rights against potential infringers may be cost prohibitive. Coupled with an uncertainty in the outcome of any action, companies are often reluctant to move forward with an infringement action. However, small and start-up entities can be easily and adversely affected by IP infringement, and larger companies cannot typically afford to lose their IP rights by failing to protect them, particularly in new or emerging markets. IP insurance may offer a company the ability to enforce their IP rights without too much concern about the cost and potential outcome. For example, where a company innovates in a new or emerging market they need to be able to prevent knock-off artists from stealing their innovations in order to maintain their market share, and, ultimately, the value of the balance sheet.

The IP assets of a company may form a large portion of the value of the company. For example, according to Brand Finance, a brand-valuation consultancy, Google's trademark – now the most valuable on the planet – is worth an estimated $44 billion, or 27% of the corporation's overall value, measured by market capitalization. An adverse ruling, such as a ruling of invalidation, unenforceability, infringement, or other loss of enforcement rights could adversely affect the value of the corporation's IP assets. Insurance products may help the company protect against any potential loss of IP asset valuation.

When selling, purchasing or being involved in some transaction involving IP assets, insurance can protect against inheriting liability, give the buyer piece of mind, and/or facilitate a transaction involving licensing or selling of the IP assets. Contracts involving reps

and warranties, or breach of clauses that involve IP can be a source of added liability to both parties to the contract. Insurance products that limit liability exposure for these situations may facilitate the execution of the contract, deal or transaction.

WHAT POLICIES ARE AVAILABLE AND WHAT DO THEY COVER?

General Liability, Content & Media Liability, Errors and Omissions, Business Operators, and Cyber-Risk Liability are forms of common business insurance coverage that may include some form of limited IP coverage for trademarks and copyrights. These types of coverage typically provide defensive coverage and indemnity, but do not typically cover patents, offensive coverage, loss of valuation, or contractual liabilities relating to IP. General Liability products typically cover trademark and copyright infringement associated with advertising or promotion of an insured's products and service; but coverage may be limited in some industries, such as websites that provide content uploading and sharing, media companies, and some other media and content providers, particularly online. Companies in these areas may require Errors and Omissions coverage, Content & Media Liability, or a Cyber-risk policy.

Standalone IP protection is designed to cover the insured for particular IP related situations. Defensive third-party coverage will typically reimburse the costs associated with defending an infringement suit. Indemnity coverage can be added, to cover any reimbursement damages that may arise from the suit. Offensive first party coverage can reimburse the insured's costs associated with enforcing their intellectual property rights against an infringer. First party loss of value coverage can reimburse the insured's lost value of IP assets, which they may incur when a negative ruling is made against the insured. For example, a finding of invalidity may impact the insured's ability to license and/or keep competitors out of the marketplace. Reps and Warranties coverage can help pay legal expenses and damages associated with a transaction, which typically involves the sale of a business, products, technology or intellectual property. Contractual coverage can help the insured cover legal expenses and damages that may be associated with a license agreement breach or breach of confidentiality.

ELIGIBILITY, PROCESS AND COSTS.

Standalone IP insurance will not cover situations where the insured knew about the possibility of an action before the policy is in force. Often, defensive coverage has an initial waiting period for responding to claims. Eligibility is related to the type of coverage desired and IP associated with the

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coverage; previous litigation; the industry sector; amount of IP and how it is being managed; and existing and future licensing and indemnification (vertically).

A broker is typically used to secure coverage, which involves an intensive underwriting process. An initial application is used to filter potential coverage, and a follow-up underwriting process results in the insurer's decision on coverage and cost, details of which are often negotiated prior to coverage. Cost often ranges from 1 to 10% of coverage; and an underwriter's fee, retention fee (typically 2%); and co-insurance (5–10%) may also be included.

OTHER ISSUES

Companies should also consider other elements when evaluating IP insurance coverage. Some coverage can limit the insured's ability to select their counsel of choice, and ability to enter into settlements. Further, there are often specific pre-claim analysis requirements, along with detailed ongoing reporting requirements. Often, smaller entities will pool resources together to purchase IP insurance coverage to help spread the significant cost. A recent California ruling stated that, during settlement negotiations, attorneys cannot misrepresent extent of insurance coverage, which is often cited as the most common misrepresentation during negotiations. ■

HIPAA Regulations Expand to Cover Companies Outside the Health Care Industry

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As technology advances and health care providers continue to utilize electronic means of maintaining health records and information, more companies outside the traditional health care field are at risk of violating various federal regulations that previously did not apply. These violations may not be covered by typical commercial general liability ("CGL") policies.

In March 2013, the Heath Information Technology for Economic and Clinical Health Act ("HITECH") went into effect, expanding the Health Insurance Portability and Accountability Act of 1986 ("HIPAA") regulations and broadening the definition of both a business associate and a breach to be more inclusive. Now, any company that is involved in any manner with this protected information, including health information organizations, subcontractors, and vendors are directly liable for breaches. Additionally, a breach now includes any unauthorized acquisition, access, use, or disclosure of protected health information, unless it can be shown that there is a very low likelihood the information has been compromised. Since the enactment of HITECH, there has also been an increase in the enforcement of these regulations and many companies, which may not even realize they are at risk, may be liable for these violations in the event of a data breach.

The costs of cyber data breaches can be crippling and with such breaches on the rise, understanding

your insurance coverage and options is critical. This is even more important for the health care sector which makes up over 36% of all data breaches. More importantly, if you believe your CGL policy covers HIPAA and HITECH violations, you may be wrong. There is very little case law addressing whether CGL policies cover HIPAA and HITECH breaches, which have more extensive penalties and requirements than typical cyber data breaches.

Policyholders most frequently seek coverage for cyber data breaches under either the property damage or advertising and personal injury sections of a CGL policy; however, both have limitations. In order for the loss of personal information from a cyber-breach to be covered as property damage, there must be a loss of tangible property, which does not include the loss of protected health information. Unless there is physical damage to a server or other tangible property as a result of the breach, the loss will not be considered covered property damage. Similarly, coverage as advertising and personal injury requires actual oral or written publication of material that violates a person's right to privacy, which is not always present in this type of data breach. In addition to these limitations, penalties and fines, which can make up a large portion of the damages sustained by a company for HIPAA and HITECH violations, are often excluded from CGL policies.

In one of the few cases specifically addressing HIPAA and HITECH breaches, a California Federal Court found that a hospital was entitled to coverage for two class actions where the allegations included disclosure of personal health information and records on a public website. The Court found that such allegations fell under the personal and advertising coverage part of the CGL policy. However, in a different scenario not involving HIPAA or HITECH violations, a court found that there was no coverage under the personal and advertising clause because there was no evidence that anyone had accessed the stolen information. A court's determination of coverage under a CGL policy in any cyber-breach depends largely on the specific facts and the court's interpretation of the policies and those facts.

However, even if the company does have an insurance policy that covers these violations, the costs associated with breaches involving personal health records and information are more expensive than a typical data breach. Companies that have a breach of personal health information or records are subject to extensive legal defense costs, potential class actions, forensic investigation costs, severe penalties of up to $50,000 per violation, and remedial requirements that may be incurred even where no one was harmed or at risk.

> "...more companies outside the traditional health care field are at risk of violating various federal regulations that previously did not apply."

In order to protect oneself, a policyholder needs to know its risks and inform its broker. In order to do this, it is imperative that the party responsible for obtaining and maintaining proper coverage knows that the company handles personal health records or information and that it is now at risk for HIPAA and HITECH violations. It is also imperative that a policyholder review the policy to ensure coverage and that the policy limits are high enough to cover a data breach of this nature. ■

Coverage for Implied Disparagement Under CGL Policies

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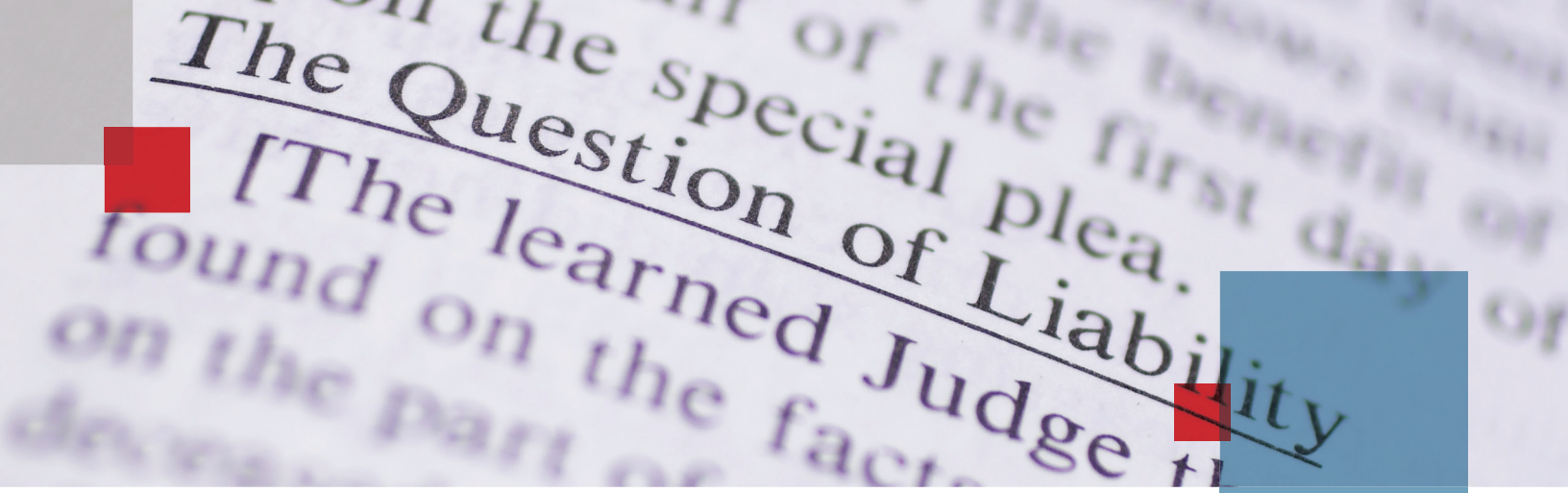
As companies have become more creative with their advertising campaigns and their methods of advertising have become more diverse, there has been much debate regarding whether traditional Commercial General Liability ("CGL") policies provide coverage for the types of advertising claims for which policyholders are seeking coverage.

Typically, CGL policies provide coverage for liability claims arising out of "personal and advertising injuries." This generally includes claims against the policyholder that allege "oral, written or electronic publication of material that slanders or libels a person or organization or disparages a person's or organization's goods, products or services." When a policyholder is sued for making comments that explicitly disparage a competitor or its products, it is almost a foregone conclusion that the CGL will provide coverage for the claims.

However, courts are currently grappling with whether CGL policies provide coverage for claims that do not explicitly disparage an entity; instead, the policyholder indirectly references the entity (ex. a man named Ronald McDonald stating that Burger King is his favorite), or the policyholder greatly brags about its own products (ex. Crest is the best product on the market for proper oral health). Would a lawsuit for publication of these advertisements fall within the "advertising injury" coverage provided by the policyholder's CGL? Are the statements actually disparagement under the policy language? As the caselaw demonstrates, courts throughout the country are split on whether the policies cover claims for "implied disparagement."

One federal court ruled that insurers have a duty to defend "implied disparagement" claims when the claimant alleges that it was injured by the policyholder's false and misleading representations. The policyholder created and sold an over-the-counter patch containing lidocaine called LidoPatch. The advertisement for LidoPatch stated that it provided "relief that lasts all day without a prescription," and "same active ingredients as the leading prescription patch." The claimant alleged



that LidoPatch's similarity to its prescription product, Lidoderm, caused the company injury because consumers would think that Lidoderm was equivalent to LidoPatch.

The court held that falsely claiming superiority over a competitor's product is disparagement if the product is not, in fact, superior. The court also stated that a statement equating a competitor's product with an allegedly inferior one is identical to, and no less disparaging than, the policyholder describing its own product as "superior." Thus, the court found that coverage existed under the "advertising injury" section of the CGL for the suit against the policyholder.

Conversely, a state supreme court recently held that coverage for a disparagement claim is not triggered under the "advertising injury" portion of a CGL policy unless the claimant shows, by express mention or clear implication, that the insured made false or misleading statements that specifically refer to, and derogate, the claimant's product. In the case, the claimant sold a cart called "Multi-Cart" and the policyholder sold a cart called "Ulti-Cart." The policyholder advertised the "Ulti-Cart" as "unique," "superior," and "patent-pending," which the claimant contended that, by implication, the policyholder was suggesting the "Multi-Cart" was inferior.

The Court held that the claims were not covered by the CGL, as implied disparagement is not included within the enumerated coverage grants for an "advertising injury." The Court ruled that disparagement is a knowingly false or misleading publication that directly disparages another's business or property and results in damages. Since the policyholder's statements about its product were mere puffery, the policyholder was not entitled to coverage for the claims.

While only a few courts have dealt with implied disparagement claims, it is likely that additional jurisdictions will be presented with cases, and the debate regarding coverage will continue. As long as "advertising injury" is not expressly limited to coverage for disparagement claims that arise from direct statements about a competitor or its product, there is an argument that the policyholder is entitled to coverage under the plain language of the CGL. Thus, policyholders should contact experienced counsel when seeking coverage under the policy for a potential claim. ■

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Attorney Highlights

Kerri L. Keller graduated from Leadership Hudson Class of 2014 in May.

Kerri L. Keller was nominated to the Board of Trustees for the Akron Bar Association in June.

Amanda M. Leffler was selected as a member of Class 31 of Leadership Akron in July.