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Protecting your competitive advantage

Embracing IP Risk Management

Thought Leadership Series



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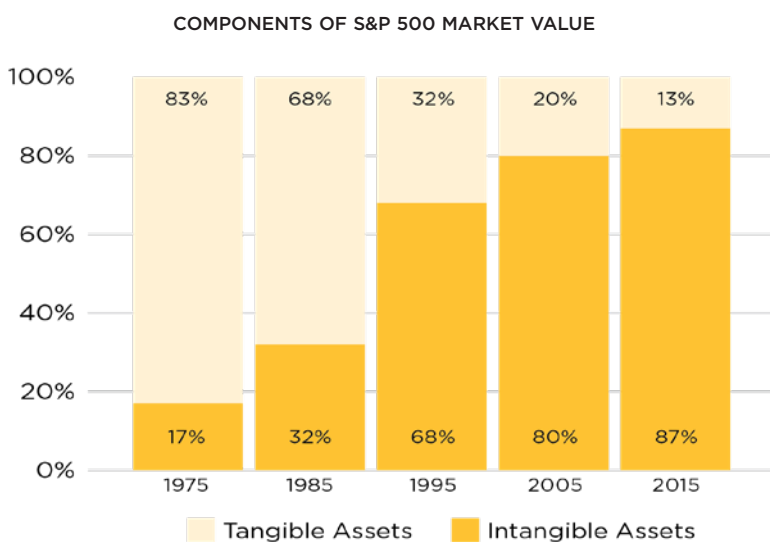
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Recognising the Intangibles

Many countries are striving today to become what is called a 'knowledge-based economy'. The emphasis is to derive value from the 'creation of mind' rather than depletable natural resources. This shift in paradigm is clearly evident in the way businesses have evolved and how they compete.

Traditionally, physical assets like buildings and plants have been value drivers for businesses and they determined competitiveness of a company in the market. However, in recent decades the situation has undergone an inversion where most of the enterprises today are powered by the intangible assets - proprietary knowledge, brands, customer data, supplier relationships, designs and innovation. Balance sheets are increasingly reflecting this shift away from tangible assets. Research by Ocean Tomo reflects how the relative value of intangible assets has increased from 17% of total assets in 1975 to almost 87% in 2015¹.



Source: Ocean Tomo, LLC

A crucial subset of intangible assets is intellectual property (IP). IP is a category of rights protected by law. IP rights allow the inventor or the creator to capitalise on the investment they made in their creation. IP rights give exclusivity to the inventor over use of the property. A product

The price of ignoring innovation and change

There are very few business tragedies as interesting as that of Kodak. Kodak, a company that once dominated the film-based camera industry, filed for bankruptcy in 2012². What is ironic is that Kodak was the inventor of digital photography technology which changed the face of the industry in the years to come. The company effectively ignored the invention as it would cannibalise the sales of film, which at the time contributed significantly to their margins. The competitors developed on the new digital photography technology and raced ahead. By the time Kodak embraced the change, it was too late.

as mundane and ubiquitous as a Post-It Note was once protected via patent. From the distinctive blue colour of Tiffany's to Lipitor, a cholesterol-lowering drug by Pfizer, all are protected by some form of IP right.

IP rights are territorial in nature, in that each country enacts its own law in this domain and generally the laws have no application outside that particular country. Multiple international treaties and conventions exist to make filing and obtaining of IP protection in various countries easier.

**INTELLECTUAL PROPERTY CAN BE BROADLY CLASSIFIED INTO TWO TYPES:
REGISTERED IP AND UNREGISTERED IP**

Registered IP	This type of intellectual property is registered with the national IP office of a country. The following are the common forms of registered IP.
Patent	Patents are granted for technical inventions like processes, machines or composition of matter. An invention must be novel, useful and show an inventive step over and above the existing technology (known as "prior art" in the IP world) to be patentable. Examples include a new machinery component that increases production efficiency or a new process of manufacturing that improves durability of a product.
Registered Trademark	Trademarks protect designs, words or other recognisable elements like a sound or smell that differentiates a business from others. Registering a trademark acts as a strong deterrent in inhibiting competitors from using a similar brandmark. In general, registered trademarks are better protected than unregistered ones and more valuable. For example, a half-eaten apple as the logo of Apple Inc. and the iconic golden arch of McDonald's.
Registered Design Right	This protects the appearance and the design element of a product. The functionality of the product is not covered under this class. In some jurisdictions, it is also called a design patent. An example is the shape of the Coca-Cola bottle.
Plant variety rights	This right allows the owner to exclusively grow and sell propagating plant material of a new plant variety. An example is protection of certain varieties of kiwifruit.
Geographical indications	These are used to indicate to the buyers that the product is from a particular location and is authentic. For example, Roquefort cheese from France.

Unregistered IP	These are not registered with the IP office but do offer legal protection. The following are the common types of IP in this category.
Copyright	Copyrights cover original works of authorship like a musical piece, movies, books, photographs and in some cases computer software codes. Copyrights cover the expression of the idea and not the idea itself. Some jurisdictions do require registration if the owner of the work wants to bring about an infringement claim.
Trade Secret	Refers to any kind of confidential business information that provides a competitive advantage to a business in the market. For example, a business might want to keep the recipe of its new energy drink closely guarded.

The difference between ® and ™

The symbol ® over a brand name signifies that the trademark has been registered with the IP office. ™ denotes that the trademark is unregistered, but it is owned by the business using it. Unregistered trademarks have some protection under common law.

Protecting the unique connection

Play-Doh, the modelling clay children love to play with, recently trademarked its smell³. The company recognised the smell of its product was a unique point of connection between the brand and its consumers. "Sweet, slightly musky, vanilla fragrance, with slight overtones of cherry, combined with the smell of a salted, wheat-based dough" is how the company described the smell of the product in its trademark application.

Achieving advantages of economies of scale in New Zealand is generally difficult. Hence, companies have geared themselves to focus on creation of value and are bringing forward innovative and niche products. This is evident in R&D spend as well. R&D expenditure has risen by 29% since 2014 to reach \$1.6 billion in 2016⁴. Companies are also going the extra mile to protect their major differentiators. Approximately 300 new patents and 6,000 new trademarks have been registered each year since 2014 by New Zealand companies and inventors.

Kiwi Ingenuity at Work

New Zealanders have long been known for coming up with unusual innovative ideas to solve problems. “No.8 wire” symbolises the spirit of innovation in New Zealand at its best. Today, New Zealand boasts of companies that are innovating at a global level; revolutionising the most ordinary daily used commodity to introducing highly advanced technology to the world.

Here are some of the companies creating a splash through their disruptive ideas and business models:

Volpara Health Technologies – The Wellington-based digital health company has developed a patented technology that assists in early detection of breast cancer. The ground-breaking technology has enhanced precision in analysing mammograms. The company is listed on the Australian Stock Exchange with users in 36 countries⁵.

Latitude Technologies – The company recognised a gap in the existing model in the way New Zealand businesses transacted with their Chinese customers. Most of these consumers were comfortable using a Chinese e-wallet for purchases which essentially meant that the seller had to wait for the transaction to clear through banks before delivery was made. The company created a platform, LatiPay, which allows payment for products in foreign currency and the seller receives it in New Zealand dollars in real time, simplifying the purchase experience for the customer⁶.

Robotics Plus – The company is bringing cutting-edge technology to the primary sector. It aims to address the challenges faced by the sector like labour shortages and pollination gaps. It has developed systems that mechanise packing and harvesting processes with the help of robots⁷. The company is in the process of taking its technologies to a global scale.

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Risks associated with IP

Like any other business asset, IP is also exposed to various kinds of risks. Unfortunately, a great number of businesses adopt a myopic view when it comes to management of risks associated with their IP.

A common misconception associated with IP rights is that they protect themselves, when in reality the business that owns the right itself is responsible for enforcing and defending its rights. This generally translates into incurring legal costs and other professional advisory expenses.

Risk to the IP owned by a company may originate from any of the following sources:

Employees

It is not uncommon for an employee to leave an organisation and carry critical confidential information to pass it on to a competitor. Much of the time the divulgence is non-malicious but in some cases the employee may seek to obtain advantage from using this information whether it be client information, trade secrets or other forms of IP. Either way, the company is forced to drain its financial resources in enforcing its rights. Conversely, if a new employee joins a company carrying protected information from the previous employer, this can create a problem for the new employer. If put to use, this information can put the company in a scenario where it has to defend an infringement claim from the previous employer.

Further, employees are a key source of creation of new intellectual property. It is generally accepted that any IP created during the course of employment is owned by the employer. However, with the boundaries between professional and personal time blurring, it is becoming increasingly difficult to define and pinpoint whether the work was conducted in relation with employment or not.

Manufacturing partners

Businesses now want to focus on core value-generating activities and want to outsource others. Manufacturing is one such activity that gets outsourced, mostly outside New Zealand. However, it is critical that businesses are cognisant of the fact that they are disclosing this technical know-how and the blueprint of the product to a third party who is domiciled in a foreign country. There is a possibility that the manufacturing

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Consequences of losing IP

In January 2018, Sinovel Wind Group (SWG), a Beijing-based wind turbine manufacturer was found guilty of stealing proprietary critical source codes from American Superconductor Corp (ASC)⁹. It is interesting to note that Sinovel was a former customer of ASC. Sometime in 2011, Sinovel contacted a disgruntled employee of ASC and paid him US\$1.7 million to steal the technology. It is estimated that ASC lost more than US\$1 billion in shareholder equity and had to reduce its workforce by almost 700 employees because of this corporate espionage.

Recognising your intangible assets ... and your inherent risks

“If 87% of company value and virtually all earnings growth derive from intangible assets then intangible assets are now a major, if not the single most important, source of company risk. Boards and senior management teams need to take intangible asset risk far more seriously than they currently do. In 750+ client engagements, we have only found one company that noted intangible asset risk on their risk register, yet these assets can dramatically impact a company’s value.”

Paul Adams
Chief Executive Officer



partner may use the technical know-how in a way that is not permitted under the contract, putting the business in the difficult situation of having to enforce its rights. Enforcing these rights in other jurisdictions can sometimes be very challenging.

Distribution partners

Licensing or franchising is a common way of commercialising IP. However, even with stringent due diligence in place, there is a possibility that the licensee will end up using the IP in a way that is beyond the scope of the agreement. The ensuing dispute with the licensee will put financial pressure on the owner of the IP. Another plausible scenario is for the licensee to be hit with an infringement claim and the IP owner (the licensor) is obliged, contractually or otherwise, to defend their business partner.

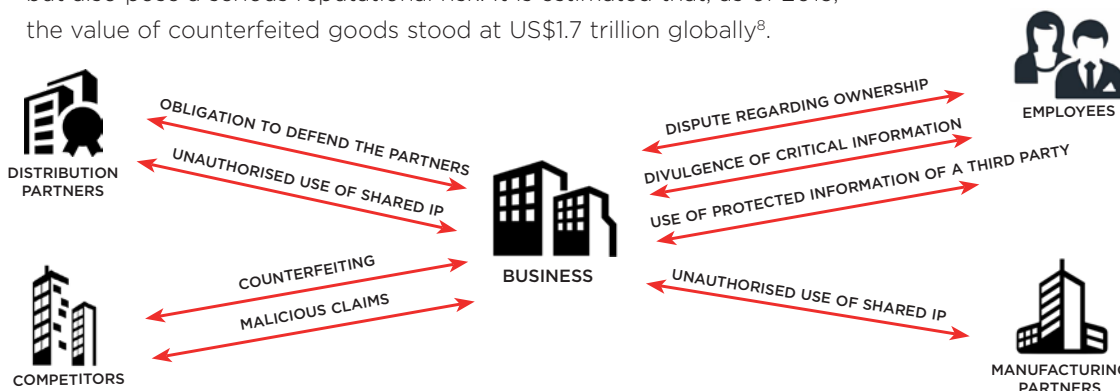
Competitors

Rivals can be a source of IP risk for a myriad of reasons. Some of the lawsuits involving competitors could be genuine. Others, however, act as an abusive tool to gain market share or stall the launch of a new product. The patent wars in the smartphone industry serve as an excellent example of how giants in the industry use lawsuits to acquire technology from startups.

Counterfeiting is another major exposure for a company. Counterfeiters, a company’s illegal competitors, not only damage a company financially but also pose a serious reputational risk. It is estimated that, as of 2015, the value of counterfeited goods stood at US\$1.7 trillion globally⁸.

What is the third shift?

Also called the ‘midnight shift’ or the ‘ghost shift’, this is a form of infringement by an authorised contractor or licensee. For instance, if a luxury brand outsources manufacturing of its shoes offshore, there is a possibility that once the contracted units are manufactured the contractor could run an additional shift to produce the product with inferior quality raw materials and sell the original looking replica in the local market.



Trends in IP Disputes

IP filing has reached a new high in recent years as global patent filing statistics show an increase of 8.3% in 2016 over the prior year¹⁰. Global trademark filing increased by 13.5% in 2016 over the prior year with approximately 9.7 million applications. China and the US are the main drivers of this increased filing activity.



Source: World Intellectual Property Indicators 2017

As an industry becomes concentrated with IP rights, it is expected that the disputes in the domain will rise. Multi-national enterprises (MNEs) are becoming more sophisticated with their IP strategy. They are proactively filing in territories which could potentially become important markets for them in the future to secure their rights. From an SME's perspective, this means that those who litigate are global with much more resources to enforce their rights.

A notable feature about IP lawsuits is that it not rare for them to either end with a licensing agreement between the parties or an acquisition being formalised. A commonality among IP lawsuits is that they are costly due to the specific techno-legal expertise required to handle these cases.

It is difficult to track and compare IP lawsuits on a worldwide basis because of differences between the court systems handling these cases. Further, some countries do not make this data public and a large number of disputes do not reach the court as a settlement is negotiated privately.

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IP Dispute Trends: US, China and New Zealand

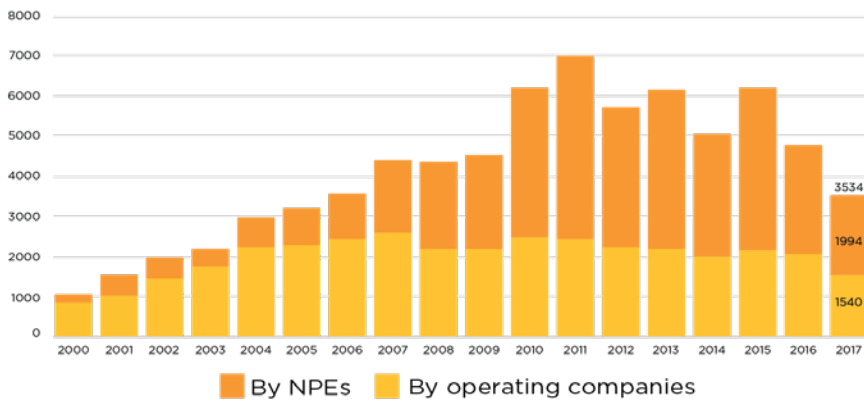
The following section tracks trends in IP disputes in the US, China and New Zealand.

The US

Lex Machina estimates that more than 31,000 patent infringement cases were filed in the US federal courts between 2012 and 2017. Trademark infringement cases between January 2009 and March 2016 were more than 28,000¹².

It is an unfortunate fact about the US business environment that there is an entire industry thriving by building an IP portfolio purely to bring about lawsuits against other companies. Non-practising entities (NPEs), colloquially known as patent trolls, acquire patents with no intention of commercialising them. Their only objective is to enforce the right, either via litigation or licensing agreements. Post 2010, NPEs have consistently added more defendants than operating companies. (graph below). Research by RPX Corporation showed that NPEs added 454 more defendants to patent lawsuits than operating entities¹³.

DEFENDANTS ADDED TO US DISTRICT COURT PATENT CAMPAIGNS ANNUALLY



Source: RPX Corporation

The figures indicate that the threat of an infringement lawsuit from an NPE is as prominent as that from a competitor.

Local operation but global competition

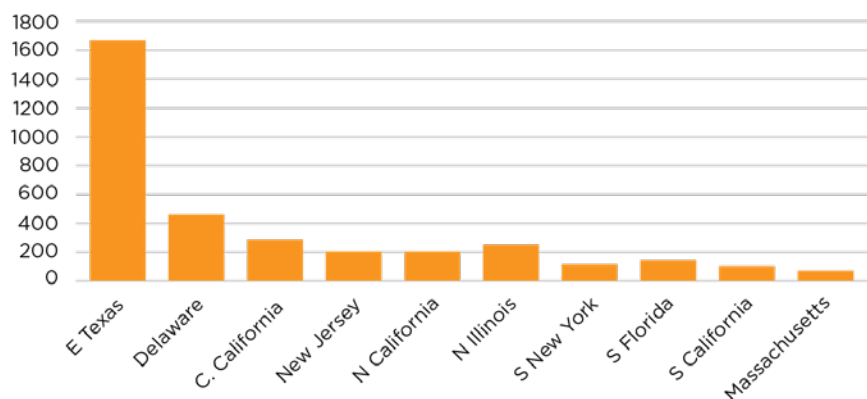
In 2018, a multinational meal-kit company called HelloFresh issued a cease and desist letter to New Zealand-based My Food Bag company over the use of words 'Hello Fresh'¹¹. HelloFresh owns registration for its logo in New Zealand which includes the words 'Hello Fresh'. It is worth noting that when the letter was issued HelloFresh wasn't even operating in New Zealand. In the Pacific region, Australia is an important market for HelloFresh and since they saw New Zealand as their next natural market, they registered their trademark well before their entry. It also highlights that the company was closely monitoring use of its trademarks and was proactive in taking legal steps where it saw a potential infringement.

The recent landmark case of TC Heartland vs Kraft Foods has impacted the modus operandi of trolls significantly. The judgement of the case has made forum shopping difficult for trolls. Hence, they are now actively targeting SMEs and startups. The methodology is simple: sending mass mails alleging infringement to hundreds of startups with a proposition to either pay a one-time fee or to face a costly lawsuit. Once a company succumbs to the demand, it exposes itself to other NPEs who would view this company as an attractive target.

Zeacom, once an Auckland-based software company and now part of Canada's Enghouse Systems, was hit by patent trolls twice. The company paid \$350,000 in the first instance instead of opting to incur millions to fight the baseless allegation. The second incident was settled for an undisclosed amount¹⁴.

Aggravating the threat of being the target of an NPE are the high legal costs in the US (with little or no prospect of recovering costs), which can put survival of a business in jeopardy. Toymaker Zuru Ltd had to incur US\$10 million in legal expenses in the US while pursuing its competitor, Telebrand Ltd, for infringing on one of its stellar products. Zuru Ltd was awarded US\$12.3 million by the court as part of the damages¹⁵.

NEW PATENT CASES IN 2016 BY DISTRICT



Source: Lex Machina

Recent high profile IP lawsuits in the US

Nintendo, a gaming console manufacturer, was ordered to pay US\$10 million as damages in 2017 to iLife Technologies. iLife Technologies brought a lawsuit against the gaming giant over infringement of its motion sensing technology¹⁸.

Samsung was ordered to pay US\$120 million to Apple in 2017 for infringing on its slide-to-unlock and quick link patents. The first ruling was delivered in 2014 and this patent war finally settled in 2017¹⁹.

What is forum shopping?

In the patent litigation parlance, forum shopping (or venue shopping) is the practice of deliberately opting for a jurisdiction or a court that is most probable to give a verdict in favour of the patent holder (including the troll). The Federal District Court of Eastern Texas has a history of being plaintiff-friendly. Hence, a lot of high-stake technology litigations were filed in this specific court until recently¹⁶.

The impact of the TC Heartland case

The verdict of the US Supreme Court in the TC Heartland vs Kraft Foods case has given much needed clarity on the venue in the patent infringement cases¹⁷. Prior to this case, the interpretation was that a plaintiff could bring a claim anywhere the defendant had business which was alleged to be infringing. This meant that even if a company had a website in a state where they had no physical presence it could still be sued there. This led to the development of the controversial trend of forum shopping. The TC Heartland case has made it clear that a plaintiff can sue only in the jurisdictions where (a) the defendant is incorporated or (b) has a regular and established place of business. This ruling is expected to change the demographics of patent litigation in the US significantly.

In 2017, mass market retailer Costco was ordered to pay US\$19 million for infringing on trademarks owned by luxury jewellery retailer Tiffany & Co. The case related to sale of diamond rings in store by Costco using the word 'Tiffany'²⁰.

Another open secret about the business environment in the US is the fact that already established companies will often try to thwart entry of a new entrant by initiating frivolous lawsuits. The fact is that, in most of the states, the defendant cannot recover legal costs from the plaintiff even after a successful defence – this clearly works in favour of larger and established players in an industry. This feature played a role in how Vlingo was acquired by Nuance. Vlingo, a US-based company developed voice-to-text technology. Soon it was contacted by its much bigger competitor Nuance with an acquisition offer. When Vlingo refused the offer, they were hit by six patent infringement claims by Nuance. As a matter of fact, they won the first one. However, to win the suit the company had to sustain legal costs to the tune of US\$3 million and soon it was left with no resources to fight the rest of them. Vlingo was ultimately acquired by Nuance in 2011²¹.

China

China has put in considerable efforts in the last few years to strengthen its IP protection framework. China saw a drastic improvement in its scores on the Global International IP Index and was ranked 25th in 2018 out of the 50 countries profiled²². The government has undertaken various programmes to educate and sensitise businesses about the importance of IP. Even with all these developments, the risk of an IP being compromised in China remains ever-present. A survey conducted by the American Chamber of Commerce in China in 2017 indicated that more than half of the respondents were sceptical about enforcement of IP laws in China²³. Chinese courts handled 213,000 IP-related cases in 2017. This figure has doubled since 2013²⁴.

Trademark-related cases are the second highest percentage of cases being heard by the courts. This is particularly important for New Zealand companies as products from New Zealand are able to command a price premium because of the country of origin.

The regulation for trademark registration is on a 'first to file' basis in contrast to a 'first to use' basis in other countries. This difference in regulation has led to emergence of an army of 'trademark squatters' who scout for companies who are planning to enter China²⁵. Trademark squatters register brands of these companies and sell it back to the original owner for an exorbitant amount. It is reported that Apple had paid US\$60 million to a squatter to gain the ownership of the 'iPad' trademark in China²⁶. New Zealand-based household product manufacturer Ecostore and food manufacturer Cookie Time had to go through a cumbersome process to regain their trademarks in China²⁷.

Striking the balance

In 2017, US shoemaker, New Balance was awarded US\$1.5 million in damages and legal costs²⁸. The court ruled against three Chinese companies that were using New Balance's slanted "N" logo. It is reported that this is one of the heftiest trademark infringement damages awarded to a foreign entity in China against a Chinese company.

This difference in regulation between a 'first to file' and a 'first to use' has led to emergence of an army of 'trademark squatters' who scout for companies who are planning to enter China²⁵.

The prevalence of counterfeit goods is another hurdle in China. A report by the OECD in 2013 indicated that close to 63% of counterfeited goods that were seized originated from China²⁹. Zespri, the marketer of kiwifruit from New Zealand, is constantly battling against fake fruit available in the Chinese market that bear a logo similar to its brand Zespri³⁰. BFM Fittings, a New Zealand company, recently managed to block two counterfeiters in China who were manufacturing its patented industrial pipe couplings³¹.

New Zealand

New Zealand businesses are increasingly appreciating and understanding the value of IP protection. A quick look at the number of trademark and patent filings by New Zealand companies indicates increased activity in the IP landscape.

It is expected that with this increase in awareness, companies are engaging themselves in protecting and enforcing their IP rights.

Interestingly, it is estimated that close to 50% of the issues do not even reach the stage of formal pleadings. A settlement is negotiated between the parties at an initial stage of the dispute. Hence, the picture regarding IP-related litigation will always remain understated.

New Zealand has seen its fair share of complicated and intricate lawsuits. The end of 2016 saw two milk manufacturers embroiled in a dispute over packaging of the products³². Energy drink manufacturer, Red Bull had to engage in a lengthy legal process to bring about an injunction against the sale of its own drink pre-mixed with vodka under the brand name 'Drink Red'³³.

New Zealand companies can no longer afford to ignore IP considerations when conducting business simply because their global counterparts are leaving no opportunity to enforce their rights. For instance, a café in Wellington received a legal notice by Coca-Cola in 2017 for using trading under the name 'Innocent Foods'. Coca-Cola owns the right to use 'Innocent' as a trademark. The café had to undergo a rebranding exercise to avoid infringement³⁴. Fisher and Paykel Healthcare is currently engaged in a complicated legal scenario against its rival ResMed over enforcement of its patents related to medical devices. Fisher and Paykel Healthcare has already incurred legal expenses of \$20.7 million in the financial year 2017³⁵.

Phitek, a New Zealand-based electronic manufacturer, was hit with a patent infringement by its US-based competitor Bose in 2008 over noise-cancellation technology used in headphones. As part of the settlement agreement, Phitek had to make changes in its headphones to avoid patents owned by Bose³⁶.

INTELLECTUAL PROPERTY GRANTED/REGISTERED USING
WIPO ADMINISTERED TREATIES - RESIDENT FILING

YEAR	PATENTS GRANTED	TRADEMARKS REGISTERED	INDUSTRIAL DESIGN REGISTERED
2014	389	6871	286
2015	344	7104	293
2016	304	6960	249

Source: World Intellectual Property Organisation

A quick look at the number of trademark and patent filings by New Zealand companies indicates increased activity in the IP landscape.

Risk Management Framework – Intangible Assets

While the competitive advantage has shifted from tangibles to intangibles, unfortunately, the risk management practices adopted by companies today largely focus only on tangible property. Managing intangible asset risks should be a board-level issue considering the dependence of businesses on them and they can no longer be entrusted to just one department.

It is failure to adopt a holistic strategic paradigm that forces companies to adopt a reactive approach to a crisis rather than a preventive approach. The following framework, contributed by EverEdge, would help in taking a structured approach towards protecting IP.

Step 1: Identify critical intangible assets

As basic as it sounds, this is one of the most important steps towards developing a robust risk management programme. A company needs to identify not only the intangible assets owned by it but also licensed to it by a third party. It is critical that a company identifies co-created IP as well, such as IP created in collaboration with a joint venture partner. Maintaining an IP inventory is a useful tool that can be used at this stage. The inventory log captures details regarding registered/unregistered intangible assets, their renewal status, internal departments that are authorised to use it and external partners that have access to them. This tool would assist in locating the risk source and best way to contain a risk in case of a crisis.

Step 2: Assess the risks

This step involves undertaking a comprehensive review of the risks an asset is exposed to and understanding the financial implications if the intangible asset is compromised. For instance, if a patent that is core of the product developed by a company is infringed, the company would sustain extensive financial and reputational damage. The company will have to engage technical consultants and lawyers to bring about an injunction. In contrast, if content of a website is copied, same can be managed without causing as much damage. This step helps an organisation to decide on the specific strategies and resource allocation for each asset. Developing a risk-mapping document is a valuable tool. This document captures details related to probability of a risk occurring, its potential consequence in terms of loss of business or a litigation being initiated against the company, and response to the risk.

Step 3: Manage the risks

Identifying response to a risk takes a specific and tailor-made approach based on the exposure and an organisation's objective. There are certain practices that a company can adopt at a broader level to minimise it:

Organisational Policies: A lot of companies miss out on addressing specific intangible asset issues while laying down general policies and procedures. It is vital that a company reviews its employment contracts to explicitly state that the organisation is the ultimate owner of the intellectual property being created and tighten its non-disclosure clauses. Further, it is important that contracts with external parties like suppliers and licensees clearly define the terms and conditions regarding the use of information being disclosed to them. Another common mistake that startups generally commit during their early stages is being unclear about the ownership of the IP among the founders. This can be a point of contention later, as the company grows.

IT Security: It is not surprising that a lot of cyber attacks are planned with the sole aim of stealing proprietary information held by a company. In spite of this, not a lot of cyber security programmes are devised to enhance the protection of intellectual assets.

Training: The most robust physical and network securities will fail to protect the assets if employees are not sensitised about perils of its disclosure. Basic training modules on the types of IP, criticality of each asset and potential scenarios of unintended disclosures in day-to-day life would equip employees to identify and avoid the pitfalls.

Continuous Monitoring: Protecting intangibles is not a one-time process but a continuous one where the company should regularly check the health of its IP portfolio. Hiring professionals to do so would help in aligning the IP strategy with business goals. Continuous monitoring also helps in restricting on-the-ground infringement at an early stage to contain the damage.

Step IV: Transfer the risks

Businesses should look at ways to transfer the risk wherever economically viable. By and large, insurers are playing catch-up as far as cover for intangible assets is concerned. Elements of coverage for IP infringement related risks exist across general liability and professional liability policies. Dedicated policies for covering intellectual property are provided by very few insurers and most of these are out of the UK or the US. Generally, these policies are very expensive and self-insured risk retentions are high, meaning that the level of risk transfer can be quite limited. Some insurers are actively working to make this cover affordable for SMEs.

This four-step preventative framework takes a structured approach towards protecting IP and should be seen as an ongoing continuous cycle to ensure an entity's intangible assets are protected.

EVEREDGE
UNLOCK YOUR EDGE

Intellectual Property Expense Insurance

Very limited coverage exists for IP under existing insurance policies. General liability policies tend to extend cover for copyright infringement during advertising and exclude other forms of IP rights.

Professional indemnity policies cover copyright and trademarks which are inadvertently breached but generally exclude patents and trade secrets. No liability policy provides cover for pursuit enforcement action, forcing most of the affected SMEs to let competitors eat away a share of their profits unless they have the financial resources to undertake such enforcement without an expectation of indemnity from their insurers.

Standalone IP policies have been in the market for approximately three decades, but the uptake of the product has been relatively negligible due to following reasons:

- > Insurers worldwide have struggled to define and provide structure to the risk being covered due to the intangibility and amorphousness of the assets.
- > As a result of the above, the appetite to underwrite these risks has been varying and insurers have historically focussed on a specific segment only.
- > The policies have been prohibitively expensive and have high attachment points, making it difficult for many companies to see value in the coverage.

At Delta Insurance, we identified a real demand from businesses to be able to protect their IP at a level that provides value but is also affordable.

The following analysis provides an overview of the Delta Insurance IP Legal Expenses coverage which is currently the only cover offered by a local provider in New Zealand. There are other products available overseas; however, we have not focussed on them for the purpose of this White Paper.

What insurance coverage is available?

Pursuit Cover for Infringement Pursuit

This pays for legal expenses to pursue a third party for an allegation of infringement of the covered IP.

Example

The insured, an exporter of Manuka honey, uses its registered trademark as a branding tool as well as a certification mark to show potential customers that the product meets strict quality standards and regional authenticity. Following receipt of information that an unauthorised company was using the trademark on their packaging, the insured felt they must undertake cease and desist measures.

The insured engaged lawyers to prevent the unauthorised user from continuing to use the trademark and to seek damages. Following initial resistance, court proceedings followed. The insured was ultimately successful and managed to recover some 35% of the legal costs incurred. However, the remainder of \$36,000 incurred was covered by the Legal Expenses Insurance and further abuse of the trademark was prevented.

Defence Cover for Infringement Defence

Pays for legal expenses to defend an allegation of infringement against the insured over the use of the covered IP.

Example

The insured recently secured a patent for an advanced tractor-suspension system. While the insured is a relatively new and fast-growing company, they were careful to do their research before bringing the product to the market. Their patent agent conducted extensive searches and freedom to operate advice was received.

However, following adoption and agreement of exclusive-use licences with a major tractor manufacturer, a cease and desist letter was received. The insured felt that the action against them was groundless and thus was prepared to strenuously fight any allegation of infringement. The insured was covered by the Legal Expenses Insurance for the \$57,000 of legal costs incurred in defending the allegations and subsequently had their patent validated by the Court.

Revocation Cover

The cover pays for legal expenses to defend an action disputing ownership of an IP right.

Protection of Exclusive Licensee for Licensee Defence

This pays for the legal expenses the insured incurs to defend an infringement allegation against the licensee arising because of use of the insured IP.

Example

The insured granted their patented solution to a major semi-conductor manufacturer in Taiwan. Following many years of a partnership, a new entrant came into the market. The new entrant began proceedings against several Taiwan-based semi-conductor manufacturers for alleged breaches of a patent portfolio they had acquired recently, in addition to their own innovations. Not only were they seeking damages but also revocation of the alleged infringer's patents.

While the licence agreement did not specifically require the insured to indemnify the licensee for any infringement defence costs, given the close and profitable relationship that the insured and licensee held, the insured was happy to assist the licensee in their infringement defence.

The insured was indemnified for the costs incurred by the licensee, as well as their own defence of revocation costs, by the Legal Expenses Insurance. This amounted to some \$143,000, although some limited recovery of costs was later achieved.

Contractual Dispute Protection for Licensee Pursuit

The cover pays for legal expenses incurred because of dispute with a licensee over the use of IP.

Example

The insured agreed with a distributor to grant an exclusive licence to manufacture trademarked toys in China for later distribution in the New Zealand market. The licensee was granted a 12-month exclusive IP usage and manufacturing agreement. Part-way through the contract the insured discovered the manufacturer was also distributing the toys in the Chinese market.

The insured was forced to seek a replacement manufacturer to maintain exclusivity and manufacturing standards. The insured was covered by the Legal Expenses Insurance to pursue the additional costs of working incurred and breach of intellectual property rights, obtaining an out of court settlement.

Public Relations Expenses

This pays for public relations expenses arising out of covered disputes under scenarios listed above.

Conclusion

There is little doubt that intangible assets have become a critical success factor in the ongoing competitiveness of a business. These assets help to differentiate a business from its competitors, act as a source of revenue and, at times, are the very reason for the existence of a business.

As technology advances, it is inevitable that their importance will continue to grow. With more companies globally protecting their intangibles by filing IP rights, they have transitioned from being a legal issue to a strategic business issue. Increasingly, these protected intangible assets are becoming a central premise for investments and M&A transactions.

New Zealand businesses cannot afford to ignore the fact that they are now competing against many companies with significant financial and technical resources to protect and enforce their rights.

Therefore, IP risk management needs to be a strategic issue for New Zealand business. Overlooking this critical factor can put the company's board and management under significant pressure and potentially place the very survival of a business in jeopardy.

Effective management of IP ensures that a business can unlock maximum value from its R&D investment and positions the business to achieve a sustainable competitive advantage.

Ultimately, one of the biggest drivers in the sustainability of an organisation's success is not only its innovation and uniqueness, but more importantly, its ability to safeguard these advantages. By developing a comprehensive and proactive intellectual property protection strategy, organisations can continue to prioritise their goal of value creation.

"Kiwi businesses are known for their 'No. 8 wire' mentality and innovativeness. Unfortunately, even with strong IP protection businesses can still fall prey to costly and extortionate acts. Strategic risk management of these assets is critical, and insurance has a major role to play in it."

Craig Kirk,
General Manager

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Notes

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EverEdge Global – Contributor

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