Lawyer Insights

Solefully Designed: Insurance Coverage Tailored for the Sneaker Industry

By Latosha Ellis and Jae Lynn Huckaba
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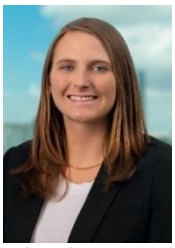

Major sneaker brands have capitalized on new trends in technology and social media to publicize sneaker culture. As sneakers become more popular, sneaker collections increase in value, thus increasing financial exposure for collectors and other entities in the sneaker industry. One might first think of theft, authentication, fire, floods, or market valuation as the general risks associated with sneaker collections. But many sneaker companies have made headlines over the past few years with lawsuits against other sneaker companies and entities, with issues ranging from traditional patent battles to exhaustive fights against counterfeiters. Often overlooked by collectors and sneaker companies alike, insurance can be vital to helping both collectors and companies faced with unexpected liability related to sneaker culture.

Given how much money is at stake in the industry—nearly $72.2 billion currently and expected to reach $100 billion by 2026—it should come as no surprise that sneaker companies are using intellectual property ("IP") law to protect their assets. For example, in early 2022, a large shoe manufacturer sued an online sneaker resale marketplace, asserting claims for trademark infringement of the shoe manufacturer's non-fungible tokens ("NFTs"), counterfeiting, and false advertising after a sneaker collector and reseller bought thirty-eight pairs of counterfeit sneakers from the resale marketplace. The litigation has likely been costly and damaging for the online reseller because of the extensive discovery process, including a discovery dispute resulting in a court order requiring the online reseller to produce information about the identity of known users who sold counterfeit sneakers through the company's resale platform. The same large shoe manufacturer also sued a major athletic apparel retailer in January 2023 for alleged infringement of footwear patents.

Sneaker companies and other entities on the receiving end of IP lawsuits—including, for example, third party retailers and online resellers—should be able to leverage their IP or commercial general liability ("CGL") policies for insurance coverage for defense costs in IP lawsuits related to sneakers and their director's and officer's ("D&O") policies for any downstream lawsuits against executives of sneaker companies.

IP INSURANCE

IP insurance covers the initiation or defense of claims for IP infringement. This means a sneaker company can leverage IP insurance to enforce its intellectual property rights against suspected infringement and to defend against allegations of infringement. Like many types of coverage, IP policies often cover litigation costs and expenses as well as potential judgments and settlements.

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CGL INSURANCE

While IP insurance, which protects a business from allegations of infringement of another business's intellectual property, may be the obvious source and first line of defense for coverage for IP claims related to sneakers, coverage may also be available under a CGL policy. Most CGL policies do not explicitly include patent infringement coverage. In fact, most CGL policies include an IP exclusion that expressly excludes patent infringement coverage, but insureds may still be able to secure coverage. Most IP lawsuits are conjoined with other allegations, such as unfair competition, which some courts have found to be fundamentally the same as an asserted trademark infringement claim,[1] thereby potentially implicating coverage under the CGL policy that the insurer acknowledges and defends. A complaint that alleges infringement of a competitor's patent may also allege defamation and disparagement of its product. Because claims for defamation and disparagement are typically covered under CGL policies, there may be defense coverage related to those covered claims. Thus, it is crucial to closely review factual allegations in the complaint that might bring the lawsuit within the scope of CGL insurance coverage.

A claim for patent infringement may also be covered under "advertising injury" that falls outside the scope of the policy's IP exclusion. Some courts have held,[2] under certain versions of the standard CGL form, that a trademark constitutes an "advertising idea," meeting the definition of "advertising injury" as that term is typically defined in standard CGL policies. In other words, the misuse of another's trademark may constitute appropriation of an advertising idea, which falls within the coverage typically provided under a CGL policy form. Willful acts of infringement are generally not covered, though; the infringement must be inadvertent.

There are some CGL policies that provide direct coverage for IP claims and do not include explicit exclusions. For example, the insured may be able to negotiate a CGL policy without an IP exclusion by agreeing to absorb routine defense costs and fees through a self-insured retention, a specific amount that the insured must pay before the insurance policy responds to a loss. A policy that includes a self-insured retention shifts some of the risk from the insurer to the insured, which in some cases allows the insured to negotiate terms that provide direct coverage for IP claims. Sneaker companies, particularly those with significant capital, may want to consider negotiating a self-insured retention in order to procure direct coverage for IP claims under a CGL policy.

D&O INSURANCE

D&O insurance may also cover claims in sneaker-related lawsuits against individual business leaders, such as directors, officers, or certain company executives, arising from certain actual or alleged acts, such as failing to adhere to state or federal laws, unethical practices, or fiduciary duty mismanagement. Companies within the sneaker industry, for example, may be subject to Securities and Exchange Commission investigations that implicate the sneaker company, as well as its individual officers and directors. A D&O policy typically covers the defense costs and expenses the company incurs during such investigations.

D&O insurance may also protect sneaker companies against lawsuits for theft of intellectual property. This is because IP-related claims often constitute a wrongful act, as that term is defined in the D&O policy, if the directors and officers are named as defendants in the IP lawsuit. If faced with allegations of IP infringement, sneaker companies should consider coverage under D&O policies that may complement any coverage afforded under CGL policies.

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INSURANCE FOR COLLECTORS

Insurance for sneaker-related claims, however, is not limited to sneaker companies. As sneakers become increasingly valuable, even individual collectors can consider insurance coverage options. Traditional homeowner's insurance typically covers personal property, including sneakers. But a traditional homeowner policy does not cover authentication issues, such as the counterfeit issue in the lawsuit mentioned earlier, or other risks unique to sneaker collecting and investments. To that end, sneaker insurance for individual sneaker collectors exists, which insures against a broader range of risks than traditional homeowner policies.

While homeowner's insurance policies often exclude coverage for property damage resulting from or arising out of flooding, sneaker insurance typically provides some coverage for flood damage. Larger collections, in particular, are more vulnerable to potential disasters, making purchasing comprehensive insurance a necessary step in protecting a collector's investment. Policies tailored for sneaker collections also provide coverage for sneakers lost or stolen during shipping, delivery, and travel—losses that are usually not covered under traditional homeowner policies. Sneaker insurance facilitates collectors' profiting from their investment through resale while decreasing exposure to the risks of shipping and delivery of valuable sneakers. Another advantage to sneaker insurance is that the sneakers are valued and authenticated during the underwriting process and insured at replacement cost, rather than actual cash value, allowing the collector, in most cases, to avoid incurring a loss because of depreciation or a decline in market value for the sneaker.

Sneaker collectors, however, should understand that sneaker insurance is an emerging market, and options are somewhat limited. This means high premiums for coverage, particularly because insurers in the sneaker industry are likely attuned to the nuances of the sneaker market and may tie premiums to market fluctuations.

CONCLUSION

Insurance is a great way to mitigate and hedge against the risk of unforeseen losses in the sneaker industry. CGL policies, D&O coverage, and sneaker insurance provide sneaker companies and collectors with various routes to securing coverage when faced with losses, including costly litigation. But the sneaker industry, especially sneaker companies with greater vulnerability to lawsuits, should recognize that insurance policies are often narrowly tailored to exclude the very claims that pose large risks to sneaker companies and collectors alike. Sneaker companies and collectors should consult experienced insurance coverage counsel to carefully consider all insurance options to protect their assets and investments.

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Notes

1. *See, e.g., Land's End at Sunset Beach Cmty. Ass'n, Inc. v. Aspen Specialty Ins. Co.*, 745 F. App'x 314, 319–20 (11th Cir. 2018) (finding that the fact allegations in the underlying action for the counterclaims of false designation and unfair competition "require elements of proof beyond [intellectual property] use and [the fact] that those types of claims may exist absent [intellectual property] infringement does not alter the analysis . . . [and] depend on [the insured's] use of [the intellectual property]'"); *see also Marvin J. Perry, Inc. v. Hartford Cas. Ins. Co.*, 412 F. App'x 607, 614 (4th Cir. 2011) (finding that a plaintiff's claim for unfair competition was based on another's use of the plaintiff's trade name, trademark, logo, and website in violation of the plaintiff's ownership of the trademark). ↥

2. *See, e.g., Lebas Fashion Imports of USA, Inc. v. ITT Hartford Ins. Group*, 50 Cal. App. 4th 548, 557, 565–66 (2d Dist. 1996) (construing the phrases "advertising idea" and "style of doing business" in a CGL policy broadly to provide coverage for trademark infringement, as "a trademark is but a species of advertising"). ↥

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