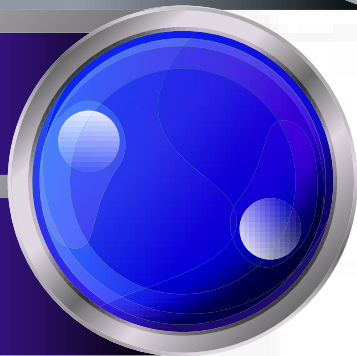




TOPE ADEBAYO LP



# **INNOVATING FINANCE:**

**HOW IP INSURANCE CAN  
TRANSFORM NIGERIAN  
INNOVATIVE STARTUPS.**

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## INTRODUCTION

In the evolving global economy, intellectual property (IP) has emerged as a critical asset for businesses, especially for startups and innovation-driven enterprises. IP assets, including patents, trademarks, and copyrights, represent significant value for many companies, but leveraging them to secure financing has traditionally been fraught with challenges, primarily due to the difficulty in accurately valuing such assets and the risks associated with their future revenue generation potential.

Insurance products tailored to IP assets offer a solution to these challenges, providing a safety net to both lenders and borrowers and enabling more secure and scalable financing solutions. A company's intangible assets, such as intellectual property (IP), which includes software, patents, copyrights, and customer goodwill, now account for a larger portion of a business's value in the innovation sector than its physical assets.<sup>1</sup> Although these intangibles now account for 90% of the S&P 500's value, many businesses still fail to protect them; only 17% of the intangible assets' value is insured against potential loss, which poses a serious risk to the com-

pany's ability to operate sustainably.<sup>2</sup>

This article explores the role of insurance in facilitating intellectual property (IP)-based financing, a growing area of interest for innovative firms seeking capital.

## THE STATE OF IP-BASED FINANCING IN NIGERIA

In Nigeria, like in many other parts of the world, intellectual property has become a critical asset class for businesses, especially those in the technology, entertainment, and creative industries. IP-based financing, which involves using intellectual property assets such as patents, copyrights, trademarks, and trade secrets as collateral for loans, presents a significant opportunity for Nigerian businesses to access the capital necessary for growth and innovation. However, despite the potential benefits, the adoption of IP-based financing in Nigeria faces several challenges.

Nigeria's economy, being the largest in Africa, is home to a growing tech ecosystem, a thriving entertainment industry, and a vast array of SMEs across various sectors.<sup>3</sup> These entities often possess valuable IP assets that

<sup>1</sup>Ocean Tomo, Intangible Asset Market Value Study, <https://oceantomo.com/intangible-asset-market-value-study/>

<sup>2</sup>AON, Intellectual Property: An Asset to Protect and Leverage in the Technology, Media & Communications Industry, (Dec. 5, 2023) <https://www.aon.com/en/insights/articles/intellectual-property-an-asset-to-protect-and-leverage-in-the-technology>

<sup>3</sup>Europa Regina, Nigeria Creative Industries, (2021), <https://europaregina.eu/creative-industries/africa/nigeria/#:~:text=According%20to%20the%20report%2C%20the> (last visited Nov 4, 2022); See, Victor Oluwale, New Report Shows Nigeria's Creative Industry Is the Country's second-largest Employer and Has the Potential to Produce 2.7million Jobs by 2025, BI Africa, 2021, <https://africa.businessinsider.com/local/lifestyle/new-report-shows-nigerias-creative-industry-is-the-countrys-second-largest-employer/mky68v9> (last visited Nov 3, 2022).

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could be leveraged for financing. The Nigerian government and various stakeholders have recognized the importance of IP as an economic asset, leading to reforms aimed at strengthening the IP legal framework and encouraging innovation.<sup>4</sup>

However, the utilization of IP-based financing remains relatively low compared to more traditional forms of financing.<sup>5</sup> This can be attributed to a combination of factors, including a lack of awareness, underdeveloped financial products tailored to IP, and the challenges inherent in valuing and managing IP assets.

## Challenges with Embracing IP-Based Financing in Nigeria

1. **Valuation of IP Assets:** One of the primary challenges is the difficulty in accurately

valuing IP assets. Unlike tangible assets, the value of IP is not straightforward and requires a deep understanding of the market, technology, and legal environment. This complexity makes lenders hesitant to accept IP as collateral.

## 2. Legal and Regulatory Framework:

While there have been improvements in Nigeria's IP legal framework, there are still gaps, especially in enforcement and protection against infringement. The lack of a robust legal framework for IP rights protection makes financiers wary of the risks associated with IP-based lending. High rates of IP infringement and piracy in Nigeria pose significant risks to the value of IP assets, making them less attractive as collateral.

3. **Awareness and Capacity:** There is a general lack of awareness among both IP

<sup>4</sup>In 2017, The Secured Transaction on Movable Assets Act (STMA), which was passed to stimulate lending to micro, small, and medium enterprises and to facilitate access to credit secured with movable assets; The Companies and Allied Matters Act 2020, provides for the creation of charges over intellectual property assets; The Start-Up Act 2022, was passed with the objective to provide an enabling environment for the establishment, development, and operation of startups in Nigeria; An amended Copyright Act, was passed in 2022, that seeks to strengthen the effective administration, regulation, and enforcement of copyright in the digital world.

<sup>5</sup>Claire Philpott & Susan Jahnke, Intellectual Property: A new Collateral, Puget Sound Business Journal (Mar. 6, 2005, 9:00 PM), <https://www.bizjournals.com/seattle/stories/2005/03/07/focus9.html>.

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holders and financial institutions about the potential of IP-based financing. Additionally, there's a gap in technical expertise required to assess, value, and manage IP assets effectively.

**4. Market and Infrastructure Development:** The Nigerian financial market's readiness for sophisticated financial products like IP-based financing is still in its infancy. There needs to be more developed financial infrastructure and markets for IP-based financial products.

### CURRENT STATE OF INSURANCE MARKET IN NIGERIA

Nigeria's insurance sector, while still growing, faces several challenges including low penetration rates and a general lack of public trust.<sup>6</sup> Despite these hurdles, the industry has shown resilience and potential for growth.<sup>7</sup> The key segments in the Nigerian insurance market are life insurance and general insurance. The market is dominated by traditional insurance products such as life, car, and health insurance, which have been crucial in providing a safety net for individuals and businesses alike. Apart from these, there are other insurance products in

the market, such as property insurance, travel insurance, and agricultural insurance, the latter gaining attention due to the significant role of agriculture in Nigeria's economy. However, these products have not reached the same level of penetration as life, car, and health insurance.

The sector's growth is, however, hampered by infrastructural deficiencies, regulatory hurdles, weak corporate governance, poor risk management practices, and a limited understanding of insurance products among the populace. A significant portion of the Nigerian population has limited awareness and understanding of insurance products and their benefits. This lack of knowledge contributes to low uptake and skepticism towards insurance services. Additionally, there is a prevalent issue of distrust towards insurance companies, partly due to past experiences where policyholders faced challenges in claiming benefits. This skepticism has greatly hampered the growth of insurance enrollment.

Addressing the issue of regulatory hurdles, the regulatory body, NAICOM, has made strides in reforming the sector. Recent reforms introduced by NAICOM aim to

<sup>6</sup>Global Data, Nigeria Insurance Industry - Key Trends and Opportunities to 2025, Market Research Reports & Consulting | GlobalData UK Ltd. (2023), <https://www.globaldata.com/store/report/nigeria-insurance-market-analysis/> (last visited Apr 9, 2024).

<sup>7</sup> Editorial, 2023: Year Insurance Became N1tn Market - THISDAYLIVE, ThisDay Newspaper, Dec. 27, 2023, <https://www.thisdaylive.com/index.php/2023/12/27/2023-year-insurance-became-n1tn-market> (last visited Apr 9, 2024).



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strengthen the sector's capacity to support economic growth. These include increased capital requirements for insurers to ensure their solvency and the promotion of more innovative insurance products.<sup>8</sup> However, the effectiveness of these regulations in fostering a robust insurance market that can contribute significantly to innovation financing remains to be fully realized. It is important to state that regulations around microinsurance and the encouragement of insurance technology (InsurTech) initiatives have stimulated innovation within the sector, leading to the development of products and services tailored to the diverse needs of the Nigerian populace.

### IP-INSURED FINANCING AND THE POTENTIAL FOR THE NIGERIAN INSURANCE MARKET

IP insurance is an important type of IP-based financing, as well as a means to resolve IP asset risks, by providing a financial safety net for companies that own valuable intellectual property.<sup>9</sup> IP-insured financing provides security for the value of a company's intellectual property assets that are used as collateral for a loan. By providing a layer of insurance protection to intellectual



property and other intangible assets, this policy solution enables debt providers to lend to growth-stage technology companies, which are broadly defined as any businesses that use technology to create or develop products at a relatively low cost of capital and without requiring equity.<sup>10</sup> It allows lenders to have more confidence in providing financing to enterprises in the growth stage, which may lead to higher borrowing capacity and better loan conditions.<sup>11</sup> The assurance of an insurance policy provides banks with funds in the event of borrower default, which makes the bank more inclined to lend. The "insurance wrap" provides additional security, providing banks with capital relief by reducing the amount of capital they need to retain to cover the risk of the loan.<sup>12</sup>

<sup>8</sup>Fitch Ratings, Nigerian Insurance Sector Recapitalising, (2020), <https://www.fitchratings.com/research/insurance/nigerian-insurance-sector-recapitalising-18-02-2020> (last visited Apr 9, 2024).

<sup>9</sup>WIPO, Country Perspectives China's Journey Unlocking IP-backed Financing Series, (2023), <https://www.wipo.int/edocs/pubdocs/en/wipo-pub-rn2023-46-en-country-perspectives-china-s-journey.pdf> (last visited Apr 9, 2024).

<sup>10</sup>Paul Murray, Intellectual Property-Insured Financing, Marsh, <https://www.marsh.com/en/services/financial-professional-liability/expertise/intellectual-property-insured-financing.html> (last visited Apr 9, 2024).

<sup>11</sup>Id.

<sup>12</sup>See, AON, *supra* note 2.

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Insurance also serves as an essential tool for increasing the value of intellectual property assets. The following are some examples of how insurance contributes to the increase in value of intellectual property assets:

**1. Risk Mitigation and Investment Attraction:** Insurance policies for IP assets help mitigate the risks associated with the ownership and exploitation of these assets. By securing insurance, IP owners not only protect against potential financial losses from litigation but also make their IP more attractive to investors and business partners. This attractiveness stems from the reduced risk profile of the insured IP, which reassures investors and lenders that their investments are less likely to be jeopardized by IP-related disputes. For instance, a startup with a patented technology may find it easier to attract venture capital if its critical IP assets are insured, highlighting the direct impact on enhancing asset value by reducing investor risk exposure.

**2. Stabilizing Market Position:** IP assets insured against legal challenges such as infringement or invalidity claims can maintain their market position more effectively. Insurance enables IP owners to assert their

rights more aggressively and defend against unwarranted claims without the fear of overwhelming legal costs. This proactive legal position can deter potential infringers and uphold the asset's exclusivity in the market, directly contributing to its sustained value. Additionally, in industries where technological lifecycles are short, such as the tech industry, maintaining an unchallenged position can significantly enhance the return on investment during the patent's enforceable period.

**3. Enhancing Licensing Opportunities:** Insured IP assets are more likely to be licensed and at better terms. Insurance provides a layer of trust and reliability to licensees, who may be more willing to enter into agreements knowing that the IP is protected against potential legal challenges. This can lead to broader market reach and increased royalties, thus enhancing the revenue-generating potential of the IP. For example, a patented manufacturing process that is insured might be more readily adopted by larger corporations under license, providing the patent owner with a steady royalty income and an enhanced valuation of the patent.

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**4. Facilitating IP Valuation:** Insurance contributes to a clearer and potentially higher valuation of IP assets. The presence of insurance can be factored into IP valuation models, providing a more robust estimation of the asset's value by accounting for risk reduction. Valuation professionals may consider an insured IP asset less risky, and hence more valuable, as the potential costs and disruptions associated with IP disputes are mitigated. This modified valuation is crucial during mergers & acquisitions, and fundraising activities, where the value of IP assets often significantly impacts the overall deal value.

**5. Leveraging Insurance in Strategic Planning:** IP insurance enables companies to plan more effectively for the future. Knowing that potential IP litigation costs are covered, companies can allocate resources towards innovation and expansion rather than allocating substantial funds for legal defenses. This strategic allocation of resources not only enhances the operational efficiency of the company but also increases the developmental pace of new IP, thereby enhancing the overall portfolio value.



The potential of IP insurance in Nigeria is vast, offering significant opportunities to promote the growth of innovative enterprises and the broader economy. To, however, effectively leverage this opportunity, a multi-faceted approach is proposed:

**1. Legal and Regulatory Framework:**

Establishing clear legal guidelines for IP valuation and collateralization is fundamental. This involves reforms to intellectual property laws and financial regulations to recognize IP assets as viable collateral.

**2. Development of IP Valuation Expertise:**

Building local capacity in IP valuation is crucial for assessing the value of IP assets accurately. This could involve training programs and the establishment of specialized firms or units within existing financial institutions.

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### 3. Partnerships with Global Insurers:

Collaborating with international insurance firms that have expertise in IP insurance can accelerate the development of local markets. These partnerships can facilitate knowledge transfer and capacity building.

**4. Awareness and Education:** Raising awareness among startups, SMEs, financiers, and insurers about the benefits of IP-based financing and insurance is essential for creating demand and fostering an ecosystem that supports innovation.

**5. Pilot Programs:** Launching pilot programs in sectors with high IP generation (such as tech, entertainment, and pharmaceuticals) can provide valuable insights and pave the way for broader implementation.

innovation financing. By embracing regulatory reforms, fostering the development of IP insurance products, and working closely with the startup ecosystem, insurers in Nigeria can unlock new growth pathways not only for their industry but for the broader economy.

## CONCLUSION

The insurance sector in Nigeria stands at the crossroads of tradition and innovation. While the foundation of the industry is built on traditional insurance plans that provide vital risk mitigation for individuals and businesses, there is a growing opportunity to revolutionize the role of insurance in supporting the startup ecosystem and



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## MEET THE AUTHORS



**MOSUN OKE**

PARTNER

[m.oke@topeadebayolp.com](mailto:m.oke@topeadebayolp.com)



**OLUCHI NWAIZIM**

SENIOR ASSOCIATE

Brought to you by TALP's Corporate and Commercial Department

*For further enquiries, log onto [www.topeadebayolp.com](http://www.topeadebayolp.com)*

Do you need to get in touch with us, to know more on how we can help you and your business?  
Kindly contact us by using any of the details provided below:

### **TOPE ADEBAYO LP**

25C Ladoke Akintola Street, G.R.A. Ikeja Lagos, Nigeria

p: +234 (1) 628 4627

e: [info@topeadebayolp.com](mailto:info@topeadebayolp.com)

w: [www.topeadebayolp.com](http://www.topeadebayolp.com)

