

Monetizing Your Intellectual Property: The Trend In Financing

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Do you want to generate additional working capital to grow your business? Do you have Intellectual Property (“IP”) to put on the table? If so, your IP can be monetized either by the now accepted method of securitization of IP assets or by a more recently developed method referred to as IP collateralization. IP collateralization may be right for your business. It is significantly less complex and less costly than securitization, which requires a substantial revenue stream derived from IP assets, rather than an IP asset portfolio. Collateralization will thus make growth capital available to more companies; and companies are beginning to capitalize on the previously unlocked potential that patents, trademarks, copyrights and other forms of IP deliver when and if growth capital is needed. Your company can too.

You probably have seen reports of the capital generated by the securitization of IP assets. Since the famous David Bowie IP backed bonds were issued, IP assets have been used to raise substantial capital. Examples of IP based securitization loans based on licensing revenues include a 1999 loan to Bill Blass in the amount of \$24 million, a 2001 loan to Gloria Vanderbilt of \$30 million; a loan of \$20 million to Candie’s in 2002, Guess’s acquisition of \$75 million in 2003 and, in the same year, a loan to Athlete’s Foot of \$33 million.

Securitization, however, is an option only if your company has a substantial stream of revenue attributable to IP, such as royalty revenue. In a securitization transaction, financing is generally accomplished by creating a special-purpose entity (“SPE” or “Issuer”) to issue securities (debt or equity certificates) based on certain receivables such as licence royalties or other cash flows from IP. The receivable is generally transferred to the Issuer, and the financing generated is paid after the offering from the Issuer to the “Originator,” the entity whose receivable was transferred to the Issuer. Security interests in the assets generally secure the commitment of the Originator to pay the debt. Bond or equity holders have recourse to seize the securitized assets in the event of a default.

Securitization may not be appropriate for your business. Risk evaluation in the context of securitized transactions involving receivables such as licence royalties or other cash flows from IP

is more difficult and uncharted than when assets consist of traditional real estate leases or supply contracts. Also, since securitization may involve the transfer of IP assets to an Issuer during the term of the loan, the type of IP that you have may mitigate against a securitized transaction. Ownership transfer—particularly for trademarks—may raise trademark specific legal issues. Securitization may not be practical for a number of other reasons, the ups and downs of Wall Street being just one of them.

A new means of raising capital is “collateralization” of IP assets—it also allows you to leverage the asset value in your patents, trademarks, copyrights, trade secrets and know-how. The monetization of IP assets by collateralization is a new financing approach. Collateralization allows relatively low cost access to capital without the complexity often inherent in securitization or other means of monetizing IP assets. Collateralized IP transactions are thus making financing more realistic for the average company.

What does collateralization of IP involve? It involves lenders, rather than investors. Traditionally, a lender will extend credit based on the tangible assets that your company owns—for example, your accounts receivables and inventory. In IP collateralization, an asset-based lender extends credit based on the IP assets themselves, in particular the disposal value of the IP that your company owns, as compared to the revenue stream of your IP, as is securitization. The IP is taken as collateral to minimize losses in the event of a borrower’s default. There is no transfer of IP assets to an Issuer; there is no issuance of securities.

Credit enhancement firms who specialize in IP transactions give “comfort” to traditional asset based lenders, who generally are still “uncomfortable” with IP as compared to traditional collateral. These lenders are reassured by the syndication of the risk with a credit enhancement firm. Credit enhancement firms essentially guarantee the repayment of the loan to the lender. Credit enhancement firms are more sophisticated in valuing the underlying IP than are traditional asset based lenders. Typically, a credit enhancement firm will conduct a valuation to provide a lender with an analysis of the collateral and with information about the rationale of a particular loan. Their involvement in a deal may even allow you to borrow from your preferred lender, who might have otherwise not issued financing based on collateralized IP.

Although an IP collateralized transaction will raise more capital than would a traditional asset based transaction (since you are adding your IP to the mix), you should know that credit enhancement firms tend to use conservative loan to value ratios for the IP. Also, they will require short transaction time frames to hedge their risk. IP values can be fleeting and if credit enhancement firms need to foreclose on the collateral in the event of default, both conservative loan to value ratios and selling the assets in the approximate “time frame” of the initial evaluation of the value of the assets ensure the firms that they will not sustain losses in the ordinary conduct of their business.

A recent example of a collateralized transaction involving IP assets is a loan made to BCBG Max Azria Group, a manufacturer and retailer of apparel, footwear and accessories, owned by Max Azria, its founder. There, \$12 million of the \$53 million dollar loan transaction was supported by a guarantee issued by a credit enhancement firm based on the collateralization of BCBG’s IP, including its current trademarks, in particular the trademarks BCBG, BCBG MAX AZRIA, BCBGIRLS, BCBG/ATTITUDE, TO THE MAX, HERVE LEGER and PARALLEL. BCBG Max Azria Group, a company wholly owned by one individual, elected collateralization instead of the more traditional ways of raising capital.

Irrespective of the financing vehicle that is right for your business, it’s time that you contact your IP lawyers and make sure that your IP is in order. You must begin to view your IP as a strategic resource and not as a cost center. While a credit enhancement firm can value your assets, nothing is more important than reviewing your IP assets with your IP lawyer. Your IP lawyer should be engaged to enforce or preserve your rights, take action to perfect your rights, and make sure that what you have will be properly reflected when the financial experts scrutinize the value of the assets in your portfolio. That’s where Gottlieb Rackman & Reisman comes in...

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