



Emerging Financing Strategy: Using IP Assets as Collateral

Legal Strategies for Borrowers and Lenders in Asset-Based Lending Transactions

A Live 90-Minute Teleconference/Webinar with Interactive Q&A

Today's panel features:

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The conference begins at:

1 pm Eastern

12 pm Central

11 am Mountain

10 am Pacific

The audio portion of this conference will be accessible by telephone only. Please refer to the dial in instructions emailed to registrants to access the audio portion of the conference.

EMERGING FINANCING STRATEGY: USING IP ASSETS AS COLLATERAL

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I. Introduction – Brief Overview of Major Forms of Intellectual Property – Scott J. Lebson

- A. Monopoly power on unique products and services;
- B. Source of funding to facilitate commercial transactions – M&A
 - 1. Patents.
 - 2. Trademarks.
 - 3. Copyrights.
 - 4. Other IP: Trade Secrets, Domain Names, etc.

II. Trends in IP Finance - Christopher G. Dorman

A. Economic evolution

1. shift in products/services (traditional assets (PP&E and Inventory)
2. change in structures (less warehousing/better shipping/overseas locals) jurisdictional factors - reliable legal system
 - i. United States/England
 - ii. Mexico
 - iii. China

II. Trends in IP Finance - Christopher G. Dorman (cont'd)

- B. Borrower's needs to Monetize
- C. IP has grown to be a major asset on the balance sheet of many businesses.
- D. Primary Credit Support
 1. Traditionally finance Real Estate, Equipment, Accounts, Inventory
 2. Boot Collateral to Primary Collateral
- E. Sophisticated Valuation Methods

II. Trends in IP Finance - Christopher G. Dorman (cont'd)

F. Improved Monitoring and Control of Collateral

1. Covenants

- i. cash flow (leverage ratio)
- ii. asset-based (verification of receivables)
- iii. confirm maintenance of TM

2. Collateral – validity/maintenance/verification

III. Issues to Consider Pre-Closing - Christopher G. Dorman

- A. Title Ownership.
- B. Assessing Value.
- C. Infringement.
- D. Validity.
- E. Loans/Encumbrances.
- F. Transferability.

IV. Security Interests In Or Relating To Intellectual Property Licenses – Ron Ben-Yehuda

A. Where the Debtor is the Licensee:

1. Bankruptcy or Nonperformance of Licensor – Section 365(n)
 - i. Applicability to International Rights Not Clear
 - ii. Section does not apply to trademark licenses – consider security interest in trademark or transfer of trademark to bankruptcy remote entity.

IV. Security Interests In Or Relating To Intellectual Property Licenses – Ron Ben-Yehuda (cont'd)

iii. Does not protect rights related to future updates, upgrades or services – consider:

- Security interest securing obligation to provide updates, upgrades or services
- Direct contractual relationship with key personnel

IV. Security Interests In Or Relating To Intellectual Property Licenses – Ron Ben-Yehuda (cont'd)

- Placing source code or other technical information in escrow – common missteps in escrowing include:
 - Ipso facto or inadequate release conditions
 - Inadequate license rights
 - Release delays

IV. Security Interests In Or Relating To Intellectual Property Licenses – Ron Ben-Yehuda (cont'd)

- iv. Licensee must pay royalties without offset – consider separately designating payments allocated to services, upgrades, etc.
- 2. Bankruptcy or Nonperformance of Licensee:
 - i. Non-assumability and Non-assignability of Nonexclusive Licenses in Bankruptcy

IV. Security Interests In Or Relating To Intellectual Property Licenses – Ron Ben-Yehuda (cont'd)

- ii. Termination of License for Nonperformance or Other Conditions
- iii. Additional Concerns re Assignments of Trademark Licenses

- B. Where the Debtor is the Licensor:
 - 1. Debtor's Capacity to Perform

IV. Security Interests In Or Relating To Intellectual Property Licenses – Ron Ben-Yehuda (cont'd)

2. Additional Concerns Re Exclusive Licenses
 - i. Viability and Creditworthiness of Licensee
 - ii. Remedies For Lower than Expected Royalties or Efforts
 - iii. Licensee's Bankruptcy – Loss of Control and Stagnation of IP
3. Impediments to Enforceability of License – Patent or Copyright

V. The Uniform Commercial Code (UCC) – Article 9 – Scott J. Lebson

- A. Application of Article 9
 - 1. Security Interests Governed by State Law despite “Federal” nature of IP Rights;
- B. Components of a Security Interest
 - 1. creation;
 - 2. perfection; and
 - 3. enforcement/release.
- C. Security Agreement
 - 1. Requirement for written Agreement
- D. Attachment

VI. The Problem of Preemption – Scott J. Lebson

- A. Federal v. State Law
 - 1. Section 9-109(c)(1)
- B. Where to Perfect
 - 1. General Rule - Section 9-301
- C. How to Perfect
 - 1. Financing Statements
 - 2. Sufficiency of Description

VII. Perfection of Security Interests in Trademarks – Scott J. Lebson

- A. Limitations upon Assignment and Relevance to Perfection
 1. Goodwill –
 2. Assignment in Gross Rule – Could Jeopardize Foreclosure
- B. U.C.C. Filing Required
- C. Dual Filings Recommended
 1. Common misconception
 2. Effect of Federal Level Recordal – 3rd party notice

VII. Perfection of Security Interests in Trademarks – Scott J. Lebson (cont'd)

A. Intent-to-Use Applications

1. Clorox Case

VIII. Perfection of Security Interests in Patents – Scott J. Lebson

- A. Patent Act Section 261
 - 1. Security interests not addressed
- B. *Waterman v. McKenzie* - Case from 1890's that stated recordal at USPTO was sufficient. Of course, this was prior to advent of UCC.
- C. Post-*Waterman* Progeny
 - 1. *In re Transportation Design* - UCC filing sufficient
 - 2. *In re Cybernetics, Inc.* - No preemption
- D. How to Proceed
 - 1. Dual Filings

IX. Perfection of Security Interests in Copyrights – Scott J. Lebson

A. Federally Registered Copyrights

1. Section 205
2. Section 101
3. Federal Level Filings;

B. Unregistered Copyrights.

1. Local Filings
2. Negotiate obligation to Perfect – After Acquired Property

X. Perfection of Security Interests in Trade Secrets, Domain Names, other IP – Scott J. Lebson

- A. Are Domain Names a form of “property”
 1. Telephone analysis
 2. ACPA - treated as property
 3. Filings under UCC the common practice

- B. Trade Secrets: do not violate fundamental rule of trade secrets (i.e., reasonable efforts to protect confidentiality) during perfection stage

XI. International Creation and Perfection of Security Interests – Scott J. Lebson

- A. Major Markets
 1. North America
 2. Europe
 3. South America
- B. Local Requirements
- C. Local Counsel.

XII. Monitoring – Christopher G. Dorman

A. Patents

1. Require Borrower to maintain patents, obtain patents on new inventions and prosecute applications.
2. Give Lender the right to do the foregoing and to sue for infringement.
 - i. Require Borrower to have agreements with employees, consultants, agents to establish the ownership of patentable inventions. Otherwise, inventions may be deemed “shop rights”, which is a royalty-free, nonexclusive, be non-transferable license to use the invention. This may make it impossible to gain a security interest.

XII. Monitoring – Christopher G. Dorman (cont'd)

B. Trade Secrets

1. Must be secret. Therefore, review of Borrower's systems to protect the secret may be necessary with monitoring technique. Employee confidentiality agreements. (Consider the un-patented medical device). The Economic Espionage Act of 1996 establishes criminal (not civil) penalties on theft of trade secrets.

XII. Monitoring – Christopher G. Dorman (cont'd)

C. Trademarks

1. Require Borrower to protect the trademark.
2. Security grant should include the goodwill of the business since TM is not independent. Note that goodwill is a general intangible.
3. Quality Control Standards
4. Customer lists

D. Copyrights

1. Require Federal Registration

XII. Monitoring – Christopher G. Dorman (cont'd)

- E. Improved Awareness of bundle of sticks and legal regimes
- F. Improving due diligence
 1. representations and warranties
 2. covenants and reporting requirements
 3. opinion letter
- G. Mitigating risks
 1. Licensor granting Lender right to use Trademark/Patent
 2. Software Escrow

XII. Monitoring – Christopher G. Dorman (cont'd)

3. Structure

- i. consider SPV
- ii. documentation (see 1-4 above and 8 below)
- iii. power of attorney
- iv. where to file

H. Monitoring

1. Covenants
2. (b) maintenance payment for Utility Patent (3.5, 7.5 and 11.5 years)
3. reporting requirements

XIII. Enforcement Rights of Creditors – Christopher G. Dorman

- A. Primarily Article 9
 - 1. rights to use or sell
 - 2. defaults
 - 3. remedies
 - 4. foreclosure

XIII. Enforcement Rights of Creditors – Christopher G. Dorman (cont'd)

- A. Consider necessity of gaining control or security interest in materials to facilitate transfer (e.g., in case of patents, equipment used in producing the patentable product)
- B. Software - Packaged software held by retailers is not inventory under Article 9 U.C.C. 9-102(a)(48). File on goods, although goods does not include a computer program embedded in goods that consists solely of medium in which program is embedded