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Finance and IP

Our recent **guide**, published in conjunction with the British Private Equity and Venture Capital Association (BVCA), notes that conducting intellectual property (IP) due diligence is essential when assessing whether and how to invest in a business.

A knowledgeable investor will understand the value of IP within a business and that IP, as a proprietary right, can be a valuable security against an investment. However, the true value of the portfolio, or lack of it can be difficult to ascertain, and first impressions are often deceptive unless a closer look is taken at the individual rights. The investor's interest in IP does not stop once the investment has been made, as evolving and growing a business's IP portfolio can lead to an increase in value of the business and ensuring that the IP is protected and used correctly can be vital for maintaining its value.

This is also true from the bank's lending perspective, as confirmed in a report published this month by the UK Intellectual Property Office (UKIPO) entitled: "Banking on IP? The role of intellectual property and intangible assets in facilitating business finance". The overriding message of the report is that SMEs, lenders and other financiers must raise their awareness and appreciation of IP (not just patents, but also trademarks, copyright and other intangibles such as trade secrets), and put it to practical use for business innovation and growth. The report makes a number of recommendations to help achieve this:

"1. **IP and intangibles must be identified during the financing process.** For IP and intangibles to be given any consideration within credit decision-making, tools to identify and describe the actual assets (not merely evidence of expenditure) need to be embedded within the lending process. Businesses must use them, and lenders must understand and take note of them. This step will have the wider benefit of boosting IP awareness amongst the business community as a whole.

2. **The value of IP needs to be taken into account.** The most important step in harnessing IP value is to realise that this value is not nil, and therefore requires active consideration. Robust approaches to determine the value of intangibles exist in the same way as for tangible property and are now included alongside them within the Royal Institute of Chartered Surveyors' Red Book, regarded as a banking industry reference point.

3. **Due diligence guidelines can help to control costs.** Checks will be needed in order to create confidence that the ownership and quality of the IP and intangibles are understood, that they contribute to serviceability and cash flow (particularly in the case of debt finance), and that their maturity is in line with what it would be reasonable to expect, given the development stage of the business. This will require templates, training and/or access to professional advice, at a cost that lending margins can support, within a turnaround time that meets business requirements.

4. **More effective charges should be part of the lending package.** Once knowledge assets are captured and verified, it becomes possible to create a proper interest over them. Legal templates and the resource toolkit will help lenders to achieve this at modest cost, firstly by providing appropriate wording for the instruments, and secondly by providing guidance on the procedures which must be followed when recording them.

5. **IP markets and IP financing could be facilitated through infrastructure improvements.** The development most likely to transform IP and intangibles as an asset class is the emergence of more transparent and accessible marketplaces where they can be traded. This is a domain where services must stand or fall on

their commercial merits; however, the available infrastructure needs to support rather than impede their establishment. In particular, as IP and intangibles become clearly identified and are more freely licensed, bought and sold (together with or separate to the business), the systems available to register and track financial interests will need to be improved. This will require the co-operation of official registries and the establishment of administrative protocols.

6. **On-going management of IP and intangibles should also be supported.** IP does not stop being important once credit is granted. The asset class is unfamiliar, and lenders will need assistance in understanding it, monitoring it and encouraging businesses to use and protect it so that risk is reduced. There could be a role for the introduction of 'milestones' (as used in equity and venture debt) and impairment tests to ensure that businesses are well informed and motivated to adopt appropriate IP management practices.

7. **Affordable risk mitigation strategies are to be encouraged.** Alongside certain guarantees, access to appropriate insurance policies to guard against unforeseen events could greatly increase banking confidence in adding further weight to IP and intangibles within the lending decision. There is private sector appetite to provide these if lenders are willing to create the demand; more detailed dialogue on the requirements of both parties is urgently required.

8. **Asset-based financing techniques should be adapted for IP and intangibles.** Recent financial upheavals have triggered something of a return to first principles in lending and a greater emphasis on assets for business finance (reflected, for example, in 'challenger' bank activity). This greater emphasis on assets needs to be extended to include IP. Alongside mainstream lending, where the Enterprise Finance Guarantee (EFG) is an obvious area of focus, asset-based finance and alternative financing methods should therefore be targeted for IP-backed finance interventions; these are the parts of the finance industry most accustomed to understanding and assessing individual assets and their value.

9. **Steps to stimulate private investment need closer study.** IP rights can be well suited to securitisation (patents, trade marks, registered designs and copyright portfolios). Given the successful track record of venture debt, more work is needed to understand onshore and offshore fund appetite to support investment in IP-rich companies, working with fund managers that have the necessary expertise.

10. **IP demands joined-up thinking.** The Intellectual Property Office (IPO) exists "to promote innovation by providing a clear, accessible and widely understood IP system, which enables the economy and society to benefit from knowledge and ideas". It therefore has a role to play in scrutinising Government and finance industry initiatives to boost lending, to ensure that the assets produced by knowledge receive consideration. But the IPO is not the only player, and only when all involved appreciate that these assets matter will their true potential be unlocked."

Carpmaels & Ransford LLP is ideally placed to help potential financiers assess risk by carrying out IP audits, performing IP due diligence and providing IP advice. Once finance has been provided, we continue to work with businesses to unlock their IP potential by identifying, protecting and defending their IP, with a view to increasing the value of the IP asset and, for investors, increasing the opportunities for a profitable exit.

Author: Sarah Kent

Need advice?

For more information, please contact email@carpmaels.com.

Carpmaels & Ransford LLP is a leading European intellectual property firm based in London. For more information about our firm and our practice, please visit our website at www.carpmaels.com.

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