Feature
By **Stefan Rüssli** and
Oliver Scherenberg

Trademark Toolkit: An innovative approach to financing

A number of crucial decisions must be made when considering whether to use your brand as collateral against corporate financing

There is general consensus that brands are among a company's most valuable assets. They can also be shown to be independent assets. It is therefore only logical to think about offering them as collateral against corporate financing. On a technical level, besides pledging the brand as collateral, the sale and leaseback concept is also worth considering. The requisite credit is covered by the company selling its brand (thereby generating liquidity) and leasing it back at the same time, so that it can continue its business operations.

The brand is usually transferred to a property company owned by a leasing company which is capitalised by the lending bank. The lease instalments are assigned to the bank. After a typical term of five to seven years, the lease amount is paid back and the brand is returned to the company. Due to this elaborate structure, and the costly brand evaluation exercises and legal and tax consultancy services involved, such transactions are typically worthwhile only if they exceed $3 million.

At the start of the new millennium, it seemed as though this innovative approach to financing would take off. In Western Europe in particular, banking institutions financed many deals, mainly in the consumer goods industry. But when the financial crisis hit in 2007, these financing concepts ground to a near standstill. Banks suddenly considered brand financing to be too risky. They believed that they would not generally be capable of evaluating the relative strength (or risk) of brands, and further that valuation would be difficult in the event of insolvency. But although these arguments are not unfounded, they can certainly be overcome. These days, there are several recognised ISO-certified brand valuation methods that clearly explain the value to be assigned to a brand. There is also a global market for brands, which ensures that brand value can be extracted in the worst-case scenario of insolvency – especially in the area of consumer goods.

Is sale and leaseback the right option?

From the brand owner's point of view, brand financing in the form of a sale and leaseback is a sensible financing option. This is especially true if free cash flow is positive, but debt is high. As the transaction takes place off-balance sheet, this concept can even assist in balance-sheet restructuring. But the risks should not be forgotten. If the lease instalments cannot be paid, the financier takes ownership of the brand and the company's entire operations are jeopardised. In our opinion, companies with larger brand portfolios are particularly well suited to sale and leaseback brand financing, as their risk is limited if the commitments cannot be honoured and the brand is subsequently lost.

Sourcing potential financial partners

So how do you find the right financing partners for such agreements? In our experience, banks are no longer the right fit, for the reasons outlined above. Instead, we have been partnering with private investors such as family offices that manage the wealth of brand-aware clans (eg, former owners or senior management of fast-moving consumer goods companies). These people understand the functions of a brand and can assess a brand's risk from experience. But we also make deals with other institutional investors looking for a steady annual income stream which can be realised through such concepts.

Contractual must-haves

Several legal issues on each side of the transaction must be considered in brand sale and leaseback scenarios. Most importantly, the financer will want to see proof of full and unlimited ownership of the brand. Since trademarks are often held by separate IP holding companies, the brand owner and the lending entity may not be the same – so either some transfers or at least some serious guarantees will be necessary. Further, the financing (and back-licensing) entity may want to establish the property company in a tax-friendly environment where licensing income is subject to reduced taxation (eg, Luxembourg or Switzerland). Benefits generated in this regard may make the overall deal more attractive for both sides, since they will have an impact on the overall economic terms. Brand owners, on the other hand, must ensure that the transaction will not limit exploitation of the brand, and at the same time leave enough room to be able to react to market changes, expand into new markets, refine and redesign the brand and explore further trademark applications. These aspects are also critical for the financing entity, since it relies on the collateralised brand staying in the market; its value would collapse if the lending party could simply replace it. Well-balanced contractual drafting is needed to deal with all of these and other important aspects. WTR

Stefan Rüssli is managing director of Assessa Brand Licenses and **Oliver Scherenberg** a partner at Preu Bohlig & Partner
stefan.ruessli@assessa.ch
ols@preubohlig.de