

Securitization of Intellectual Property

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What Is Structured Finance?

- Securities backed by financial assets and credit support from a third party
- Aliases
 - Securitization
 - Asset-backed securities
 - Mortgage-backed securities



Characteristics of Structured Finance

- Loans are segregated from originator/servicer
 - Legally insulated from bankruptcy of originator/servicer
 - Insulated from ongoing management influence
- Predictable cashflows
 - Large number of loans
 - Historical experience
- Cashflows supplemented with credit enhancement
 - Letter of credit, surety bond, corporate guarantee, reserve fund, subordinated interest of other investors



Three Types Of Analyses

- **Asset credit quality analysis**
 - To what extent will assets pay as promised?
- **Structured cash flow analysis**
 - Who gets that cashflow?
- **Legal analysis**
 - Can other investors make a claim on that cashflow?



Intellectual Property

What has been securitized to date?

- Music Royalties
- Film Receivables
- Trademark Licensing Royalties
- Drug Patent Licensing Royalties
- Franchise Fees
- TV Syndication Rights





Music Royalties



The Beginning : Music Royalties

- Several music royalty transactions rated 1997-2001
- No activity recently in the area
- Two major revenue streams:
 - record master rights
 - music publishing
- Potential for one transaction to be completed in 2007, likely publishing royalties





Film Receivables



The Assets Include the Following:

- The entire output of a studio
- The tangible film materials as well as rights to:
 - release, distribute and exhibit
 - receive gross receipts from agreements the studio already has with distributors
 - enter into new agreements for distribution of the films



Different Distribution Windows...

...provide for different streams of cashflows

Applicable for domestic and international

- Theatricals
- Home Video
- Pay TV
- Free TV



Types of Transactions

- **Future Film Portfolio (aka “Slate Financing”)**
 - Portfolio of not yet released films of a studio
 - Film’s production costs and a portion of studio overhead are financed
 - Distribution expenses funded by the studio and reimbursed from the deal’s waterfall
 - Exposure to film performance risk

- **Film Revenue Advance**
 - Advancing against film’s projected future revenues
 - Films funded 4-8 weeks after domestic theatrical release
 - Reduced exposure to the film performance risk



Transactions Rated in 2005-2006

- Kingdom Films, rated Baa2 in 2005
- MVL Film Finance, rated Aaa in 2005
- The Weinstein Portfolio Funding Company, rated Aaa in 2005
- Gun Hill Road, rated Baa2 in 2006



Outlook for Film Receivables

- Three-four transactions in 2007
- Future transactions
 - Slate financing with distribution costs on the top of the waterfall
 - Include films from multiple studios in one deal





Trademark Licensing



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Assets include....

- The trademark
- Royalties generated from the sale of licensed branded products
- Could include sales through:
 - Wholesale
 - Retail
 - 3rd Party License



Moody's Approach

General Considerations

- Strength of the trademark
 - History and longevity
 - Competition and positioning
- Manager and servicer
 - Need for a back-up manager
- Potential market for the trademark in distressed situations



Moody's Approach

Cash Flow Analysis

- Revenues from wholesale and retail sales
 - Historical experience and future growth trends
 - Default of the master licensee

- Cash flows from 3rd party licensees
 - The current licenses in place
 - Credit quality of the 3rd party licensees
 - Potential renewals



Transactions Rated

- \$1.8B KCD LLC, rated Baa2 in 2006
- \$53M BCBG Max Azria, rated Aaa/Baa3 in 2004
- \$75M Guess?, rated Baa2 in 2003
- \$20M Candies, rated Baa3 in 2002
- \$20M Bill Blass, rated Baa3 in 1999





Patent Licensing Royalties



Moody's Rated First Patent Transaction in 2003

- **Drug Patent: Royalty Pharma**
 - Trust owns patent rights and rights to receive royalties for a pool of pharmaceutical drugs
- **Moody's has historically looked at other technology patents**



Risks Considered in Patent Royalty Transactions

- Technology marketing and acceptance
- Technological obsolescence
- Licensee payment risk
- Servicing risk
- Legal risks



Outlook : Patent Licensing Royalties

- A lot of interest and inquiries regarding securitization of patent royalty rights
- Possibility of two to three transactions to be completed in 2007





Franchise Fees



What are the Assets?

- Intellectual property of the concept
- Franchise fees paid by franchisee for the right to use name and concept
- Additional revenues might include upfront amounts paid when new stores are opened
- If franchisor provides certain specific materials to franchisees, then the profits on these materials might also be included



Key Points to Consider in Analysis Include:

- Historical data on the performance
- Competition for similar concept
- Industry overview
- Role and strength of franchisor/servicer,
- Need for back-up servicer?
- Reason for securitization
- Legal concerns (core assets, true sale, non-consolidation, fraudulent conveyance)



Rated Securitizations Backed by Franchise Fees

- **Arby's (2000)**
 - \$290 Million/Aaa (Ambac Wrap)
- **Athlete's Foot (2003)**
 - \$33 Million/Ba2
- **Quiznos (2004)**
 - \$250 Million/Baa2
- **Dunkin' (2006)**
 - \$1.7 Billion/Aaa (Ambac Wrap)





**DB Master Finance, LLC
Series 2006-1**



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DB Master Finance, LLC Series 2006-1

| Class | Amount (MM) | Coupon | Frequency | Expected Final | Legal Final | Rating |
|--------------|----------------|----------|-----------|----------------|-------------|--------|
| Class A-1 | 100 | Variable | Monthly | 6/20/2011 | 6/20/2031 | Aaa |
| Class A-2 | 1,500 | Fixed | Monthly | 6/20/2011 | 6/20/2031 | Aaa |
| Class M-1 | 100 | Fixed | Monthly | 6/20/2011 | 6/20/2031 | Ba3 |
| Total | \$1,700 | | | | | |

- Master Trust Structure
- Collateral
 - IP (Trademarks, Patents, Recipes, Etc.)
 - Franchise Agreements (Royalty Payments)
 - License Agreement
 - Real Estate/Leases
 - Equity in International JV Subs



Key Risks

- Loss of Brand Popularity ('Brand Viability')
 - Consumer Preferences
 - Competitive Environment
 - Event Risk
- Linkage to Seller
 - Corporate Risk (B3 Senior Unsecured)
 - Business Risk (Sales, Brand, Franchise Base)
- Legal Risk
 - Separation of Assets from Seller



Modeling Approach

- Monte Carlo Simulation
- Multi Scenario Approach
 - Test Key Inputs (AUV/PODs)
 - Built-In Default Events (tied to Corporate Rating)
 - Default and Event Risk Haircuts
 - Brand Viability – Cash Flow Impact
 - Gradual/Rapid Deterioration
 - Random Walk (Deterioration/Plateau/Improvement)
 - Brand Viability Sensitivity Analysis (Chapter 7)
 - Residual Value Analysis





TV Syndication Rights



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TV Syndication Rights

- First securitization rated in 2005
 - \$301m Prime Time Trust, rated Aaa (Ambac wrapped)
- Debt repayment from the sale of the right to broadcast programs to broadcast or cable stations
- Programming can be sold via
 - Cash
 - Barter
 - Distributor of the show retains some commercial time that can be sold to advertisers



Points to Consider

- **General Considerations**
 - Genre of the show and number of episodes
 - Competition and sustainability of future demand
 - Portfolio of shows

- **Cash Flow Analysis**
 - Contracted cash agreements
 - Creditworthiness of broadcast stations
 - Barter
 - Show ratings, time slots, audience
 - Non-contracted future cash flows
 - History of contracts renewal and price
 - Experience of the manager





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