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Another significant Fortress deal suggests that patent-backed finance is coming to the fore - UPDATE

Continuing to build its reputation as a leading provider of IP-backed funding, **Fortress Investment Group** (FIG) has **agreed to loan Andrea Electronics $4 million** secured against the company's patent portfolio, in addition to paying the company $3 million for a share of its IP monetisation revenues.

Andrea Electronics – which sells microphone, headset and teleconferencing products – says in its **most recent 8K filing** with the US Securities and Exchange Commission (SEC) that it has "issued $200,000 of notes to the note purchasers [a FIG vehicle named AND34 Funding LLC] and has agreed to issue and sell to the note purchasers an additional $4,000,000 during the four years after the closing date". The 8K goes on to state that the "proceeds of the notes will be used to pay preclose expenses of the company and… note purchasers and the company's future patent monetisation expenses… The notes are also secured by the patents".

In addition, for a further $3 million FIG has obtained a stake in any returns that Andrea generates from monetising the patents it currently owns. According to the 8K form, these returns include – but are not limited to –new licence fees, settlement payments and judgment amounts. The SEC filing also reveals some interesting details of what proportion of Andrea's total monetisation proceeds FIG will receive:

Any Monetization Revenues (as defined in the Agreement) received from the Patents will first be applied 100% to the payment of accrued and unpaid interest on, and then to repay outstanding principal of, the Notes. After the Notes are paid off in full, the Monetization Revenues received from the Patents will be allocated amongst the Revenue Participants [AND34 Funding LLC] *and the Company in accordance with certain predetermined percentages (based on aggregate amounts received by the Revenue Participants) ranging from 100% to the Revenue Participants (such percentage to be allocated to the Revenue Participants until they have received $3,000,000) to ultimately 20% to the Revenue Participants.*

Furthermore, the agreement between FIG and Andrea requires the latter to "use its best efforts to diligently pursue the monetisation of the patents pursuant to a business plan agreed to by the company" and its lender. Failure to comply with this business plan could result in a default – meaning that FIG would be able to "either exercise the patent licence granted to the collateral agent, direct the company to assign the patents to a special purpose entity controlled by the note purchasers and revenue participants or perfect the security interest in the patents, provided that in the case of any assignment of the patents, the company will have a non-revocable, perpetual sub-licensable right and license back to use the patents for the sale of proprietary products and other licences consistent with the agreement".

The terms of this deal appear to be very similar to those offered by FIG when it agreed to **loan cloud computing company Netlist up to $15 million** against its patent assets in July last year. The arrangement with Netlist also went beyond a straight-up loan using patents as collateral; it likewise entitled the lender to a cut of any monetisation proceeds and required the patent owner to be proactive in seeking additional revenue from its assets. The Andrea deal may even go a step further in that it explicitly grants FIG an active role in designing, implementing and directing the patent owner's monetisation strategy.

This agreement with Andrea is the latest sign of FIG's intentions in the burgeoning IP collateralisation marketplace, following the deal with Netlist and the **hiring of RPX co-founder Eran Zur** to head up the investment management firm's IP Finance Group in March last year. FIG's co-ownership of German NPE IPCom has begun to reap some **significant returns of late** and shows that its IP monetisation interests are not limited to patent-backed financing.

It is probably safe to assume that we will see more and more innovative, IP-based financing arrangements like this in the future. They can make a lot of sense for both the lender and the patent owner. The lender gets a cut of any royalties and settlement payments that are secured through licensing the patents, and has the guarantee that it will be able to monetise the collateralised IP rights itself should the loanee default. The patent owner, for its part, gets the capital it requires to expand its business and finance a monetisation campaign, while retaining ownership of its patents. For many businesses, that is likely to be a far more attractive proposition than selling their rights to an NPE.

UPDATE - FIG also agreed a patent-based loan deal with Document Security Systems (DSS) earlier this month, according to a recent 8K filing from the latter company. The arrangement with DSS - which sells security technology products and services alongside its patent licensing business - suggests that IP monetisation-focused entities, as well as operating companies, are exploring the potential benefits of collateralising their patents and royalty streams.

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Licensing, **Patents**, **IP business**, **IP finance**
