

# The Use of IP Assets to Access Funding for SMEs









The realisation of a guide about the use of Intellectual Property Assets by the SMEs to get access to funding, special scope statement  
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# Glossary<sup>1</sup>

<b>Business angels</b> - High-net-worth investors who invest in and support high-risk start-ups at a very early stage, in exchange for participation in the future profit of the enterprise. Besides money, they can invest time, experience and knowledge, and provide connections to their large networks in order to guide the enterprise in its new business.
<b>Class</b> - The category to which the goods and services listed in the trademark application are allocated. Goods and services are classified according to the international Nice Classification.
<b>Collateralization of IP</b> - In the Belgian law system, IP assets are classified as movable and intangible assets and, as such, they can be used as collateral. In other words, a lender can accept IP assets as security for a loan and, if the borrower fails to pay the loan back, the lender can seize the collateral and sell it to recoup some or all its losses.
<b>Copyright</b> - Intellectual property right given to creators of literary or artistic works.
<b>Copyright fiscal deduction</b> - A regime that allows creators of an artistic or literary work, who assign their copyright and neighboring rights to a third party, to benefit from a separate tax rate of 15% on the income obtained in return.
<b>Design</b> - The appearance of the whole or a part of the product, resulting from the features of the lines, contours, colors, shape, texture and/or materials of the product.
<b>Equity financing</b> - The process of raising capital of the company through the sale of shares.
<b>Financial statements</b> - Reports illustrating the financial position of the entity for a specified period. They usually comprise of the balance sheet, an income statement (or profit and loss statement), a cash flow statement, and a statement on the changes in equity.
<b>Infringement</b> - Violation of an exclusive intellectual property right.
<b>Innovation Box</b> - Also called “deduction for innovation income” (IID) allows companies to exempt 85% of their qualifying net income (license fees, etc.) from eligible intellectual property rights (patents, for instance) from tax in the form of a tax deduction or to exempt it, provided that certain conditions are met.
<b>Intellectual property (IP)</b> - Creations of the mind or intellect. Intellectual property is divided into two categories: industrial property, which includes patents, trademarks, industrial designs, and copyright, which includes literary and artistic works such as novels, poems and plays, films, musical works, artistic works such as drawings, paintings, photographs and sculptures, and architectural designs.
<b>IP securitization</b> - Financial model wherein future cash flow from IP assets is used as a guarantee for repayment of debt.
<b>IP valuation</b> - The process of determining the value of IP assets.
<b>Joint venture</b> - The business relationship between two or more enterprises pooling their resources to realize a common business goal, whereas one party usually provides technology or know-how, and the other party contributes financially.
<b>License</b> - Contractual agreement that gives written permission to another party to use an intellectual property right belonging to another person or company and defines the terms of use.

<sup>1</sup> This glossary lists a number of terms that we use frequently in this study. Please note that these are not legal definitions but rather short and practical explanations, provided with the aim of making your reading and understanding of the study easier.

**Non-Fungible Tokens (NFTs)** - Digital assets (images, songs, videos, etc.) that are verified through blockchain technology. In other words, NFTs create a blockchain-based digital certificate, which testifies that the asset at issue is owned by a specific person.

**Patent** - Legal title that gives inventors the right, for a limited period, to prevent others from making, using or selling their invention without their permission in the countries for which the patent has been granted.

**Pledge** - Collateral security with which movable property can be encumbered. It is possible to establish a pledge on IP assets (for instance, on trademark).

**Research and Developments (R&D)** - Activities that companies undertake to innovate and introduce new products and services.

**SMEs** - Small and medium-sized enterprises.

**Strategic alliance** - A form of a cooperative strategy whereby firms combine resources and capabilities to achieve mutual goals

**ToolBox** - A go-to, easy-to-handle summary of the different aspects of the study, that comprehends advice and strategies, schematics and key facts that may prove useful for SMEs trying to obtain funding through their IP.

**Trademark** - A sign that entrepreneurs use to differentiate their goods and services from those of their competitors.

**Venture capital investors (venture capitalists, VC)** - Private equity investors that provide capital to young enterprises with high growth potential in exchange for an equity stake.

# 1. Introduction

Over the last decade, the growing contribution of intellectual property assets to the market value of companies, especially for Small and Medium Enterprises (hereinafter “SMEs”)<sup>2</sup>, has primarily been driven by the emergence of a new economy, known as a *knowledge economy*, in which core capital takes the form of technologies such as patents, processes, know-how, customer reach or again workforce talent<sup>3</sup> rather than being based on the classical model of *bricks and mortars*.

Today, the use of the intellectual property as collateral should therefore be routine exercises in corporate finance, but is still beset with structural uncertainty<sup>4</sup>. Moreover, there is still substantial underinvestment in innovation and R&D due to the un-appropriable nature of knowledge as an intangible product. Theoretically, it seems that this phenomenon could be counterbalanced with a proper valuation of Intellectual Property Rights (hereinafter “IPRs”), and a more robust and comprehensive approach to the fair valuation of intangible assets.

With companies’ growing IP portfolio, obtaining IP backed securitization and using IP assets as collateral could prove to be an important means of financing for innovative firms, and one may ask whether it may be considered as an alternative to traditional financing<sup>5</sup>.

In Belgium, SMEs must play at the different regulatory levels, and at the interplay of different sets of rules, divided between the specific regime applying to IPRs and the ones regulating the larger question of securitization, funding and valuation of company assets. The latter often divides itself between different tools and different approaches, which are often overlooked by Belgian SMEs.

This report will therefore present an overview of the question at hand, and shall provide a series of recommendations on ways to use IP in order to access proper funding. We shall discuss the different approaches which exist to use IP as access to funding (part 2), by going over the role and importance of IP securitization as well as presenting different mechanisms currently existing in the Belgian landscape and going from IP as collateral for debt-financing to IP as an insurance policy. Furthermore, we will develop the current Regulatory framework (Part 3) and noteworthy policies applicable to SMEs and inform them on different legal and fiscal tools that are available. Lastly, we shall conclude on the different challenges that still represent an obstacle to proper funding through intangible assets (Part 4) and most importantly, we will provide a Toolbox, composed of practical and easy-to-use information to the attention of SMEs owners to improve the management of their IP strategy in Belgium.

## 2. IP as Access to Funding

### 2.1. Role and Types of IP Securitization Approaches

Small and medium-sized enterprises (hereinafter “SMEs”), are often described as the backbone of the economy: essential for ensuring job creation, innovation and economic growth<sup>6</sup>. In recent

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<sup>2</sup> KPMG Spain, „2019 Intellectual Property SME Scoreboard“, *Commissioned by the European Union Intellectual Property Office*, 2019, p. 5.

<sup>3</sup> V. SHARMA, R. ROHIT, „How to get the most out of IP Financing“, *Iam-media*, available at: [How to get the most out of IP financing | IAM \(iam-media.com\)](https://www.iam-media.com/en/how-to-get-the-most-out-of-ip-financing)

<sup>4</sup> E.-M. KIENINGER, „Security Rights in Intellectual Property: General Report“, E.-M. KIENINGER (ed.), *Security Rights in Intellectual Property, Ius Comparatum – Global Studies in Comparative Law* 45, Springer Nature Switzerland 2020, p. 3.

<sup>5</sup> Dr. C. DONEGAN, “It is a great time to be involved in IP finance”, *Iam-media*, available at: [It's a great time to be involved in IP finance | IAM \(iam-media.com\)](https://www.iam-media.com/en/its-a-great-time-to-be-involved-in-ip-finance)

<sup>6</sup> KPMG Spain, “2019 Intellectual Property SME Scoreboard”, *Commissioned by the European Union Intellectual Property Office*, 2019, p. 6.

years, another trend shows that businesses of all sizes have been investing more in intangible assets, in particular Intellectual Property (hereinafter collectively described as “IP”), than in fixed or physical assets<sup>7</sup>.

Yet, SMEs do struggle to use their IP assets as a way to grow: their balance sheets often do not represent their IP value, and the current European and Benelux regulatory framework is still divided and sometimes actively works against the consideration of IP as an asset class<sup>8</sup>. This results in an important disconnect between banking regulations and practices and the Belgian SMEs’ willingness to access funding to grow.

The problem of making knowledge assets – i.e. intangibles – bankable has already been partially addressed at the international level<sup>9</sup>.

In Belgium, as in many jurisdictions, the situation is promising but remains complex due to different factors. Firstly, IP is a federal matter in Belgium, which is regulated differently depending on the type of IP right at hand<sup>10</sup>. Secondly, IP rights stem from statutory, IP specific, provisions<sup>11</sup>; these sets of rules constitute the first step towards the creation of securities: the IP-specific regulations need to provide for such possibilities. More importantly, the possibility to use IP as security implies that common property law allows for such usage<sup>12</sup>. IP fundamentally needs to be useable as collateral, as this is the crucial step towards its valuation and its use as access to funding.

### 2.1.1. Economic Importance and Economic Challenges

The use of IP as collateral for securitization seems to be set with structural uncertainty, as it seems that globally, there are only a few states where such practice is facilitated and/or efficient<sup>13</sup>, especially for SMEs<sup>14</sup>. It stems from the latest reports at the European level that IPRs are often misunderstood by SMEs and are often seen as a cost rather than as an investment<sup>15</sup>. In 2019, only 25% of medium-sized IPR owners had professionally valued their intangible assets, and this drops to 20% for both small and micro-sized IPR owners<sup>16</sup>. In most cases, IP is still used as an all-asset security right, where it is only a part of a group of company charges being secured. And yet, we may underline an international consensus that “IP right could be economically valuable, if not crucial, for SMEs”<sup>17</sup>.

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<sup>7</sup>M. BRASSEL, K. KING, “Banking on IP ? The role of intellectual property and intangible assets in facilitating business finance – final report”, UK Intellectual Property Office, *Crown Copyright*, 2013, p.3.

<sup>8</sup> Ibid.

<sup>9</sup> According to BRASSEL and KING, op.cit., : “Malaysia and Singapore implemented guarantees to facilitate IP-backed lending; Denmark and India are supporting the development of IP marketplaces; Germany has sought to articulate the ‘Wissensbilanz’ to assist financial analysis of individual firms; Brazilian banks are experimenting with IP audits prior to lending”.

<sup>10</sup> M.E. STORME, J. MALEKZADEM, „Security Rights in Intellectual Property in Belgium“, E.-M. KIENINGER (ed.), *Security Rights in Intellectual Property*, *Ius Comparatum – Global Studies in Comparative Law* 45, Springer Nature Switzerland 2020, p. 120.

<sup>11</sup> Those of which are mostly provided in the Belgian Code of Economic Law.

<sup>12</sup> E.-M. KIENINGER, „Security Rights in Intellectual Property: General Report“, op. cit., p. 3.

<sup>13</sup> Ibid.

<sup>14</sup> KPMG Spain, „2019 Intellectual Property SME Scoreboard“, op.cit., 2019, p. 8.

<sup>15</sup> The KPMG report shows that most companies with registered IPRs, regardless of size, have never tried to gain finance by leveraging their intangible assets, as essentially this is not viewed as a relevant option.

<sup>16</sup> Ibid., p. 11.

<sup>17</sup> KPMG Spain, „2019 Intellectual Property SME Scoreboard“, op.cit., 2019, p. 6.



This frown upon IP may be explained by the fact SMEs are often extremely reliant on bank loans and credits to grow, as they do not often have sufficient funding and/or collateral to guarantee those lending operations. IP would therefore prove to be useful in this sense, should the regulatory framework guarantee a proper securitization regime for IPRs. The main struggle is that in most states, the development of the market for IP collaterals is non-existent or underdeveloped<sup>18</sup>. Indeed, many jurisdictions do not yet offer adequate legal means for IP financing, i.e. using IP rights to obtain or secure finance<sup>19</sup>.

We may identify two main challenges to developing IP-backed debt financing for SMEs as follows:

1. the lack of a clear connection between the security and the underlying asset; and
2. the complexity and lack of transparency in the IP system that results in distrust of the intangible economy<sup>20</sup>.

Some scholars pushed the reflection further and estimated, in the alignment of what the UNCITRAL Legislative Guide on Secured Transactions (hereinafter “UNCITRAL Guidelines”) proposed that IP financing may be fostered by: (1) Drafting a generic law of financing that is applicable for all types of IP under all current international IP related conventions; (2) Coordinating priority systems in IP financing with priority systems in debtor financing; (3) Refining IP valuation methods; (4) Increasing the strength of IP laws and the reliability of registries; (5) Integrating underwriters and title insurers to help increase confidence in IP securities<sup>21</sup>.

## 2.1.2. Collateralization of IP Rights : Taxonomy of Property Law

The possibility of using IP right as collateral can flow from its general classification as personal, movable, or intangible property in the sense of the general principles of property law.

The different types of interest that may be taken by SMEs in IPRs mainly depend on secured transactions law, which is not unified nor harmonized internationally<sup>22</sup>. Secured transaction law is also is not always designed to cover IP rights; while some jurisdictions apply the rules relating to security rights over tangibles, others follow the rules on security over intangibles in general or on security over claims<sup>23</sup>.

We may therefore differentiate between different types of approaches: some jurisdictions apply a functional, uniform approach which is often accompanied by a notice filling approach<sup>24</sup>: such *functional approach* - which resembles the approach implemented in the US and in Canada, where the market is more liberal - implies that it covers all interests in any personal property “that secures payment or performance of an obligation”, regardless of its form<sup>25</sup>.

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<sup>18</sup> J. DENONCOURT, „IP Debt Finance and SMEs: Revealing the Evolving Conceptual Framework Drawing on Initiatives from Around the World“, T. KONO (ed.), *Security Interests in Intellectual Property*, Perspectives in Law, Business and Innovation, 2017, p. 2.

<sup>19</sup> Ibid., p. 3.

<sup>20</sup> B. TUNCAK, “The WIPO Information meeting on IP Financing: some notes”, (2009), available at: <http://www.ip.finance/2009/03/wipo-information-meeting-on-ip.html> ;

<sup>21</sup> Ibid.

<sup>22</sup> E.-M. KIENINGER, “Security Rights in Intellectual Property: General Report”, op.cit. p.15.

<sup>23</sup> Ibid.

<sup>24</sup> Ibid.; see also J. DENONCOURT, “IP Debt Finance and SMEs: Revealing the Evolving Conceptual Framework Drawing on Initiatives from Around the World”, o.cit., p. 4.

<sup>25</sup> Ibid., p. 16.

Another approach is a *non-functional approach* that rather lists different types of security rights, some of which are based on the model of a limited real right (i.e. pledge, charge, and mortgage) and some of which are based on ownership (i.e. security ownership, security assignment, and retention of title) and adopt a non-functional approach where the classification of the different types of collateral is of greater importance.

### 2.1.3. Belgium Hybrid Regime : a Functional and Non-Unitary Approach

Belgium is now considered one of the most modern European regimes regarding the provision of securitization for IP. Its latest regime has been vastly influenced by the UNCITRAL Guidelines<sup>26</sup>. However, it does not fully recognize IPRs as collaterals, but its New Pledge act allows for property rights to be granted on all types of IP rights, regardless of the type of right concerned. In Belgium, IP rights are considered to be “movable and intangible assets”, and as such are capable of being the subject of those security rights that exist for movable, intangible assets<sup>27</sup>.

Despite this characteristic that qualifies within a rather *functional approach*, Belgian law still distinguishes between retained rights, granted rights, and privileges by operation of law and is therefore characterized here as a *functional but non-unitary system*<sup>28</sup>. Also, Belgium has opted for a system of transaction filing rather than notice filing<sup>29</sup>.

Therefore, we can advance that Belgium is currently using an IP-debt financing system where the possibility to grant IP assets in exchange for funding is already recognized for all types of companies, with some specific conditions. The main issue of the current Belgian regime lies with (i) the risk of diminution on the long term of the IP asset value, and the mismatch with the possibility to use license to generate funding while such rights are pledged and (ii) with the current dissymmetry caused by the registration requirements of the right of the pledge which is split between the general national pledge register and the specific IP rights registers. There is, therefore, a need for better coordination between IP registries and the use of registration as a mode of perfection under secured transactions law<sup>30</sup>.

## 2.2. Importance of IP Valuation

The value of an IP asset essentially derives from (i) the exclusivity it grants to its owner, (ii) the measure it generates measurable economic benefits and (iii) the measure it increments the value of assets of a different nature but associated with it. Such value can be obtained through direct exploitation of the IP asset (e.g. by integration with a product, sale or licensing), or by other means (e.g. reducing substitutes on the market).

A proper IP valuation is fundamental and necessary to use IP rights as an instrument to obtain credit and/or financing, as well as for catching the attention of potential partners: in cases of a joint venture, strategic alliance, merger or acquisition, it can also help in determining the contribution of each partner involved. The possibility of valuating IP assets separately is

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<sup>26</sup> J. DENONCOURT, “IP Debt Finance and SMEs: Revealing the Evolving Conceptual Framework Drawing on Initiatives from Around the World”, o.cit., p. 4.

<sup>27</sup> E.-M. KIENINGER, “Security Rights in Intellectual Property: General Report”, op. cit., p. 9.

<sup>28</sup> Ibid., p. 25.

<sup>29</sup> Ibid.

<sup>30</sup> E.-M. KIENINGER, “Security Rights in Intellectual Property: General Report”, op. cit., p. 42.

particularly relevant in increasing the success rate, together with the ability to prove that they will remain valid until the end of the financing repayment term<sup>31</sup>.

### 2.2.1. Obstacles to IP Valuation

Despite its importance, IP valuation also poses substantial issues and obstacles. The valuation of intangibles and, in particular, intellectual property assets, involves a series of steps and there is a lack of a commonly recognized standard method, a situation made more complex by the variety of IP rights and the difficulty in determining a specific and stable value for IP assets.

Moreover, to be evaluated, an IP asset needs to, inter alia: (i) be separately identifiable and describable; (ii) have tangible evidence of existence; (iii) have an identifiable time of creation and destruction/termination; (iv) be legally enforceable and transferable, separately from the other business assets; and (v) have a specific income stream<sup>3233</sup>.

The calculating of IP assets' value is, moreover, easier to achieve if they have acquired formal protection, e.g. through trademarks or patents registration, and if they are tradable on a non-regulated market<sup>34</sup>.

### 2.2.2. Classical IP Valuation Methods

The first step for an IP valuation is the gathering of information on the IP asset, including its position in the specific business and the characteristics of the relevant market/industry. The valuation can be carried out internally, but also through IP auditing: in particular, the type of IP auditing recommended is the event-driven one, also known as *IP due diligence*<sup>35</sup>.

Once the relevant information has been gathered and analyzed, there are three main valuation methods applicable and each of them can lead to differing results: they are the revenue method, the market method, and the cost method.

#### The Revenue Method

The revenue (or income) method is the most commonly used method for IP valuation and it is based on the estimated financial benefits deriving from the IP right, often including an adjustment to present-day value. This method is best used in the case of IP assets with positive cash flows, whose cash flows can be estimated with some degree of reliability for the future, and if there is the possibility of obtaining discount rates through a proxy for risk<sup>36</sup>.

There are various income methods applicable and the most used one is the Discounted Cash Flow (hereinafter "**DCF**"), in which the appropriate measure of economic income is projected for several discrete time periods into the future, a projection that is then converted into a present value by the use of a present value discount rate.

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<sup>31</sup> WIPO, Valuing Intellectual Property Assets, [https://www.wipo.int/sme/en/value\\_ip\\_assets/#](https://www.wipo.int/sme/en/value_ip_assets/#)

<sup>32</sup> Ibid.

<sup>33</sup> Korean Intellectual Property Office and World Intellectual Property Organization, "IP Panorama", Module 11 *IP Valuation*, 2007, p. 8

<sup>34</sup> T. KARIUS, "Intellectual property and intangible assets: Alternative valuation and financing approaches for the knowledge economy in Luxembourg", *EIKV Schriftenreihe zum Wissens- und Wertemanagement*, No. 3, European Institute for Knowledge & Value Management (EIKV), Rameldange, 2016, p.22.

<sup>35</sup> WIPO, Valuing Intellectual Property Assets, op. cit.

<sup>36</sup> WIPO, Valuing Intellectual Property Assets, [https://www.wipo.int/sme/en/value\\_ip\\_assets/#](https://www.wipo.int/sme/en/value_ip_assets/#)

This DCF method is easiest to use with, and it best captures the value of, IP assets (i) with currently positive cash flows, (ii) with cash flows which can be estimated with some reliability for future periods (iii) generating relatively stable cash flows (iv) where a proxy for risk can be used to obtain discount rates.

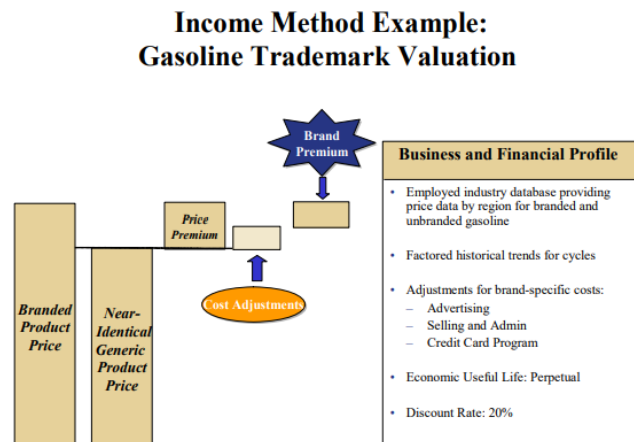
However, the DCF method fails to accommodate options like the nature of some corporate investments and does not keep into account managerial flexibility. All risks are aggregated and are considered to be appropriately adjusted for in the discount rate and the probability of success, rather than being broken out and dealt with individually. It also does not consider dependencies on patents owned by third parties and it does not consider the unique independent risks connected with an IP asset like patents <sup>37</sup>.

#### Example 1:

Type of right: retail gasoline trademark of an oil company.

Gasoline price is inter alia defined by the prices of crude oil, refining, local regulatory factors, location and brand. Knowledge of the data relating to price and brand allows the company to determine a price premium for the trademark, vis a vis the price of similar unbranded gasoline.

The price premium is then adjusted to account for the incremental costs related to brand support, (e.g. advertising, costs connected to the credit card program, identifiable selling and admin costs estimated to be above those necessary for an unbranded product) and multiplied by the annual projected sales of branded gasoline. As the economic life of a trademark can be infinite if preserved well, there is no terminal value but a discount rate of 20% can be employed, based on standard rates of return on brand-related assets.



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#### Example 2:

Type of right: a bundle of 100 patents.

A company is considering becoming a licensee of 100 patents, as it knows that their owner will offer the patents for sale to third parties and there is a risk of being sued for the infringement of 5 patents.

Therefore, considering the following:

- 80% chance of being sued on a risky patent

<sup>37</sup> Korean Intellectual Property Office and World Intellectual Property Organization, "IP Panorama", Module 11 "IP Valuation", 2007, pp 24-25

<sup>38</sup> P. FLIGNOR, D. OROZCO, *Intangible Asset and Intellectual Property Valuation: a multidisciplinary perspective*, 2006, ipthought. Com, pp 11-12

- 30% probability of loss
- 10 M targeted activity and est. exposure in case of loss
- 1 M of litigation costs?

Risk Patents		Hit Rate		Expected Suits		Loss Rate		Exposure in Loss		Avg. Lit Expenses		Total
5	x	80%	=	4	x	[(30%	x	\$10M)	+	\$1M]	=	\$16M

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## The Market Method

The market method includes a search for comparables, as it involves a comparison with the price actually paid in similar circumstances for the transfer of comparable assets. While it is simple in theory and it is more likely to mirror market perceptions and dispositions, it needs an active marketplace for the interested IP right and access to such business information, which can be lacking. Moreover, the market method does not account for the unique characteristics of a specific IP asset and/or transaction<sup>40</sup>.

To conduct the comparison, many variables and factors need to be kept into consideration, inter alia: IP duration, exclusivity and territory (geographical coverage), nature of IP asset, the degree to which the IP asset contributes to the demand for the related product, the existence of substitutes. Sources of Comparables and "Industry Standard" Data include: statutory/official filings, surveys licensing publications, valuation books, published court cases, published agreements, online databases (Royalty Source, ReCap, Windhover), consultants<sup>41</sup> (in particular licensing specialists), Licensing Executives Society, and company annual reports.

This method is best used to evaluate royalties and tax and can be combined with the revenue method<sup>42</sup>.

Example

Type of right: royalty rates of trademarks of a cosmetic company.

The trademarks will be licensed for a specific timeframe to a series of companies in a specific region - e.g. Latin America - on an exclusive basis.

First, there is the identification of a baseline transaction (in this case, an exclusive license of the same trademarks with no upfront fee and a royalty rate of 7% to a company located in a different geographical region- e.g. Western Europe- and a longer timeframe). To apply the Market Method, the following adjustments have to be done on the baseline transaction:

- Location: Keeping into consideration the demographics and competitive factors of the territories, the underlying value of the trademarks in the cosmetic industries have been deemed comparable.

<sup>39</sup> APEC Intellectual Property Group, Intellectual Property (IP) Valuation Manual: A Preliminary Guide, 2018, p. 21

<sup>40</sup> T. KARIUS "Intellectual property and intangible assets: Alternative valuation and financing approaches for the knowledge economy in Luxembourg", , EIKV Schriftenreihe zum Wissens- und Wertemanagement, No. 3, European Institute for Knowledge & Value Management (EIKV), Rameldange 2016, p.25

<sup>41</sup> Korean Intellectual Property Office and World Intellectual Property Organization, "IP Panorama", Module 11 "IP Valuation", 2007, pp 21

<sup>42</sup> WIPO, Valuing Intellectual Property Assets, [https://www.wipo.int/sme/en/value\\_ip\\_assets/#](https://www.wipo.int/sme/en/value_ip_assets/#)

- Advertising support: As Latin America is a new territory, additional expenses have to be considered for advertising. The Licensor agrees to provide marketing support and the royalty rate is consequently adjusted by reimbursing the licensor for the advertising costs (e.g. 1M) plus a one-year cost of capital to compensate for the time value.
- IP Strength: The protection and ability to manage trademarks is deemed lower in Latin America. Therefore, there is a decrease in the royalty rate of 0.5% of net sales.
- Length: longer licensing agreements usually have lower royalty rates, unless the agreement is likely to be renewed at the end of the shorter license taken into consideration. In the latter case, no adjustment is needed;

Base royalty rate 7% of net sales			
Base Contract	Tested Contract	Adjustment Method	Adjustment
<b>Location:</b> Western Europe	Latin America	None	0%
<b>Advertising:</b> None	Up to \$1M in year 1	Reimburse	0.2%
<b>IP Legal Strength:</b> Strong	Moderate	Subjective Estimate	(0.5%)
<b>Length:</b> 5 years, renewable	3 years, renewable	None	0
			<b>6.7%</b>

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## The Cost Method

The Cost Method considers the cost of creating the IP and can be applied also through comparison, by looking at the cost of similar IP assets. It has two variants: the reproduction cost method considers the creation of a copy of the subject IP, while the replacement cost method focuses on the cost to recreate the functionality or utility of the relevant IP<sup>44</sup>.

This method is often criticized and is the least used one, also because it does not account for wasted costs and can fail to consider specific characteristics of the asset, but it is particularly suitable for: (i) easily reproducible assets; (ii) hard to quantify economic benefits; and (iii) if the IP asset is currently not generating income, as it is newly created.

It is, therefore, particularly recommended for the evaluation of software, early-stage technology that is not yet producing revenue, or to determine floor price<sup>45</sup>. This method can also be used where the IP asset's owner has enough knowledge and data to assist in the estimation of the cost or where the IP asset is part of the income-producing process but does not actually generate any income by itself<sup>46</sup>.

### Example

To identify the cost related to the development of a pharmaceutical preparation, the company can decide between reproduction (the cost that will be spent to reconstruct the exact replica of the IP asset) and replacement (what is usually spent to replace an asset) costs. For the type of asset in question, the company has to account for:

<sup>43</sup> P. FLIGNOR, D. OROZCO, *Intangible Asset and Intellectual Property Valuation: a multidisciplinary perspective*, 2006, ipthought. Com, pp 10-11

<sup>44</sup> Korean Intellectual Property Office and World Intellectual Property Organization, "IP Panorama", Module 11 "IP Valuation", 2007, pp 16

<sup>45</sup> Ibid.

<sup>46</sup> International Chamber of Commerce (ICC) "Handbook on valuation of Intellectual Property Assets" 2019, p. 16

- R&D (e.g. 1.1 B)
- Patent registration and legal costs (85 K)
- Clinical Trials (USD1.2 B)
- Labor and other costs (171 M)<sup>47</sup>

### 2.2.3. Alternative Methods to IP Valuation

In view of the flaws of the aforementioned traditional methods, different ones have been proposed to date. Between them, the one proposed by Tim Karius is particularly interesting. He recommends the use of a more anticipative approach similar to the one applied by the IPscore<sup>48</sup>, an IP evaluation tool, introduced by the Danish Patent and Trademark office<sup>49</sup> and developed at EU level by the European Patent Office (EPO).

This IPscore uses a qualitative approach by focusing on characteristics like the strength of the legal protection and by analyzing various indicators to then give a rating to the IP right. Therefore, it allows the evaluation of patent portfolios and individual patent applications and granted patents.

The method suggested by Tim Karius uses a similar approach, by calculating an average IP risk factor based on duration and object of protection, and jurisdiction. Such an approach is easier to use for IP assets with an established protection period while, for the other assets, the point of reference is the asset's life expectancy<sup>50</sup>.

Irrespective of the choice of method, the effect of functional, technological and economic obsolescence on the value of IP needs to be considered. Moreover, it is possible to combine the methods to crosscheck the results<sup>51</sup>.

In summary, the method should be chosen according to: (i) the kind of industry, (ii) the degree of maturity of the asset, (iii) the degree of risk, (iv) the IP right, (v) available information / price of comparable assets. Furthermore, the valuation should be done regularly<sup>52</sup>.

### 2.2.4. Standards and IP Valuation

While assessing the value of IP rights, it is also recommendable to look for and consider existing Standards that can be relevant including, in particular, accounting standards, as they can give guidance in applying the methods and in understanding the result of their application. There are several standard-setting bodies at the international level, inter alia the International Organization for Standardization (ISO)<sup>53</sup>, the Organisation for Economic Cooperation and Development (OECD), the International Accounting Standards Board (IASB) or the International Valuation Standards Council (IVSC). There are also some bodies at the regional level, such as the CEN

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<sup>47</sup> APEC Intellectual Property Group, Intellectual Property (IP) Valuation Manual: A Preliminary Guide, 2018, p. 17

<sup>48</sup> European Patent Office, IP score, available at: <https://www.epo.org/searching-for-patents/business/ipscore.html>

<sup>49</sup> P.- E. NIELSEN, „Evaluating Patent portfolios – a danish initiative“, World Patent information, Volume 26, Issue 2, 2004, p. 143-148.

<sup>50</sup> T. KARIUS, “Intellectual property and intangible assets: Alternative valuation and financing approaches for the knowledge economy in Luxembourg”, op.cit., p.41.

<sup>51</sup> Ibid., p.23.

<sup>52</sup> C. HACKL “IP value extraction and commercialisation - Determining the value of IP“, EPO in collaboration with the Technical University of Munich, 2018, p. 80.

<sup>53</sup> <https://www.iso.org/home.html>

(Comité Européen de Normalisation), and national ones<sup>54</sup>. In Belgium, the Bureau for Standardisation (NBN) is responsible for developing and selling standards in the country<sup>55</sup>.

While specific, generalised standards for IP valuation do not currently exist, standards for the valuation of intangibles can be used as guidelines<sup>56</sup>: e.g. the ISO 10668:2010<sup>57</sup> on brand valuation<sup>58</sup> and ISO 20671 on brand evaluation<sup>59</sup>; the International Valuation Standards IVS-210 on intangible assets<sup>60</sup> (it provides general guidance on the valuation of intangible assets, IP included); the International Accounting Standards IAS 38 on intangible assets; and the IFRS standards, including the specific standards for small & medium-sized businesses. The recognition of IP assets as specific assets by international accounting standards is indeed a signal of the rising importance of IP for many businesses: such standards should then be kept into consideration, together with local accounting standards applicable<sup>61</sup>.

## 2.3. Use of IP as Collateral for Debt Financing

In 2000, the United Nations Commission on International Trade Law (UNCITRAL) established a Working Group to address security rights in personal property, including intangible assets, while intellectual property rights (IPR) began to be formally introduced as a separate type of encumbrance for exploration as of 2008.

It is well-known by today that intangible assets, including IPR, can significantly increase a company's asset value, thus improving the company's position in negotiations with banks, facilitating the company's access to credit or securing cheaper interest rates on credits. In cases where borrowers pledge their patents, trademarks or copyrighted works, the collateral pool increases in value and the chances to receive a loan are increased as well.

Companies, particularly smaller ones, that do not have enough tangible properties but do have IPR, could opt for IP debt financing, meaning that they could use IPR as collateral for banking institutions that provide funds to the company<sup>62</sup>. However, in practice, IP debt financing is still "reserved" for large companies that have portfolios of already commercialized IPRs, while smaller companies depend on IP valuation - an activity that faces many problems in practice, as was presented in detail in the previous part of the study<sup>63</sup>.

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<sup>54</sup> International Chamber of Commerce (ICC) "Handbook on valuation of Intellectual Property Assets" 2019, p. 10.

<sup>55</sup> <https://www.nbn.be/en>

<sup>56</sup> T. KARIUS, "Intellectual property and intangible assets: Alternative valuation and financing approaches for the knowledge economy in Luxembourg", op.cit., p.38.

<sup>57</sup> <https://www.iso.org/standard/46032.html>

<sup>58</sup> To be noted a recent ISO standard relevant for IP: the ISO 56005:2020 proposing guidelines for supporting the role of IP within innovation management.

<sup>59</sup> <https://www.iso.org/standard/68786.html>

<sup>60</sup> <https://www.ivsc.org/>

<sup>61</sup> International Chamber of Commerce (ICC) "Handbook on valuation of Intellectual Property Assets" 2019, p. 10

<sup>62</sup> T. SHIMIZU, Intellectual Properties and Debt Finance for Startups, T. KONO (ed.), *Security Interests in Intellectual Property, Perspectives in Law, Business and Innovation*, Springer Nature Singapore Pte Ltd. 2017, p. 40.

<sup>63</sup> Chapter 9. IP-Based Financing Of Innovative Firms, Enquiries Into Intellectual Property's Economic Impact, OECD, 2015, p. 463



### 2.3.1. Situation in Belgium

As presented, Belgian law considers IPR to be movable and intangible assets, and as such, they are capable of being the subject of the security rights that exist for movable, intangible assets<sup>64</sup>.

Article 7(6) of the new Belgian Pledge Act<sup>65</sup> specifically mentions pledges having as their object IP rights as potential collateral as long as they are not incompatible with other provisions specifically governing such pledges:

*“... Les dispositions du présent Chapitre ne sont applicables aux gages ayant pour objet des droits de propriété intellectuelle que dans la mesure où elles ne sont pas incompatibles avec d'autres dispositions régissant spécifiquement de tels gages.”*

Registration of the pledge is necessary to be carried out in the National Register of Pledges (article 26(1) of the Belgium Pledge Act. Registration is valid for 10 years and it can be renewed for another 10-year period (article 35(1)).

With regards to the pledges secured over certain IPRs, the Belgian Code of Economic Law (hereinafter “CEL”) specifies when they must be registered in their IP- specific Register. In case of the securitization of a Belgian Patent, article XI. 52 CEL provides that the pledges secured over patents must be notified to the Patent Office. Once notified, the pledge will be registered in the Patent Register. The ratio legis behind the registration of the pledge in the Patent Register stems from Article XI. 50, §4 which governs the assignment of the IPRs of Belgian patents, and more precisely the dissemination of information and the opposability of the status and the application of the patent to third parties.

Nevertheless, it remains unclear whether a proper registration in the IP-specific register, such as the Patent Register, will be automatically implemented in the National Pledge Register. This implies that SMEs holders may still be under the obligation to check both registers to receive a complete overview of the securitization status of their IPRs. “

### 2.3.2. Security Rights in IP Related Assets (e.g. Royalties and Licences) / IP Royalty Securitization

IP securitization can be defined as a financing technique, which consists in placing an IP asset or the rights to its projected revenues (e.g. royalties) by a company (borrower) in a special purpose vehicle (SPV), which in turn issues securities in the capital markets. This technique enables a borrower to obtain more favorable funding conditions, as the securities issued by the SPV are in theory separated from the company's risk and the lending institutions can eliminate risks<sup>66</sup>.

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<sup>64</sup> E.-M. KIENINGER, Security Rights in Intellectual Property: General Report, E.-M. KIENINGER (ed.), *Security Rights in Intellectual Property, Ius Comparatum – Global Studies in Comparative Law* 45, Springer Nature Switzerland AG 2020, p. 9.

<sup>65</sup> Law on the Right of Pledge, available at:

[http://www.ejustice.just.fgov.be/cgi\\_loi/change\\_lg.pl?language=fr&la=F&cn=2013071122&table\\_name=loi](http://www.ejustice.just.fgov.be/cgi_loi/change_lg.pl?language=fr&la=F&cn=2013071122&table_name=loi)

<sup>66</sup> Chapter 9. IP-Based Financing Of Innovative Firms, Enquiries Into Intellectual Property's Economic Impact, OECD, 2015, p. 464

The main differences between IP securitization and securitization of tangible assets are based on the following:

- IP consists of exclusive rights, enforceable against anyone (with certain limitations of IPR)
- IPRs cannot be held in possession.
- IPR are non-rivalrous and non-excludable
- Intellectual property is frequently contained in tangible – physical – embodiments

Benefits of IP securitization:

- (i) IP is an untapped source of collateral;
- (ii) IP securitization offers a quick return on research and development; and
- (iii) IP securitization captures additional value.

IP securitization is an appropriate method for funding or financing industries where making money on products or services is a lengthy process (for instance, the IT and biotech industry, where production and research costs are high, and the capital is required not only to operate, but also to develop and market the products).<sup>67</sup> In the case of IP securitization, the company assigns a portion of its future revenue from licensing its IP portfolio in exchange for upfront, lump-sum funding. Namely, the company, as a licensor of IP, presents the future cash flow expected from a license agreement in order to receive a respectable cash payment upfront, while it keeps the possibility to profit from the upside value beyond the security interest on the debt<sup>68</sup>.

Yet, one of the obstacles for IP securitization is reflected in the fact that, when it comes to SMEs, IPR is usually embedded in the business, meaning that owners create IP specifically for their own businesses and do not consider the possibility of licensing those IP. In other words, they do not consider how to make money by using IP themselves but rather how to make money by using IP as a part of their business. Therefore, it is difficult to exercise security rights, as IPR are developed under the specific context of the particular business and they lose their value once separated from the business<sup>69</sup>.

Regarding the IP royalty securitization in Belgium, the creation of a security right in royalties is possible without any registration<sup>70</sup>.

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<sup>67</sup> D. ERDENECHIMEG, *Using Intellectual Property As Collateral: An International Experience And A Mongolian Perspective*, WIPO And University Of Turin, 2016, p. 10.

<sup>68</sup> D. ERDENECHIMEG, *Using Intellectual Property As Collateral: An International Experience And A Mongolian Perspective*, WIPO And University Of Turin, 2016, p. 7.

<sup>69</sup> T. SHIMIZU, *Intellectual Properties and Debt Finance for Startups*, T. KONO (ed.), *Security Interests in Intellectual Property, Perspectives in Law, Business and Innovation*, Springer Nature Singapore Pte Ltd. 2017, p. 48. – author gives an example of Japan, but it seems to be the situation in other countries as well

<sup>70</sup> E.-M. KIENINGER, *Security Rights in Intellectual Property: General Report*, E.-M. KIENINGER (ed.), *Security Rights in Intellectual Property, Ius Comparatum – Global Studies in Comparative Law 45*, Springer Nature Switzerland AG 2020, p. 21.

### 2.3.3. IP License-Backed Transactions and IP-Backed Loans

Aiming at increasing its liquidity for short-term operations but maintaining the use of its IPR, a company can sell its IP to a third party (the back-licensor) in exchange for immediate funding and purchase the license for its IP assets (the company is now the back-licensee). The company may retain the option to buy back the IP asset at a predefined price, during or at the end of a specified term<sup>71</sup>.

The transaction can be backed by the stream of revenues tied to a single intellectual asset or to the firm's entire portfolio. In the pharmaceutical and biotechnology sectors, transactions are usually backed by a current or prospective royalty stream<sup>72</sup>.

On the other side, IP can directly be pledged as collateral in a loan agreement, so that the lender can seize it if the firm becomes insolvent. The key difference between this financing method and IP license-backed transaction is that, in the second case, a company is not borrowing money, but rather it is selling or licensing back a stream of anticipated future cash flows that would otherwise accrue to the company directly.

However, lending to SMEs is usually subject to high transactions costs for a few reasons: (i) asymmetric information on the company's creditworthiness, (ii) operating at small-scale increases the fixed risk-assessment costs and (iii) the presence of IP can be perceived as an additional source of uncertainty about the expected returns of the company's projects and the value of IP<sup>73</sup>.

### 2.3.4. IP Collateral Enhancement

In addition to the previously presented methods, the IP assets can be used as an addition to a broader collateral package<sup>74</sup>, thus improving the overall credit profile of a borrower and possibly lowering interest rates demanded by the lender. IP collateral enhancement provides the lender with a creditworthy value upon which to determine lendable IP collateral advance rates.

When assessing collateral for collateral enhancement purposes, a key question for lenders and bank regulators is whether the collateral can be sold or monetized in a reasonable period of time. The typical term of IP collateral enhancement coverage is up to five years, and the fees vary based on the perceived riskiness of the borrower and the IP assets<sup>75</sup>.

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<sup>71</sup> Chapter 9. IP-Based Financing Of Innovative Firms, Enquiries Into Intellectual Property's Economic Impact, OECD, 2015, p. 464

<sup>72</sup> New Approaches to SME and Entrepreneurship Financing: Broadening the Range of Instruments, OECD Report 2015, p. 20.

<sup>73</sup> *Ibid*, p. 465

<sup>74</sup> S. VEPACHEDU, "Intellectual property monetization and collateralization", *Cardinal Intellectual Property*, Inc. 2017

<sup>75</sup> Article "Financing Alternatives for Companies" as of 10 May 2020, at the Quantum Analytics Platform, available at: <https://quantumterminal.com/financing-alternatives-for-companies/> ; Article mentions a US collateral enhancement firms that specialize in IP transactions (M●CAM Global Holdings LLC), which assist regulated banks and traditional asset-based lenders to evaluate IP as collateral.

### 2.3.5. Non Fungible Tokens (NFTs) as a Tool to Raise Funding

Non-fungible tokens (“**NFTs**”) represent digital assets (images, songs, videos, etc.) that are verified through blockchain technology. In other words, NFTs create a blockchain-based digital certificate, which testifies that the asset at issue is owned by a specific person<sup>76</sup>. Unlike physical money or cryptocurrencies, one NFT cannot be exchanged for another, nor can two NFTs be equal.

NFTs can only have one official owner at a time and they are secured by the Ethereum blockchain so that no one can modify the record of ownership or duplicate the NFT. Ownership of each NFT is publicly recorded and can be verified by anyone.<sup>77</sup> Therefore, the NFTs enable evidencing the ownership of assets represented in a token form (i.e., tokenized assets).<sup>78</sup>

NFTs present a new way for creators to license, monetize and enjoy more substantial financial participation throughout the copyright's duration.<sup>79</sup> For example, instead of selling the artwork with the help of auction houses, an artist can sell it directly as NFTs. As a result, artists can gain more profits, so they will receive a percentage of sales whenever their artwork is sold to a new owner. In addition, using NFTs for digital artwork as collateral in a decentralized loan is an example of how NFTs can be used for unlocking new financing opportunities.<sup>80</sup>

#### - Decentralized finance and NFT-backed loans

Decentralized finance (“**DeFi**”) is a global financial system that encompasses financial products and services accessible to anyone with an internet connection. Within the DeFi, markets are open and there are no centralized authorities (governments or institutions) who could deny access to financial services to anyone<sup>81</sup>.

There are DeFi platforms<sup>82</sup> that offer a possibility of borrowing money by using NFTs as collateral, which guarantees that the loan will be repaid back to the lender. If the borrower fails to pay back the borrowed amount, the assets tokenized as NFTs will be transferred to the lender.

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<sup>76</sup> According to Forbes (see [here](#)), NFTs are becoming an increasingly popular way to buy and sell digital artwork. There are already some companies that allow creators to own and sell their work as NFTs. For instance, [UREEQA](#) verifies the creative work's ownership, authorship and originality in order to place work at issue on the Ethereum blockchain in the form of a non-fungible token (NFT).

<sup>77</sup> Information available here: <https://ethereum.org/en/nft/> , last access on 25 June 2021

<sup>78</sup> Evans, Tonya M., Cryptokitties, Cryptography, and Copyright, 2018 Brigham Young University Copyright and Trademark Symposium - Emerging Issues in the Digital Age, AIPLA Quarterly Journal, Vol. 47, Issue 2 (Spring 2019), p. 248.

<sup>79</sup> *Ibid.*, p. 264.

<sup>80</sup> Information available here: <https://ethereum.org/en/nft/> , last access on 25 June 2021

<sup>81</sup> Information available here: <https://ethereum.org/en/defi/#lending> , last access on 26 June 2021

<sup>82</sup> NFTFI, a platform for NFT collateralized loans, available here: <https://nftfi.com>

## 2.4. Use of IP as Security for Equity Financing

As explained above, accessing finance is a major issue for SMEs because of multiple reasons. Access to banking finance is even more difficult for SMEs with a higher risk-return profile, whose business model relies on intangibles and whose profit patterns are often hard to forecast. Furthermore, not all means of financing are suitable for all SMEs, depending on their risk-return profile, stage in the business life cycle, size, scale, management structure and financial skills<sup>83</sup>.

For new and innovative SMEs, which have a high risk-return profile, equity finance can be a good (alternative) solution to provide adequate funding. Equity finance encompasses funding by business angels, joint venture and venture capitals, and structural alliances<sup>84</sup>.

The main difference between debt finance and equity finance is that equity investors do not focus exclusively on IP but rather take a stake in the whole company. Therefore, instead of making a decision solely on the valuation of the IP of the enterprise at issue, equity investors assess the expected profitability of the enterprise in its entirety. Nevertheless, the presence of IP rights and/or IP strategy can signal the quality of the company to the investors, particularly business angels and venture capitalists<sup>85</sup>. Unlike debt finance, equity finance does not impose specific repayment requirements, which means that the pressure on the firm's cash flow is minimal, so the cash flows can be used to finance growth and expansion. Finally, equity investors, particularly venture capitalists usually provide non-financial services (for instance, they identify business opportunities or provide management and technical assistance) that can add value to the business and improve the corporate governance of the enterprise at issue.

The availability of equity financing for SMEs is often influenced by national authorities, in particular through the taxation position of investors and enterprises. In 2012, the European Business Angel Network (EBAN) has carried out a review of the amount of tax relief available in different Member States to business angels and found that Belgium is one of eight countries<sup>86</sup> that have fiscal incentives specifically available for venture capital, private equity and start-up angels. Incentives in these countries usually include government guarantees, reductions on tax rates or tax credits<sup>87</sup>.

Finally, Belgium has recently changed its corporate law in a way that might ease SMEs' access to equity finance. Namely, the new Code of Companies and Associations (*Code des sociétés et des associations*) from 2019 promotes the private limited liability company (BV) as the most important form of the company, and offers a high degree of flexibility by allowing the founders to structure equity as they wish. The BV can create new kinds of securities, such as different forms of multiple voting rights (without limitation in the number of votes), preferential dividends, etc. Also, the articles of association of the BV can freely determine the modalities of the exit of the shareholder<sup>88</sup>.

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<sup>83</sup> E. Pederzini, A. Toniolo, *SMEs' Equity Financing: Does Corporate Law Matter?* European Company Law Journal 17, no. 6, 2020, p. 2

<sup>84</sup> In addition, equity crowdfunding may also be seen as a means of equity finance, whereas it presents a financial tool that can be used by startups to close a gap in funding at a very early stage or to avoid selling substantial equity to other types of investors (see: E. Pederzini, A. Toniolo, p. 3).

<sup>85</sup> Chapter 9: IP-based financing of innovative firms, OECD report, 2015, p. 460 (p. 457-477), available here: <https://www.oecd.org/sti/ieconomy/Chapter9-KBC2-IP.pdf>

<sup>86</sup> The full list of the EU Member States with fiscal incentives includes the following countries: Belgium, France, Ireland, Italy, Germany, Luxemburg, Portugal and the United Kingdom

<sup>87</sup> EBAN and BDO, Tax outlook in Europe – Business angels perspective, 2012, p. 7, available here: <http://www.eban.org/wp-content/uploads/2014/09/12.-Compendium-fiscal-incentives-2012.pdf>

<sup>88</sup> See note 73, p. 8.

### 2.4.1. Business Angels

Business angels are high-net-worth investors (usually individuals) who invest in and support high-risk start-ups at a very early stage, in exchange for participation in the future profit of the enterprise. Besides money, they also invest time, share experience and knowledge, and provide connections to their large networks in order to guide the enterprise in its new business.

In other words, business angel investment covers the riskiest stage in an SME's development, thus providing the SMEs with the necessary funds to continue developing and reaching the next stage, where it can look for new investors (e.g. venture capital, as it will be presented below). Importantly, business angels are generally patient investors, meaning that they do not expect to refund the invested money in a short period of time<sup>89</sup>.

Given that business angels decide on investing in the very beginning of the existence of SMEs, they might have difficulties in screening the potential targets (SMEs) and selecting those that have the greatest chances to develop and become successful. In that regard, the presence of IPR can be a strong signal for the business angels that the enterprise at issue has the potential to become profitable. Moreover, for very small enterprises, IPR can be the only asset such enterprises have that can be objectively evaluated when deciding whether to invest.

In Belgium, there are two main business angels networks, members of the Business Angels Europe association based in Brussels:

- Business Angels Network (Ban Vlaanderen) is the Flemish business angels network, founded in 1999. Its goal is to stimulate the economic growth in Belgium by developing, guiding and promoting entrepreneurship by bringing together capital-seeking entrepreneurs and private investors (business angels).
- Be Angels operate in the French-speaking area of Belgium, and it was formed in 1999 to bring together entrepreneurs looking for support and financial means and private investors (business angels) ready to invest in promising companies.

### 2.4.2. Joint Ventures and Venture Capitals

A joint venture may consist of any variety of business relationships that involve two or more enterprises pooling their resources to realize a common business goal. In such relationships, one party will often provide technology or know-how of which they are the proprietor and the other party may contribute financial support and expertise of their own to the project<sup>90</sup>.

Venture capital investors (or venture capitalists, VC), are private equity investors who provide capital to young enterprises with high growth potential in exchange for an equity stake. They may fund start-ups or small enterprises that wish to expand and that have already reached the stage where they are looking to commercialize their idea. Like for business angels, IP can signal to the VC that the selected enterprise has the potential to gain profit in the future. Namely, IP rights give a strong signal to investors of the seriousness of the SME, that they have taken steps to protect their assets and that they believe in their innovative or creative product without relying on other companies' IP rights unless they are authorized by such other companies<sup>91</sup>.

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<sup>89</sup> See note 73, p. 8.

<sup>90</sup> 'Chapter 4: The Contribution of Industrial Property to the Transfer and Dissemination of Technology', in World Intellectual Property Organization / WIPO, Introduction to Intellectual Property: Theory and Practice, 2nd edition, 2017, p. 67 - 120

<sup>91</sup> *Ibid.*

In effect, a study of the US market showed that start-ups with pending patent applications could increase the funded amount invested by 630,000 USD<sup>92</sup>. This clearly shows the strong signal IP assets represent for Venture Capitalists.

The Belgian Venture Capital and Private Equity Association (BVA) was founded in 1986 as a professional association representing the VC and private equity community in Belgium. In 2012, Belgium was marking a small 0.025% of its GDP that was used as a Venture Capital Investment, while the worldwide leaders, Israel and the US, were marking 0.35% and 0.18% respectively<sup>93</sup>.

### 2.4.3. Strategic Alliances

Collaboration or strategic alliance is an agreement to share resources, such as expertise, goodwill, and capital, to increase the performance of both parties. They present a form of a cooperative strategy whereby firms combine resources and capabilities to achieve mutual goals.

### 2.4.4. Crowdfunding

Crowdfunding is a way to raise money from large groups of people pooling together small individual investments to provide the capital needed to get a company or project off the ground. Individuals, charities or companies can create a campaign for specific causes and anyone can contribute<sup>94</sup>.

SMEs may therefore use crowdfunding to raise capital efficiently for their venture, through a large group of investors. Moreover, in business, crowdfunding is mostly associated with start-ups, angel investments, and transactions outside of the traditional financial institutions<sup>95</sup>.

Nevertheless, involving one's IP in a crowdfunding project may represent some risks for those IP assets, as crowdfunding involves wide and rapid disclosure of information. It therefore requires a proper protection of those assets prior to their use in any crowdfunding campaign, to avoid any unforeseen effects on their value<sup>96</sup>.

## 2.5. IP Insurance

### 2.5.1. An Introduction to IP Insurance

IP insurance is not a long-standing practice, but it has a series of evident and less-evident benefits. It is not only a valuable instrument to evaluate the IP assets, but it can also provide the funds necessary to withstand infringement litigation, both as plaintiff and defendant and, in ensuring that no investments will be rerouted to litigation costs, it can attract investments<sup>97</sup>. Furthermore, also because of its effects as a risk mitigator, it can significantly boost banking confidence in adding further weight to IP and intangible assets in the lending decision<sup>98</sup>.

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<sup>92</sup> OECD, „Chapter 9 – IP-based financing of innovative firms“ in *Enquiries into IP's Economic Impact*, 2015, p. 462.

<sup>93</sup> Ibid.

<sup>94</sup> S. KURANI, „What is crowdfunding and how does it work ?“, *Republic*, available at : [What is crowdfunding and how does it work? – Republic](#)

<sup>95</sup> Ibid.

<sup>96</sup> For more information, see this comprehensive article : JA Kemp LLP, „UK: Protecting your IP when crowdfunding“, *Mondaq*, 2021, available at : [Protecting Your IP When Crowdfunding - Intellectual Property - UK \(mondaq.com\)](#)

<sup>97</sup> G. B. HALT, Jr. et al., *Intellectual Property in Consumer Electronics, Software and Technology Startups*, DOI: 10.1007/978-1-4614-7912-3\_13, ÓSpringer Science+Business Media New York 2014 p 158

<sup>98</sup> M. BRASSELL, K. KING *Banking on IP? The role of Intellectual Property and intangible assets in facilitating business finance*, the Intellectual Property Office (UK IPO) 2013, p. 18

In particular, in relation to the support given by IP insurance to bank lending, the firm Aon envisions that where IP is used as collateral, the role of the insurer could be slightly different than in other scenarios. Instead of ensuring the value of the IP, the insurer would offer a guarantee to the bank to secure a fraction of their debt in the event of default. The insurer would then take ownership of the IP and sell it to diminish the loss<sup>99</sup>.

Despite the multiple advantages related to IP insurance, e.g. for the banks to insure themselves against the risk related to IP-backed lending, there is still a widespread lack of experience and knowledge in relation to insuring IP assets and other intangibles<sup>100</sup>. The current market for IP insurance is very limited and its costs can be very high: with the growing interest in the topic and understanding of its benefits, there is space for a positive change in the coming years.

## 2.5.2. Applicable Insurance Policies

These are the basic policies available for intellectual property:

- 1 The IP value insurance covers direct loss and is prompted by legal claims against the IP causing loss of revenue or value. This type of insurance is usually linked with IP-rich products' future revenue streams, licensing revenues, royalties, valuation of IP assets and portfolios, R&D expenses, and financial arrangements involving IP like IP loans, securitization, monetization, and investments in IP-intensive businesses.
- 2 The IP Infringement/Liability insurance is the most common. It ensures the insured from infringement claims against and the latter's ownership rights in the IP. It also ensures the indemnification of other parties, such as customers and distributors, against infringement allegations and against damages following a judicial decision or settlement: however, some policies do not include damage awards. It is, therefore, a typically defensive insurance<sup>101</sup>.
- 3 The IP Enforcement coverage indemnifies for the legal costs incurred in enforcing and/or protecting the IP rights of the insured. It covers issued related to patents and patent applications, registered, and filed trademarks, registered and non-registered copyrights, as well as trade secrets. It is designed to aid IP owners with the enforcement of their IP rights against alleged infringements<sup>102</sup>.
- 4 The IP representations and warranties infringement liability insurance is usually associated with mergers and acquisitions, or a purchase agreement and it guarantees the validity of the involved IP. It protects against infringement/ownership liability, and it includes the reimbursement of defense and/loss expenses arising from decisions and settlements<sup>103</sup>.

However, securing coverage is a hard task in a series of circumstances. First, the insurers will not be willing to provide coverage in case of existing allegations of IP infringement brought against the IP holder (including verbal warnings and cease-and-desist communications) and, in all circumstances, the insurance will not include past litigations. It is also a common practice for the IP insurance to have an exclusionary period after the start of the policy during which infringement actions are not covered<sup>104</sup>.

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<sup>99</sup> M. BRASSELL, K. KING *Banking on IP? The role of Intellectual Property and intangible assets in facilitating business finance*, the Intellectual Property Office (UK IPO) 2013, p. 163

<sup>100</sup> "Ip based financing of Innovative Firms", *Enquiries into intellectual property economic impact* OECD 2015

<sup>101</sup> G. B. HALT, Jr. et al., *Intellectual Property in Consumer Electronics, Software and Technology Startups*, DOI: 10.1007/978-1-4614-7912-3\_13, ÓSpringer Science+Business Media New York 2014 p 12

<sup>102</sup> G. B. HALT, Jr. et al., *Intellectual Property in Consumer Electronics, Software and Technology Startups*, DOI: 10.1007/978-1-4614-7912-3\_13, ÓSpringer Science+Business Media New York, 2014, p. 12.

<sup>103</sup> *The Importance of Intellectual Property Valuation and Protection*, MarshMcLennan, [The Importance of Intellectual Property Valuation and Protection \(marsh.com\)](http://www.marsh.com/The-Importance-of-Intellectual-Property-Valuation-and-Protection)

<sup>104</sup> G. B. HALT, Jr. et al., *Intellectual Property in Consumer Electronics, Software and Technology Startups*, DOI: 10.1007/978-1-4614-7912-3\_13, ÓSpringer Science+Business Media New York 2014, p. 12.



## 3. Policies and Regulatory Framework

### 3.1. Regulatory IP Framework for SMEs to Access Funding

#### 3.1.1. IP as Movable (and Intangible) Property

##### A. Belgian Pledge Law Reform

Securities are granted most commonly on patents, trademarks, designs and models, while the most common form of security over intellectual property is a pledge: the latter can either be granted on a specific IP right, or the IP rights can be contained in a general business charge<sup>105</sup>.

Security in IP rights, difficult to grant under the old law, has received a more favorable legal basis in Belgium due to a major reform of its secured transaction law with the new Pledge Act, in force since 1 January 2018. The legislator has pursued a functional approach, yet a variety of security rights are still existing, with their own rules (e.g. retention of title, termination with proprietary effect, seller's lien, fiduciary transfer)<sup>106</sup>.

The new Pledge Act creates more security as to the validity of such security rights, including unregistered IP rights, by expressly providing the right to grant pledges over IP rights. Disposition is no longer a validity requirement, but one potential way of giving a proprietary effect: this effect can now also be achieved by registering the right of pledge in the Belgian register for pledges on movables (excluding pledging rights of performance, according to Article 20).

Another difference from the previous framework relates to the pledge of an enterprise: under the new Pledge Act, there is no longer a specific regime for pledging a business or enterprise and a pledge can refer either to a single asset or a whole category. Therefore, when a pledge of a business is granted, it now also covers IP rights, unless there is an agreement to the contrary. When a business is pledged under the new Pledge Act, in case of conflicting rights in certain assets of the business, the conflict has to be solved for each asset individually and, on the other hand, the pledgor maintains the authority to dispose of the assets in the ordinary course of business.

Art. 7 VI, however, states that the Pledge Act applies to IP rights only if not incompatible with rules specifically regulating the latter, without giving any indication as to how this compatibility should be determined: this general rule should be kept into account in creating a right of pledge of an IP right<sup>107</sup>.

In the creation of a right of pledge, Belgian law requires – like for any transfer of property or creation of a proprietary right on the basis of a contract – (i) a valid underlying (contractual) obligation; (ii) the consent of the grantor ; and (iii) the authority of the latter to dispose of the IP right in question.

As for the formation and validity of the underlying contract of pledge, the Pledge Act imposes formal requirements, with some slight differences between consumer and non-consumers:

- the contract of the pledge can only be proven in writing and the writing must indicate the encumbered assets (a general description is sufficient), the secured debts, and the ceiling

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<sup>105</sup> D. VAN DER MOSEN, A.P. ANDRE-DUMONT, *Lending and taking security in Belgium: overview*, Buyle Legal, Thomson Reuters 2016 available at [uk.practicallaw.thomsonreuters.com](http://uk.practicallaw.thomsonreuters.com)

<sup>106</sup> E.M KIENINGER, *Security Rights in Intellectual Property: General Report*, "Security Rights in Intellectual Property", Springer Nature Switzerland AG 2020, p. 16.

<sup>107</sup> M.E. STORME, J. MALEKZADEM, *Security Rights in Intellectual Property in Belgium*, "Security Rights in Intellectual Property", Springer Nature Switzerland AG 2020, pp 126-127.

or maximum amount for which the assets are encumbered. This general rule does not apply when there is the dispossession of the asset;

- the formal requirements for any pledge granted by a consumer apply also to pledges over IP rights: the pledge agreement must be in document form and signed by both parties and it must indicate the value of the assets pledged (not required for pledges by a non-consumer)<sup>108</sup>.

It is also possible to include future IP rights and to stipulate a pledge securing all present and future debts towards the pledgee.

This new legislative framework is a big step in the accessibility of securities concerning IP rights and makes the Belgian system particularly future-forward.

## B. Importance of Registration and Formalities

As mentioned before, the Pledge Act provides two ways to make a right of pledge effective towards third parties, e.g. in insolvency proceedings: dispossession or registration in the pledge register. However, it does not abolish the possibility to make a pledge in registered IP rights effective through registration in the specific register, thus creating a double regime and increasing the importance of registration procedures.

In relation to the specific IP registers, the right of pledge must be in writing and be notified: (i) For Belgian patents to the Belgian National Patent Office, (ii.) For Benelux trademarks to the Benelux Office for Intellectual Property. (iii.) For Benelux models and designs to the Benelux Office for Intellectual Property.

A specific case refers to IP rights with no specific register in Belgium, copyright in particular. As it is doubtful that copyright can be pledged through dispossession, registration in the national online pledge register according to the new Pledge Act could be the only safe method for making the pledge effective<sup>109</sup>.

While the registration of a right of pledge does not protect the pledgee if the pledgor lacks authority, and older rights will thus prevail, it can protect the pledgee against the later acquisition of rights by third parties who are professional acquirers. On the contrary, non-professional acquirers have no duty to consult the pledge register<sup>110</sup>.

In relation to the Pledge Register, any registration is effective for 10 years but can be renewed for another 10 years and it can be made directly by the secured creditor, who has to notify the debtor. It requires the existence of a pledge agreement - making advance filing impossible - but the agreement itself does not have to be registered.

The information requested for the registration of a right of the pledge are the following:

- data on the identity of pledgor and pledgee
- encumbered assets
- secured debts
- ceiling

The registration, renewal, modification, deregistration, subordination and transfer of security interests in moveable assets can only be executed by the pledgee, the security agent, or attorney-in-fact. In order to register the relevant security interest, a Belgian eID card must be used and, otherwise, an agent may act as representative.

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<sup>108</sup> Ibid., pp 127-128.

<sup>109</sup> Ibid., p. 129.

<sup>110</sup> Ibid., p. 131.

### 3.1.2. SMEs-Friendly IP Policies

#### A. Public Funding Initiatives

The EU Level:

Belgian SMEs have access to funds and benefits established at the EU level. An initiative to highlight is the Ideas Powered for business SME Fund<sup>111</sup>, a €20 million grant scheme created to support European SMEs in accessing their IP rights. The supporting benefits offered are:

- a 75% reimbursement of IP pre-diagnostic services (IP Scan). IP experts identify the value of the SMEs IP assets, examine the business model, products/services and growth plans to create an effective IP strategy. This service includes all IP rights, including the unregistered ones, and terminates with a report on the IP rights of the SME and recommendations on how to manage and protect those IP rights in the future.
- a 50% reimbursement on trademark and design basic application fees.

Each SME can be reimbursed up to a cap of 1,500 EUR.

To evaluate the eligibility for this fund as a European SME, the criteria of the EU recommendation 2003/361 have to be kept into consideration in relation to the main factors of the staff headcount and either the turnover or the balance sheet total. The following scheme<sup>112</sup> applies to individual enterprises:

Company category	Staff headcount	Turnover	or	Balance sheet total
Medium-sized	< 250	≤ € 50 m		≤ € 43 m
Small	< 50	≤ € 10 m		≤ € 10 m
Micro	< 10	≤ € 2 m		≤ € 2 m

For SMEs willing to engage in European R&D, the Horizon 2020 Programme is also a very important funding tool.

Horizon 2020 is the biggest EU Research and Innovation program ever with nearly €80 billion of funding available over 7 years (2014 to 2020), in addition to the private investment that this money will attract. It promises more breakthroughs, discoveries and world-firsts by taking great ideas from the lab to the market<sup>113</sup>.

Belgium as a whole benefits from 10 regional programs stemming from the EU level. In total, the countries received 2.7 billion euros from European Structural & Investments Funds (ESIF) between 2014 and 2020, with a total budget of 6 billion. It has allocated the most funding to the competitiveness and growth of Belgian SMEs, with a total budget of 1.2 billion allocated globally<sup>114</sup>.

Belgian level:

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<sup>111</sup> For more information, see <https://euipo.europa.eu/ohimportal/en/online-services/sme-fund>.

<sup>112</sup> For more information, [https://ec.europa.eu/growth/smes/sme-definition\\_en](https://ec.europa.eu/growth/smes/sme-definition_en)

<sup>113</sup> European Commission, „What is Horizon 2020?“ available at: [What is Horizon 2020? | Horizon 2020 \(europa.eu\)](https://ec.europa.eu/horizon2020/what-is-horizon-2020_en)

<sup>114</sup> European Commission, European Structural and Investment Funds, Country data for Belgium, available at: <https://cohesiondata.ec.europa.eu/countries/BE#>

Each Belgian Region provides different financial grants, including to SMEs, and some of them include, under specific conditions, services related to IP. The following scheme provides an intuitive overview of these initiatives, applicable to Belgian SMEs who want to capitalize on their IP<sup>115</sup>.

	Support provided	Available for	Amount
<b>BRUSSELS-CAPITAL</b>			
PATENT FILING AIDS	Financial intervention in patent procurement procedures, including official fees	SME with innovative activities in the Brussels-Capital Region	50% of the application and procedure cost.
INNOVATION VOUCHERS	Financial intervention for services supporting the SME's innovation strategy	SME's with innovative activities in the Brussels-Capital Region	Max of €10,000 per year and max of 75% of the expenses
CONSULTANCY PREMIUM - Legal analysis	Financial intervention in legal consultancy	SMEs located in the Brussels-Capital Region	Basic level of 40%, up to 60% in specific cases. Max €10.000 per year
SUBSIDIES FOR IP ADVICE on trademark filing, registration and certification abroad	Subsidies for part of the consultancy costs for this procedures abroad	SMEs located in the Brussels-Capital Region	50% of the fees with a max of €10.000 per year
<b>FLANDERS</b>			
KMO PORTEFEUILLE: IP Advice	Subsidies for advice on IP	SMEs located in Flanders	
KMO PORTEFEUILLE: IP Trainings	Subsidies for IP trainings and workshops	SMEs located in Flanders	Small enterprises: Support of 30% with a max of € 7.500 per year Medium sized enterprises: Support of 20% with a max of € 7.500 per year
<b>WALLONIA</b>			
IP VOUCHERS	Subsidies for services to strengthen the innovation strategy of the SME	SMEs with innovative activities in Wallonia	Support of 50% with a max of €45.000 for 3 years
PATENT FILING SUPPORT	Subsidies for costs related to patenting procedures	SMEs with innovative activities in Wallonia	40% to 50% of First filing 50% Territorial extension 50% Opposition (PATOP)
VOUCHERS FOR DIAGNOSTIC OR GROWTH SUPPORT	Subsidies for services supporting growth and development	SMEs with business activities in Wallonia	Support of 50% with a max of €25.000 for 3 years

## B. IP Vouchers

IP Vouchers are an effective and intuitive support mechanism for SMEs and they are created to encourage this category of enterprises in the capitalization and understanding of their IP potential, as well as to diminish the gap with the giants of the same markets.

Here is some additional information on these benefits at the Belgian Level:

*Brussels-Capital Region's Innovation Vouchers* - This funding applies to technical support in a research center and allows easier access to expert assessment of an innovative project. To be eligible, the enterprise must develop all or part of its activities in the Brussels-Capital Region, to the economic, employment, or sustainable development on which the project would have a positive impact.

<sup>115</sup> C. LEFEBVRE, *SUBSIDIES: Each Belgian Region has different grants for entrepreneurs and SMEs to foster economic developments*, Gevers, available at: <https://www.gevers.eu/en/Q5deg89VI/subsidies--each-belgian-region-has-different-grants-for.php>, last update 01/09/2020.

The application for the voucher must be filled in together with the accredited research center and the report shall be completed in 15 months<sup>116</sup>.

*Walloon Region's IP Vouchers* - These Intellectual Property Vouchers allow SMEs to access the support of IP specialists, who can: analyze the invention and determine whether it is patentable, or whether there is a risk that someone will oppose it; provide an overview of all the existing patents and documents relating to the field of the invention (state of the art evaluation), which can then lead to a "patent mapping" and more strategic decision-making; set up a technology watch, adapted to the specific needs of the SME.

These vouchers are only available to SMEs registered as a business enterprise in the BCE<sup>117</sup>.

*Walloon Region's Voucher for Diagnosis of Business Growth and Development* - Particularly indicated for enterprises that want to grow and/or diversify, this voucher allows easier access to specialists to develop a diagnosis of the current situation and of possible needs, either through a general analysis from different perspectives or a specialised auditing process. The final stage is the proposal of an action plan by the consultant, which can then be approved by the SME or not: in the first alternative, the support includes the refinement of the plan and assistance throughout its implementation.

SMEs with business activities in Wallonia can access this voucher<sup>118</sup>.

*Walloon Region's Voucher for Support for Business Growth and Development* - This voucher is particularly indicated for enterprises that are growing fast and it gives support in securing the assistance of specialists to improve the business methods, including financial aspects, production and logistics, quality management, safety standards, HR, communication, investment policy, distribution or licensing, transfer of technology, and so on. This service can also cover commercial aspects, such as marketing and commercial differentiation.

SMEs with business activities in Wallonia can access this voucher<sup>119</sup>.

For SMEs and professionals with headquarters in *Flanders*, while there are no IP Vouchers available, there are a series of subsidies dedicated to supporting growth and innovation<sup>120</sup>. Of particular interest about IP, is the *SME Portfolio*: a web application through which enterprises can obtain subsidies for training, advice, technology watch and internationalization. This aid is only for enterprises that fit the definition and that have an acceptable legal form and main activity on the basis of the NACF Revenue E Code: NGOs are excluded. For trainings, the level of subsidy can amount to 50% of the eligible costs - up to 2,500 EUR per year - and the minimum project amount must be 100 EUR. The eligible costs include fees, training materials and meals.

### C. IP Bonus

The measure called "Innovation Bonus" consists of the complete exemption of the bonus granted and paid by an employer to its creative workers to reward the expression of a new idea implemented within the company.

The company does not pay social security contributions on this bonus. The worker does not pay social security contributions and is not taxed on this bonus. This bonus is therefore 100% net.

The conditions to benefit from it are always the same<sup>121</sup> but the number of employees who may benefit from it varies depending on the number of workers in the company.

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<sup>116</sup> For more information, <https://innoviris.brussels/innovation-vouchers>

<sup>117</sup> For more information, see <https://www.cheques-entreprises.be/cheques/cheque-propriete-intellectuelle>

<sup>118</sup> For more information, see <https://www.cheques-entreprises.be/cheques/diagnostic-croissance-et-developpement-dentreprise>

<sup>119</sup> For more information, <https://www.cheques-entreprises.be/cheques/accompagnement-croissance-et-developpement-dentreprise>

<sup>120</sup> For more information, [Subsidies for entrepreneurs | Agentschap Innoveren en Ondernemen \(vlaio.be\)](#)

<sup>121</sup> For more information, see [Prime d'innovation | SPF Economie \(fgov.be\)](#)

## 3.2. Financial Regulations on the Use of IP as a Financial tool

### 3.2.1. Specific Financial Regulations for SMEs

On 9 July 2009, the International Accounting Standards Board issued the first set of international accounting requirements developed specifically for SMEs: the International Financial Reporting Standards (IFRS) for SMEs. It has been prepared on IFRS foundations but is a stand-alone product that is separate from the full set of requirements. The IFRS for SMEs has simplifications that reflect the needs of users of SMEs' financial statements and cost-benefit considerations<sup>122</sup>.

In 2015, the G20 and the OECD developed the G20/OECD High-Level Principles on SME Financing<sup>123</sup>, which called for the enhancement of SMEs financial skills and strategic vision. A few years later, Belgium was offering the following non-financial support tools as part of its policy range for SME finance: (i) specific programs combining debt finance products and advisory services (Flanders region), (ii) coaching and mentoring provided together with loan guarantees by guarantee institutions, and (iii) web-based advisory services (Walloon region)<sup>124</sup>.

### 3.2.2. Intangible Assets and IP in Financial Statements

Financial statements are reports which illustrate the financial position of the entity for a specified period. They usually comprise the balance sheet, an income statement (or profit and loss statement), a cash flow statement, and a statement on the changes in equity. These reports provide investors, lenders, and other creditors (present and potential ones) with the information required to make decisions about buying, selling or holding equity or debt instruments, providing or settling loans or other forms of credit<sup>125</sup>.

As part of a financial statement, a balance sheet contains the elements directly related to the financial position of the company at issue. Namely, a balance sheet reports on a company's assets, liabilities, and equity at a given point in time. To be recognized and incorporated in the balance sheet, the items must satisfy the following criteria for recognition:

- any future economic benefit associated with the item will probably flow to or from the company and
- the item's cost or value can be measured with reliability.

Since an intangible asset is classified as an asset, it should appear in the balance sheet. While meeting these criteria in terms of incorporating tangible assets in the balance sheet is not problematic, it might be difficult for the SMEs to get recognition for investment in intangible assets, including IPR, even when they make up a significant part of the company valuation.

Considering the second criteria presented above, the intangible assets will most likely be listed on a balance sheet where such assets are gained as part of the acquisition of another business,

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<sup>122</sup> IFRS for Small and Medium-Sized Entities, IAS Plus, available [here](#).

<sup>123</sup> G20/OECD, *High-level principles on SME financing*, November 2015, available [here](#).

<sup>124</sup> Evolution and Trends in SME Finance Policies since the Global Financial Crisis, OECD, July 2020

<sup>125</sup> Conceptual Framework for Financial Reporting 2018, IAS Plus, accessed in July 2021, available [here](#).

or they were purchased as individual assets since the value of the asset in these situations can be precisely determined. However, the significant investments in internally generated IP will rarely appear on the company balance sheet<sup>126</sup>. This means that the balance sheet, and thus the financial statement itself, may not reflect the real value of the company and decrease the chances for said company to access funding.

### 3.3. Specific Tax Regimes for Innovation and SMEs

Innovation may be characterized beforehand as a “knowledge economy”<sup>127</sup>. It is deeply linked with a scientific approach, where ideas and projects need to be researched, invested in and properly funded and, lastly, appropriately protected for them to bring value to the company that capitalizes on it. Under this point of view, the financing of innovation comes as a preliminary stage for SMEs that launch an innovative project, and IPRs come at a later stage, where SMEs may protect and create value over their investment<sup>128</sup>. But both mechanisms are part of the same objective, namely perpetuating the value and market power of one’s company.

Innovation often requires initial funding, used to develop and research the material infrastructure or to produce the prototypes of the project. In Belgium, most SMEs have the choice to (i) rely on their own funding or (ii) to rely on external collaboration, from public and/or private institutions<sup>129</sup> to fund their innovation<sup>130</sup>.

In line with the European Commission Policy of Fostering Innovation, Belgium has been implementing legal rules that provide considerable incentives for companies to invest and register their Research & Development (hereafter “R&D”) programs and to register also the IP relating to innovation. In doing so, Belgium places itself as one of the most “generous” countries according to OECD standards<sup>131</sup>, which is one of the most comprehensive regimes to intensify R&D and innovation of Belgian SMEs<sup>132</sup>. Indeed, since 2007, Belgian companies may choose between a tax deduction and a tax credit for R&D investments to do so. Since 2008, they were also able to benefit from a tax deduction of 80% of their patent income. In 2016, this benefit was replaced by a deduction of up to 85% of their innovation income<sup>133</sup>.

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<sup>126</sup> Intellectual property, finance and economic development, WIPO Magazine, published in February 2016, available [here](#).

<sup>127</sup> Ayming Institute, *Le baromètre International de l’Innovation 2020*, p. 14.

<sup>128</sup> R. Hendrice, *Innovation support mechanisms – UCL presentation*, Deloitte, 2021, p. 48.

<sup>129</sup> As an example of public funding, the EU commission launched its IP Action 2020, which sets an emphasis on supporting encouraging SMEs to manage their IP assets more efficiently and improve their competitiveness by giving them an easier access to personalized and strategic IP advice via public funding programs. The Commission also announces concrete financial support for SMEs jointly with the European Intellectual Property Office in the form of partial reimbursements (up to a maximum amount of EUR 1 500 per SME) for trademark and design registrations and, in certain Member States, for IP pre-diagnostic service (“IP scan”) ; See Elvinger Hoss, *European Commission’s Action Plan on IP*, 2021, available here [European Commission’s Action Plan on Intellectual Property | Elvinger Hoss](#), and the website of the Commission, here : [IP vouchers for SMEs: first window closes on 31 January \(europa.eu\)](#) for more information.

<sup>130</sup> Ayming Institute, *Le baromètre International de l’Innovation 2020*, p. 16.

<sup>131</sup> According to an OECD report, 2019 edition, the Belgian R&D tax package is ranked third worldwide in the ranking of attractive tax regimes for SMEs, see SPF Finance, *Incitants Fiscaux pour la recherche et développement et l’innovation*, 2020, p.3., available here: [704-brochure-RD-TaxIncentives-2020-fr.pdf \(belgium.be\)](#)

<sup>132</sup> Bureau Fédéral du Plan, *Tax incentives for business R&D in Belgium - Third evaluation*, Bureau fédéral du Plan, 2019, Working Paper, p. 4-19.

<sup>133</sup> Ibid.

Particularly, the Belgian legislator included in the Belgian Income Tax Code of 1992 (hereinafter “ITC 92” or “ITC”) different provisions that provide fiscal and financial incentives for SMEs to invest and protect their innovation practices<sup>134</sup>.

The goal of those incentives is to foster innovation, attract and maintain R&D profiles in Belgium and encourage investment in this field to guarantee a certain level of excellence in entrepreneurship and innovative creations.

The ITC distinguishes different mechanisms, which will be described in the sections below. We can divide them into the following categories: Innovation Income Deduction (Hereinafter “IID”) or “Innovation Box”, which aims to replace the current Patent Income Deduction (hereinafter “PID”) or “Patent Box”, Wage Tax Incentives, R&D tax credit – or deductions.

### 3.3.1. Innovation Box – the Tax Preference regime relating to IP

Article 205/1, subsection IIIbis of the Belgian ITC foresees the application of a specific fiscal regime relating to the interplay of IPRs in the field of innovation, that proposes a fiscal deduction for the amount generated by specific and limited types of IPRs owned by Belgian companies.

The Innovation Box Regime requires different conditions to be met : (i) the company must be active in the field of innovation, and (ii) it concerns specific incomes stemming from specific IP rights, as follows :

- Qualifying IP Rights :
  - Patents;
  - Supplementary Protection Certificates ;
  - Plant Variety rights<sup>135</sup>;
  - Orphan drugs<sup>136</sup>;
  - Data or market exclusivity granted by a public body<sup>137</sup>;
  - Computer programs protected by copyright, upgraded software included<sup>138</sup>.

An important limitation is that most of the commercial IPR such as know-how, trade secrets, trademarks, tradenames, brands, designs and models are not qualifying IP rights. Therefore, it seems that the Innovation Box Regime still holds the scars of the powerful lobby of Food & Drugs in Belgium. Practically, the regime would become even more popular if its scope was enlarged towards other, industrial, types of IP rights, which are often met in the Belgian landscape. Nevertheless, SMEs which exercise in these fields and should choose to conduct an innovative project may be able to benefit from this legal fiscal deduction for specific types of incomes, i.e. the ones relating to the value they bring from the IP rights stemming from their innovative project.

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<sup>134</sup> R. Hendrice, *Innovation support mechanisms – UCL presentation*, Deloitte, 2021, p. 48.

<sup>135</sup> Filed as of 1 July 2016 or acquired after 30 June 2016.

<sup>136</sup> Filed as of 1 July 2016 or acquired after 30 June 2016 and limited to the first 10 years of registration in the EU register of Orphan drugs.

<sup>137</sup> If granted after 30 June 2016.

<sup>138</sup> Not for incomes generated before the 1<sup>st</sup> July 2016.



- Qualifying Incomes :

License fees;

IP income embedded in sales product or services;

IP income embedded in the production process;

Compensation for damages of IP rights infringements;

Capital gains.

- Qualifying Expenditures:

Research and development expenses directly related to intellectual property rights;

If the company justifies these criteria, it may be eligible to receive additional government support. The company shall start by assessing the amount stemming from each IPR it owns, and it may then deduce 80-85% of that amount from its tax base.

- But What about the Old Patent Box Regime?

The Innovation Income Deduction is intended to replace the Patent Income Deduction (PID, also known as the Patent Box) and came into force on 1 July 2016. As of today, the two systems coexist: for patents applied for or obtained before 30 June 2016, you can still claim the Patent Box until 30 June 2021, if these patents had not yet been commercialized before 1 January 2007. For these patents, you can also opt immediately for the Innovation Box<sup>139</sup>.

Since 1 July 2021, the Patent Box is no longer available and only the Innovation Box remains<sup>140</sup>.

### 3.3.2. Wage Tax Credit

The R&D Wage Tax Credit has been implemented in Article 275 ITC to the benefit of the employers of R&D profiles in Belgian companies. Typically, it is characterized as a partial exemption professional withholding tax and applies to employees performing R&D related activities and holding a qualifying degree<sup>141</sup>.

Concretely, it dispenses up to an 80% exemption of withholding tax for the employers, and up to a 25% of salary cost reduction<sup>142</sup>.

The Tax Wage Reduction is available under the following conditions: (i) the employer should be able to demonstrate the R&D nature of the activities of its employees and the time spent on R&D projects/within an R&D program; (ii) the tax incentive can only be applied from the moment the R&D project or program is notified to Belspo;

Specific rules apply for Public R&D centers, universities, young innovative companies and commercial companies partnering with public R&D centers and/or universities.

It can be combined with R&D tax credit/investment deduction and the Innovation box deduction.

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<sup>139</sup> Ayming, *Déduction pour Revenus d'Innovation*, 2021, p.2.

<sup>140</sup> Ibid.

<sup>141</sup> R. Hendrice, *Innovation support mechanisms – UCL presentation*, Deloitte, 2021, p. 48.

<sup>142</sup> Ibid.

### 3.3.3. R&D Tax Credit

Articles 68 and 69 of the ITC 92 provide for a complementary fiscal regime concerning R&D programs. Under this regime, companies that invest in R&D can benefit from an R&D investment deduction or an R&D tax credit.

The R&D investment deduction/tax credit applies to R&D investments capitalized in Belgium's generally accepted accounting principles (namely with the distinction between the tangible/intangible fixed assets);

It offers an option between a one-shot deduction (3.38€ per 100€ invested) or a spread R&D investment deduction (5.13€ per 100€ invested spread out over the period needed to amortize the investment);

Companies wishing to benefit from the regime will have to respect the following requirement: they must obtain a regional certificate confirming the absence of any negative impact on the environment of the new products or prospective technologies resulting out of the R&D activities.

### 3.3.4. Copyright Fiscal Deduction

Introduced in 2008<sup>143</sup>, this regime allows creators of an artistic or literary work, who assign their copyright and neighbouring rights to a third party to benefit from a separate tax rate of 15% on the income obtained in return. It only applies to authors exercising as physical persons. The law also includes the different types of Belgian associations.

The regime applies to income coming from the assignment or licensing of copyright and neighbouring rights. Indeed, such individual income is now referred to as an income of movable property from a tax perspective.

This regime allows part of the income to be taxed at a favourable withholding tax rate of 15% insofar as it does not exceed a certain indexed threshold (62,090 euros for the exercise 2020), after deduction of flat-rate or actual professional expenses.

Above this limit, royalties are taxed as professional income (at the normal progressive tax rate of a maximum of 50%), when the tax authorities prove that the income was acquired in the course of professional activity. If this is not the case, the qualification of "movable income" continues to apply<sup>144</sup>. Therefore, the first thing SMEs will have to check to benefit from it is whether their activities generate creations and whether these can be considered as 'works' protected by copyright.

This regime does resemble other fiscal incentives such as those described above, but it has a larger scope. Indeed, it is not limited to a specific field – i.e. to the artistic professions -, which implies that other professions can also benefit from it. This has led more and more professionals outside of the classical artistic fields – especially in the IT and digital fields – to deduct their income based on this regime.

The direct consequence of this phenomenon resulted in a lively debate at the Belgian Parliament with the aim to limit the abusive use of the regime by diminishing its scope. The government is discussing ways to frame its scope to artistic professions only but it is not yet enacted<sup>145</sup>.

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<sup>143</sup> Voyez la Loi du 16 Juillet modifiant le codes des impôts sur le revenu 1992 et organisant une fiscalité forfaitaire des droits d'auteur et des droits voisins.

<sup>144</sup> Wolters Kluwer, *Régime fiscal des droits d'auteurs*, 2021, available at : [Régime fiscal des droits d'auteur | Wolters Kluwer](#)

<sup>145</sup> S. BURON, *Fiscalité : il y a-t-il des abus sur les droits d'auteurs ?* Trends Tendence, Juin 2021, p.2.

## 4. Conclusion: Challenges of Using IP Assets for SMEs to Access Funding and Recommendations

### 4.1. Challenges

Belgium is currently paving the way for a better practice towards the use of IP as access to funding for SMEs. As it has been underlined in this report, Belgium has indeed updated its regulatory framework in this sense, notably by amending the Belgian Pledge Act, or by proposing fiscal incentives for innovation and R&D, which have been classified amongst the most modern in the world currently.

Yet, the day-to-day practice still is at a very early stage. The practitioners and professionals in the field still are very unfamiliar with many of the valuation methods, and do not yet offer sufficient financial packages or practical mechanisms for the SMEs to actually benefit from it. Indeed, many institutions in the banking and finance or insurance sector, or even private companies are still struggling to consider IP for what it should become with this purpose in mind : a clear, direct asset that could be easily leveraged by SMEs to create value, and unlock funding accordingly by using their intangible assets as a security.

As of the moment, we may conclude that IP assets and intangible assets are only properly valued in certain situations, that are often linked with the global value and assets of a company ; in this sense, IP still represents only *indirect leverage* towards the valuation of one's company.

Indeed, it is still difficult to argue that IP may be considered as sole collateral for Belgian SMEs, for different reasons that may be summarized as follows: (i) IP is often regarded as having low to no capital weighting for the lending institutions; (ii) IP is difficult to value and even harder to monetize when necessary and often requires a specific, case-by-case analysis for proper valuation depending on the method used; (iii) IP is still often used as a top-up, i.e. as a component added to the lending package rather than as the primary asset.

It is nevertheless feasible to consider IP as a funding opportunity for SMEs, and it is, therefore, crucial it remains considered by Belgian SMEs in the larger framework of their quest for funding. A proper IP strategy and management has the potential to unlock funding opportunities towards better innovations programs or better valuation of one's market value.

### 4.2. Recommendations

Having in mind all stated above, we would recommend the following:

1. **Creating confidence in the ownership and quality of the IP**, to convince the banks to consider the SME for funding. Training and professional advice on how to calculate and properly present (expected) cash flow, how to make proper expectations about the time and volume of monetizing the assets and similar, should be taken into account and provided for SMEs.
2. **Creating a specific financial category in the financial reporting of one's company where IP assets could be included, accounted for and properly based upon for funding.** As presented in section 3.2.2. of this report, banks will always consult the financial statements when deciding whether or not to provide a loan or other forms of credit to SMEs. If IP assets would be recognized and incorporated in these documents, banks could easier make a decision and assess the interest rate, while SMEs' chances of funding would be increased. Additionally, it would be recommended to create a separate tab in financial statements where the volume and costs of investment in internally generated IP will be

presented. This information would be used as a strong signal for banks that the company at issue take its IP assets for serious and, based on this information, it would be easier to determine the value of such IP assets.

3. **The new Belgian Pledge Act should specify whether the pledge over IP assets needs to be registered both with the Pledge registry and the IP-specific registry,** or registration with the first one would suffice. For the sake of transparency and the reliability of the registers, we would recommend recording the pledge in both registries.
4. **IP financing could be facilitated through the emergence of better infrastructure of their marketplaces.** In this sense, the development of the Belgian Pledge Regime is already going in the right direction as it is likely to transform IP and intangibles as an asset class that may be traded. It allows for IP and intangibles to become identified, certified, and to be more freely licensed, bought and sold. Nevertheless, the systems available to register and track financial interests will need to be improved, especially considering the two registration approach available, namely the Pledge register or the classical IP rights registration regime. This will require the cooperation of official registries and the establishment of administrative protocols.
5. **Asset-based financing techniques should be adapted for IP and intangibles.** The greater emphasis on assets needs to be extended to include IP in lending mechanisms. Alongside mainstream lending, asset-based finance and alternative financing methods should therefore be targeted for IP-backed finance interventions.
6. **Improving the guarantees for the lending institutions by encouraging risk mitigation strategies.** Alongside certain specific guarantees, which could take the form of the public scheme that could work as a safety net for the banks, the creation of appropriate insurance policies to prevent unforeseen events could greatly increase banking confidence in adding further weight to IP and intangibles within the lending decision.



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