

Video Game Finance: Leveraging Value of IP Assets

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Access to Capital & Intellectual Property

- Video game companies primarily use traditional debt financing methods to source capital
- Intellectual Property are the principle assets of video game companies
- Innovative structured finance transactions unlock the full value of IP assets
- Several alternative financing methods to traditional borrowing programs should be considered

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Traditional Debt Financing

- Typical loan transactions do not meet the funding needs of most video game companies
 - Lenders are unable to adequately value IP assets
 - Interest rates are too high
 - Advance rates are too low
 - Loan covenants can be burdensome
 - Many lenders want an equity kicker

Structured Finance & Securitization Funding

- Structured Finance Transaction – Focuses on assets that create cash flow
- Securitization – Sale of securities backed by assets that create cash flow (asset backed securities – ABS transaction)
- Advantages
 - Lower interest rates
 - Higher advance rates, especially for IP assets
 - Loan covenants tend to be less burdensome
 - An equity kicker is generally not required

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Structured Finance Characteristics

- Structured finance eliminates bankruptcy risk by isolating IP assets in a special purpose subsidiary
- Repayment of debt flows directly from cash flow of transferred IP assets
- Lower interest rates due to investment grade rating of transaction

Potential Applications of Structured Finance/Securitization for Game Companies

- Asset-backed commercial paper facilities
- Securitization of royalties, license fees and related game revenue
- Slate financing of new productions

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Asset Backed Commercial Paper Facilities

- Segregate IP assets that produce cash flow (royalties, license fees and other game revenue)
- Pledge only IP assets to a commercial paper conduit facility to support a borrowing from the CP facility
- CP facility is a program sponsored by a large investment bank or commercial bank funded by the sale of commercial paper

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Asset Backed Commercial Paper Facilities

- Borrowing can be term or revolving
- New IP related assets can be pledged as created to increase borrowing capacity
- Third party may insure value of IP assets
- Interest rate generally tied to rate paid on CP issued by CP provider – usually a LIBOR based rate

Securitization of Royalties

- Transfer IP assets (royalties, license fees and other related game revenue) to an SPE
- SPE sells notes to investors
- Cash flows from transferred assets service notes with excess cash flows ultimately released to SPE
- Third party may insure value of IP assets or otherwise guaranty cash flow will be sufficient to service notes

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Securitization of Royalties

- When notes repaid, IP assets and cash flow revert to developer
- Interest rates generally tied to margin over equivalent LIBOR
- ABS transaction frequently used to pay-off a CP facility

Slate Financings of New Productions

- **Financing facility established to fund new productions based upon company's track record**
- **SPE sells notes to investors based upon anticipated future cash flow, deposits cash in blocked account**
- **Transfer IP assets (royalties, license fees and other related revenue for productions) as created to SPE**

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Slate Financings of New Productions

- Cash drawn from blocked account to finance an agreed percentage of new production costs
- Cash flows from new productions devoted to servicing notes with excess cash flows ultimately released to SPE
- Third party may insure value of IP assets or otherwise guaranty cash flow will be sufficient to service notes

Making Structured Finance/ Securitization Work

- One size does not fit all
- Be imaginative – be creative
- Work closely with investment bankers, accountants, investors and attorneys with structured finance/securitization experience
- It takes time, especially the first time
- But, when it works, it's worth the effort

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Thank you

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