Accurate IP valuation in multiple environments

*The IP rights belonging to a well-managed, buoyant company will be worth a lot more than those owned by a business on the verge of bankruptcy. The key to a successful IP valuation therefore is to understand the reasons why it is being done in the first place. By **Weston Anson** and **Daryl Martin***

The question is often asked: why value IP? Why value a company's trademarks, patents or other intellectual property? What are the driving forces that make trademarks and other IP increasingly important and increasingly valuable? These are all good questions. There are a number of underlying trends that are driving the need for valuation of IP assets. There are trends that are specifically related to intellectual property as a topic, and there are market trends that specifically relate to the corporate environment.

Those reasons specifically related to IP include:

- Increasingly valuable IP assets used as a financing vehicle.
- Mergers and strategic alliances based on IP assets.
- Leveraging the full bundle of IP rights.
- Unused IP and IT assets as a source of working capital.
- Accurate valuation of IP and IT grows in importance.
- Global awareness of market value of IP/IT.

In addition, there are a number of reasons for valuation of rights that relate to the general corporate environment. These include:

- An increasingly competitive business environment.
- Pressure to maximise return from all assets, not just tangible assets.
- Expanded global marketing and branding.
- Multiple financial leverage alternatives from IP.
- Corporate reorganizations/bankruptcy focus on IP.

Bundling the assets

Traditionally, analysts have thought of intellectual property as discrete individual assets or pieces of property and, in particular, have adopted this approach when valuing trademarks. In other words, a single trademark is valued without regard to any other brand or marketing assets. We believe that the more appropriate way to value intellectual property is to look at bundles of intellectual assets.

There are anywhere from a dozen to 15 different bundles of intellectual property that might be found in a typical corporation. However, we have focused on the three primary ones in Table 1 (bundles of intellectual assets - see over). They are the marketing bundle, the technical bundle and the information technology (IT) bundle. The marketing bundle is the primary focus of our valuation discussion here. The marketing bundle is, of course, based on trademarks. However, a trademark does not travel in a vacuum - in fact, it rarely does in the real world of brands and branding. Instead, there are a number of other elements and assets within the marketing bundle. The primary thought to take away from this brief overview is that the most effective approach to trademark valuation, and the one that is most reflective of real-world trademark usage, is to identify and bundle all of the marketing-related assets and then value the bundle.

Valuation applications: context + time = value

In approaching a valuation project one must always consider the context in which the trademark or other IP is being valued. The value of a trademark or other brand assets can be vastly different in a bankruptcy scenario than in a going concern, or a sale of the trademark assets. In general, the bases for trademark valuation can be grouped into five areas:

- Bankruptcy/reorganisation

- Business transactions
- Loan securitisation
- Financial and tax purposes
- Litigation

In a bankruptcy or reorganisation of a corporation, value will certainly vary depending upon context and time. The value of a trademark in a reorganisation is much greater than it would be in an orderly disposition and that value, in turn, will be much greater than the value of the trademark should the company be liquidated.

Briefly stated, business transactions include sale, acquisition, merger, spin-off, licensing, joint venture or other business deals that make use of trademarks and other IP. Valuation in this environment is obviously more business driven, without the imperatives of bankruptcy and/or tax or other financial concerns. Frequently, market comparable transactions can be used to identify the value of a trademark in such an environment.

Trademarks and other valuable intellectual property are being used more and more as a financial lever. The process of borrowing money against a family of trademarks, patents or other IP is increasing in frequency and degree. Whether in a post-merger environment, or as security in the reorganisation of a company in Chapter 11, the trademark and IP portfolio can be used to securitise debt, either short-term or long-term. Increasingly today, corporations are using their trademark portfolios as security for capital restructuring or refinancing, as well as expansion of the business model. In reorganisation the value of trademarks is important as a source of funding for either debtor-in-possession (DIP) financing or take-out refinancing.

Another valuation environment in the United States that is often seen involves a company's efforts to comply with either federal, state or international tax legislation; and/or to comply with the new standards of valuation required by the Financial Accounting Standards Board (FASB). In the former case, valuation for tax reasons would typically fall under the IRS Section 482 Transfer Pricing Standards. Similarly, when a holding company is set up to own trademarks and other intangible assets, a level of commitment to various state, federal and international arm's length standards must be met.

The FASB regulations, Sections 141, 142 and 144, deal with trademarks, brand names, and other intangible assets acquired by a company. Those assets which are deemed to have an extended and uncertain lifespan need to be revalued from time to time, in order to ensure that the acquiring company has not lost or squandered part of the value of its trademark portfolio or other IP. Other financial or tax-driven reasons for valuation include the donation of a trademark to a non-profit group which would fall under IRS scrutiny, as well as establishing value of trademarks for a subsidiary company holding a corporation's trademarks and other intellectual property.

Valuation of trademarks in various litigation scenarios is important to a successful prosecution or defence of a specific case. Cases of trademark infringement require valuation of the trademark assets. Also, trademark dilution and confusion cases will often require valuation of the assets. Naturally, in a trademark damages case one would look at the value of the asset, as well as the lost profits and/or lost royalties.

The valuation process

As briefly discussed above, the value of a trademark and its associated brand assets will certainly vary from time to time. The most important concept in the valuation of trademarks and other IP is that valuation is context specific and time critical. As we can see in Table 2, the value of a given trademark will vary substantially based on whether the company is a going concern, or in an orderly disposal or liquidation environment. Similarly, a litigation environment can substantially change the value of a trademark. Adverse litigation will, of course, reduce the overall value of a trademark.

In Table 2, we illustrate the difference between going-concern value and liquidation value. It is important to note the substantial

Table 1: bundles of intellectual assets

Marketing bundle	Technical bundle	IT bundle
Trademark registrations	Key patents	Operating systems
Umbrella brand name	Packaging technology	Mailing lists
Sub-brand names	Manufacturing technology	Proprietary software
Product names	Product shapes	Databases
Copyrights	Process technology	Shrink-wrap software
Graphics	Technical designs	Certifications
Corporate name and logo	Drawings, manuals	Source code

Table 2: going-concern value vs. disposal/liquidation*

Case study	Going-concern value	Disposal or liquidation	Proportion
Polaroid	US$400M+	US$60M	15%
Boston Market	US$210M	US$31M	14.7%
TWA	US$800M	US$50M	6.3%
Marvel	US$1B	US$232M	23.2%
Amherst Fiber Optics	US$5M+	Approx. US$250K	5%
Average			**12.8%**

**Actual valuation numbers have been modified to protect the confidentiality of our client assignments* difference between going-concern values for important trademarks and their ultimate realised values in liquidation. Perhaps Polaroid is the best recent example where prior to its move into bankruptcy and reorganisation the trademark and brand assets were variously valued at between US$400 million-plus and US$2 billion. In the liquidation or disposal of an asset in a distressed environment the value will be depreciated by as much as 70% to 90% from a going-concern value. Table 2 illustrates that in cases we have been involved in the average disposal or liquidation value was approximately 13% of its corresponding going-concern value.

Valuation techniques

Any discussion of the valuation process must, of course, focus on more than context and time - it must also focus on methodology and valuation technique. Traditionally, three approaches have been used to value trademarks and other intangible assets (and these three methodologies are born out of experiences in valuing tangible assets in the professional valuation community). The market approach, the cost approach and the income approach are those three primary methodologies. The market approach is used whenever comparable transactions can be found - but in valuing trademarks and other IP, good comparables are rarely available. The cost approach is not particularly well suited for valuing trademarks and other IP because it is based on historical cost, which typically does not measure the current market value of an intangible asset like a trademark or brand. Finally, this leaves the income approach. This technique tends to be quite simplistic and it is typically used by most valuation experts. Their approach is simply to select a royalty rate for a trademark and apply that to the sales of the trademark product, with the present value of those cash flows representing "the value of the trademark". While the income approach is good as a back-up or a sanity check, we believe there are other methods of valuation.

Over the last 15 years we have developed several proprietary valuation methods, two of which are worth mentioning here. The first, VALMATRIX®, is the basis for an objective comparison of a trademark or a brand's strengths relative to its competition. The VALMATRIX score is then applied against the wide range of royalties for similar trademarks; and the application of that score to the royalty rate range results in a much more focused and appropriate imputed income level. Immediately below, we see a brief explanation of the Brand Value Equation (BVEQ) which, in simple terms, states that because a trademark does not travel in a vacuum, valuing the brand asset bundle is often more appropriate than valuing the individual trademark. Using BVEQ, two elements of value are established: the first is the core trademark value and the second is the value of the other incremental efficiencies or incremental value elements. The total brand value then becomes the sum of the core trademark value and the incremental value elements. Table 3 summarises an application of the BVEQ methodology against the Coca Cola brand.

Table 3 – valuing the Coca Cola brand using BVE_Q

Brand has multiple elements of value:
- Core brand value (CBV)
- Incremental value elements (IVEs)

$BVE_Q = CBV + (IVE_1 + IVE_2 + \ldots + IVE_N)$

BVE_Q Summary: COCA COLA*
Recognises total value of a brand bundle

1. Core brand value (Coke TMs)	CBV	US$10B
2. Incremental value elements	IVE_1	US$0.2B (eg, Corporate colours)
	IVE_2	US$0.5B (eg, Umbrella ads)
	IVE_3	US$0.3B (eg, Foreign TMs)
	IVE_4	US$1.8B (eg, Diet Coke TMs)
Total brand value		**US$12.8B**

**Actual valuation numbers have been modified to protect the confidentiality of our client assignments*

Case studies

In this part of our discussion we look at four different case studies (see Table 5), as well as the underlying cause and environment in which the trademark and IP assets are being valued. In each of these cases there were different reasons for the valuation of the trademark assets. In the case of the Budget Group in which Budget Rent-A-Car, as well as other assets such as the Ryder trademarks, licence agreements and various franchise agreements, were valued, we used a range of methodologies to get the value for each of these assets. Once we went through the valuation process we were able to establish going-concern value, which was in excess of US$500 million, versus liquidation value, which was slightly more than US$100 million*.

Our second case study involves Polaroid Corporation and the valuation of its trademarks and brand assets. In addition, we valued the patents and technology assets of the company. The valuation process took place during the company's Chapter 11 reorganisation and the focus of our work was to determine whether the value of the assets would be substantially greater in an orderly disposal than in an immediate liquidation. In this case, the valuation of the trademark assets required knowledge of possible acquirers and competitors. As we see in the chart in Table 5, the orderly disposal values for the assets were in the US$46 million to US$65 million range, whereas the liquidation values were between US$10 million and US$12 million*. It is important to note that all the values shown in Table 5 were net of hard costs of liquidation or disposal.

In the case of Amherst Fiber Optics we were asked to identify all of the IP with value, to identify acquirers and to sell the assets. Because we were working on a very tight time schedule, we had to perform all the valuation and disposition tasks prior to the end of the calendar year. As a result, we moved swiftly to identify and value the trademarks and other brand assets and also to identify the group of technology assets with value. In liquidating these assets for the parent company TVC, our goal was to move quickly, not necessarily to maximise cash from the sales. The reason for this is that by disposing of these assets prior to 31st December, the company could then be eligible for a tax refund of more than US$10 million as reimbursement for development costs incurred.

Valuing assets in a tax-based environment requires a great deal of accuracy and extensive supporting materials. The IRS, as well as the tax authorities in France, the United Kingdom, Germany and other industrialised countries, are keenly interested in the value of trademark assets - as well as the fees and royalties charged on an inter-company basis for use of those assets. In the case of L'Oreal we were asked to identify key brands and trademarks, as well as other elements of value for a given brand. The valuation methodology used comparable transactions and the report and its supporting materials were set to the standards of IRS Section 482, as well as the French tax authorities. What is clear from the two L'Oreal-related charts in Table 5 is that the brand had several elements of value including sub-brands and internet brand assets. ■

__Weston Anson__ is Chairman of CONSOR®, an intellectual asset consulting firm specialising in trademark, patent and copyright licensing, valuations and expert testimony. The firm is headquartered in La Jolla, California, and has offices in New York and London.
wanson@consor.com.
__Daryl Martin__ heads up the valuation division for CONSOR, and is responsible for analysing all types of intellectual property, including trademarks, copyrights, patents, trade secrets, domain names, mailing lists and customer databases.
dmartin@consor.com.

Table 4 – case studies, valuation in practice

Case study #1 - acquisition/bankruptcy Budget Group, Inc.

Asset description	Primary methodology	Secondary methodology
Budget trademark (North America)	Relief from royalty	Market
Franchisee rights (North America)	Relief from royalty	Market
Budget trademark (International)	Relief from royalty	Market
Franchisee rights (International)	Relief from royalty	Market
Ryder truck licence	Relief from royalty	Cost
Reservation system	Relief from royalty	Cost
Airport concession rights	Relief from royalty	Cost
Mailing list and database	Market approach	Cost

Case study #2 – bankruptcy/reorganisation Polaroid Corporation

Key assets

Technology	Marketing intangibles
800+ patents	Core Polaroid brand
52 clusters	Sub-brands
10 key clusters	Trademark licences
IDP technologies	Photo archive
500+ patent applications	
30,000+ chemicals	
Patent licences	

Polaroid net asset values*

	Orderly disposal	Immediate liquidation
Total technology asset value	US$15.2M - US$19.5M	US$36.5M - US$430M
Total brand	US$30.8M - US$45.2M	US$67M - US$78M
Net value (after all hard costs)	**US$46M - US$65M**	**$10.4M - US$12.1M**

Case study #3 – liquidation/asset sale Amherst Fiber Optics

Company:	TVC
Context:	Liquidation of subsidiary
Cause:	Massive potential tax benefit
Components:	Eight independent patent bundles, fibre optics after-market, trademarks
Valuation approach:	Components of value, liquidation value

Case study #4 – tax based L'Oreal

Value IP and set royalty rates for IP holding company
Identify value of key brands
Identify other IP with value
Select best valuation methodology
Valuation to standards of IRS Section 482, and French tax authorities

L'Oreal valuation summary*

Context is tax-based	
Use of CUT (Comparable Uncontrolled Transaction) to meet IRS needs	
Core brand	US$250M
Sub brand	US$115.3M
Sub brand	US$43.4M
Internet brand	US$11M
Total	**US$419.7M**

** Actual valuation numbers have been modified to protect the confidentiality of our client assignments*