The Valuation of Copyright-Related Intangible Assets

Katherine A. Gilbert

A copyright benefits from a specific bundle of legal rights that provides the author/creator the right to authorize or to prohibit the uses of the copyrighted work. Generally, the author of the original work owns the copyright, even though there are exceptions to this rule. Copyrights can be sold or transferred by assignment or by licensing. This discussion presents an overview of the generally accepted valuation approaches and methods that the valuation analyst may consider when performing a copyright-related intangible asset valuation.

Introduction

From a valuation perspective, copyright-related intangible assets have similar economic and legal characteristics to other types of commercial intellectual property. These other types of commercial intellectual property include: trademarks, patents, and trade secrets.

All of these types of intellectual property are specifically protected by either federal or state statutes. These statutes provide very specific economic and legal protection to (and, thereby, very specific development motivation to) the intellectual property owner.

First, we will describe the factors that are relevant to the identification and valuation of copyright-related intangible assets. Second, we will discuss the generally accepted copyright valuation approaches and methods. Last, we will present two simple examples, using two different analytical methods, to illustrate the valuation of copyright intellectual property.

"As is true with all intellectual property, a copyright has a special set of legal rights and protections that is afforded to the copyright owner. These legal rights are the basis for the value of a copyright."

Description of Copyright-Related Intangible Assets

In the following sections, we will consider each of these questions regarding the identification and valuation of copyright-related intangible assets:

1. What is a copyright and what economic advantage does it provide?
2. What are the social and macroeconomic benefits of copyright protection?
3. What types of creative works are subject to—and not subject to—copyright protection?
4. What are the various categories or types of copyrights?
5. What is the legal term of federal copyright protection?
6. What is the economic impact of copyright registration on the intellectual property owner?
7. What are the common forms of ownership interest transfer of the copyright?

Economic Benefits Associated with Copyright-Related Intangible Assets

As is true with all intellectual property, a copyright has a special set of legal rights and protections that is afforded to the copyright owner. These legal rights are the basis for the value of a copyright. And, these legal rights provide for the various commercialization opportunities related to copyrights. These legal rights are summarized below.

A copyright provides for a bundle of exclusive rights that provides authors of original literary, musical, dramatic and

artistic works with the sole right to authorize (or prohibit) the following uses of their copyrighted works:

- to reproduce all or part of the work
- to make new (derivative) versions
- to distribute copies by selling, renting, leasing, or lending them
- to perform (that is, to recite, dance, or act) the work publicly
- to display the work publicly, directly, or by means of film, TV, slides, or other device or process

The first three rights are violated when anyone copies, excerpts, adapts, or publishes a copyrighted work without permission. In rare cases, an author may dedicate a work to the public domain. However, unless the facts prove otherwise, the valuation analyst will typically assume that all original works published less than 75 years ago in the United States are protected by copyright.[1]

It is noteworthy that the above definition uses the term "author." As it is mentioned above, copyrights cover a variety of creative and artistic works—many of which are not literary.

One reason for this is that, under copyright law, the term "author" includes artists, composers, photographers, computer software programmers, and other individuals of creative talent—in addition to writers. Also, since copyrights are sometimes granted to businesses, an "author" can be a corporation or other non-individual business form.

"Copyright and trade secret laws sometimes protect the same kinds of information. And, copyright and trade secret laws are sometimes mutually exclusive of each other."

Basically, a copyright provides legal protection regarding the original expression of ideas. A copyright does not protect the ideas themselves. That is, an idea cannot be copyrighted. Rather, it is the expression of the idea—the way the idea is presented—that is copyrighted.

A copyright gives the owner the exclusive right to (and prohibits all other parties from the right to) perform, reproduce, alter, distribute, or display the original work of expression. A copyright allows the owner to—and prevents another party's ability to—economically benefit from the original work.

There are several legal and economic similarities between copyrights and trade secrets. Some of these similarities are discussed below.

Copyright and trade secret laws sometimes protect the same kinds of information. And, copyright and trade secret laws are sometimes mutually exclusive of each other.

The following discussion summarizes the salient points of how trade secret and copyright legal protections can work together under the Copyright Act of 1976.

- Trade secret and copyright protection are both available for unpublished works as long as (1) the idea (or ideas) in the work are sufficiently innovative to qualify as a trade secret (any confidential information that provides a business with a competitive advantage) and (2) the information is kept confidential.
- Trade secret and copyright protection may both be available for works that are distributed on a limited and restricted basis under a copyright licensing arrangement requiring the licensee (user) to recognize and maintain the trade secret aspects of the work. This dual protection is especially important for the computer software business.
- Trade secret protection is generally not available for software—if the source code is made available to the public on an unrestricted basis through such means as listing it in a computer magazine or on a medium of distribution (for instance, a compact disc).
- The deposit of a physical copy of the work that is being registered with the U.S. Copyright Office operates to disclose any trade secrets in the work. This statement is true unless the deposit in some way masks the material that comprises the trade secret.

  For instance, it is impossible to deposit samples of source code with major portions blacked out so that the parts of the code being maintained as a trade secret are not disclosed.

  There are several other methods for simultaneously registering a computer program and maintaining trade secrets. One common way is to withhold the source code altogether and deposit object code—which is impossible to understand when read in the U.S. Copyright Office.[2]

Generally, the "author" of the original work owns the copyright. Again, with regard to copyrights, the creative person in any discipline (e.g., the artist, composer, or musician, etc.) is called the author.

There are three exceptions to this rule regarding copyright ownership:

1. If an employee, in the normal course of employment, creates the copyright material, then the employer owns

the copyright. Such copyrighted materials are called "work made for hire."

2. If the copyrighted material is commissioned by a patron and the patron and the author sign "a work made for hire" agreement, then the copyright is owned by the patron. An example of this may be the commission of a family or executive portrait.
3. If the author sells the copyright, then the buyer owns the copyright. This statement is true regardless of whether the buyer is an individual, corporation, or some other form of entity.

All of the material in a copyrighted original work does not have to be new. Inexperienced valuation analysts sometimes believe that the compilations of the work of other "authors" are not subject to copyright protection. This belief is not correct. In fact, the compilation of existing work itself may be considered an original expression subject to copyright protection.

A compilation is a copyright work that is the result of bringing together or arranging preexisting material (regardless of whether that material is protected by copyright) in an original—or nonobvious—way.

Copyright protection is based on the original selection, coordination, or arrangement of the material, not the copyright status of the preexisting material itself.

There are two types of compilations:

1. fact compilations
2. collective works

Arranging public domain information, such as names and addresses or other data, in some minimally creative way creates a fact compilation. Common examples of fact compilations are electronic databases, directories, almanacs, price lists, and catalogs.

A collective work is a special type of compilation created by arranging copyright elements in a single work. Common examples are poetry anthologies, encyclopedias, newspapers, and magazines.[3]

Copyrights allow monopolistic exploitation benefits to the copyright owners. There are general social benefits to providing these individual economic benefits.

These general social benefits related to copyrights are explained as follows:

> The Founding Fathers recognized that everyone would benefit if creative people were encouraged to create new intellectual and artistic works. When the United States Constitution was written in 1787, the framers took care to include a copyright clause (Article I, section 8) stating that "The Congress shall have Power…to promote the Progress of Science and useful Arts, by securing for limited times to Authors…the exclusive Right to their…writings."
>
> The primary purpose of copyright, then, is not to enrich authors; rather, it is to promote the progress of science and the useful arts—that is, human knowledge. To pursue this goal, copyright encourages authors in their creative efforts by giving them a mini-monopoly over their works—termed a copyright. But this monopoly is limited when it appears to conflict with the overriding public interest in encouraging creation of new intellectual and artistic works generally.[4]

Categories of Materials that May Be Subject to Copyright

While there is only one legal form of a copyright, there are several categories or types of work that are subject to copyright protection.

These several categories of works that are subject to copyright protection are listed below:

1. artistic—including paintings, sculptures, and drawings
2. choreographic works—including ballet
3. dramatic works—including plays and operas
4. literary works—including books, manuscripts, newspapers, magazines, poetry, and advertisements
5. musical works—including compositions, song lyrics, and advertising jingles (musical works include the compositions themselves and the recordings of the works)
6. pictorial and photographic—including cartoons, pictures, maps, prints, drawings, and photographs
7. video and audiovisual works—including movies and motion pictures, music videos, and television programs

These works do not have to be published, recorded, or performed in order to be subject to copyright protection. For example, an unpublished work—and even a work that has never been performed or played—may still be protected by copyright.

"While there is only one legal form of a copyright, there are several categories or types of work that are subject to copyright protection."

Statutory Term of the Copyright Protection

Estimating the term of copyright protection is somewhat confusing. This is because the law related to this point changed in 1976.

The current U.S. Copyright Act was enacted in 1976 and covers works created after December 31, 1977. The previous U.S. Copyright Act was enacted in 1909 and covers works created up to December 31, 1977.

With consideration to these statutory changes, the term of copyright protection is as follows:

> Few things in this world last as long as copyright protection. Indeed, an author's work is likely to be long forgotten before her copyright in it expires. The copyrights in works created after 1977 by individuals usually lasts for the life of the author plus an additional 70 years. The copyright in works created by employees for their employers lasts for 95 years from the date of publication, or 120 years from the date of creation, whichever occurs first.
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> The copyright in works created and published during 1923–1963 lasts for 95 years from the date of publication if they were (or are) timely renewed. . . . As a result, it may be necessary to do some legwork to find out if a renewal was filed for a work. The copyright in works created or published during 1964–1977 lasts for 95 years regardless of whether a renewal was filed. The copyright in works created but not published before 1978 lasts at least 70 years after the author dies.[5]

"Many inexperienced valuation analysts believe that it is necessary for an author to register the created work in order for it to be subject to copyright protection. Unlike patents and trademarks, however, registration is not required with regard to copyrights."

Copyright Registration

Many inexperienced valuation analysts believe that it is necessary for an author to register the created work in order for it to be subject to copyright protection. Unlike patents and trademarks, however, registration is not required with regard to copyrights.

Nonetheless, there are several reasons why an author may wish to formally register his or her work with the U.S. Copyright Office. Some of these reasons are summarized below.

> A creative work is protected by copyright the moment the work assumes a tangible form—which in copyright circles is referred to as "fixed in a tangible medium of expression." Contrary to popular belief, providing a copyright notice and/or registering the work with the U.S. Copyright Office is not necessary to obtain basic copyright protection. But there are some steps that can be taken to enhance the creator's ability to sue or stop others from copying:
>
> - Place a copyright notice on a published work.
>
> The copyright notice, or "copyright bug" as it is sometimes called, commonly appears in this form: "© (year of publication) (author or other basic copyright owner)." By placing this notice on a work that is published (distributed to the public without restriction), the author prevents others from claiming that they did not know that the work was covered by copyright. This can be important if the author is forced to file a lawsuit to enforce the copyright, since it is much easier to recover significant money damages from a deliberate (as opposed to innocent) copyright infringer.
>
> - Register works with the U.S. Copyright Office.
>
> Timely registration within three months of the work's publication date, or before the infringement actually begins—makes it much easier to sue and recover from an infringer. Timely registration creates a legal presumption that the copyright is valid and allows the copyright owner to recover up to $150,000 (and possibly attorney fees) without proving any actual monetary harm.[6]

Transferability of Copyrights

Copyright rights can be (and often are) sold or transferred between individuals and between corporations, in whole or in part. In fact, the transfer of copyright rights is the most common way for authors to commercialize their copyrighted work.

The two most common types of copyright transfer structure are:

1. assignments and
2. licenses.

The differences between assignments and licenses are summarized as follows:

> When all copyright rights are transferred unconditionally, it is generally termed an "assignment." When only some of the rights associated with the copyright are transferred, it is known as a "license." An exclusive license exists when the right being licensed can only be exercised by the licensee and no one else. If the license allows others to exercise the same rights being transferred in the license, the license is said to be non-exclusive.[7]

Licensing is a very common form of the transfer of copyright rights. A license separates the bundle of legal (and economic) rights associated with copyrights between a licensor and a licensee.

These contractually divided bundles of rights are described as follows:

> Any of the exclusive rights that make up a copyright can be subdivided, or split, into smaller and smaller pieces and then transferred to one or more parties. Just think about the way books are marketed. In addition to book rights, there are audio rights, foreign translation rights, performance rights, film adaptation rights and even future technology rights. Each exclusive right is jealously guarded and, as a rule, sold piecemeal to one or more persons to maximize the author's return. The ways in which the copyright pie can be sliced are almost endless.
>
> A copyright owner may limit any (or all) of the rights granted to another by (1) time, (2) geography, (3) language, or (4) type of use. Rights can even be split by market segment or channels of distribution (e.g., hardcover vs. paperback rights). Copyrights are infinitely divisible. Bear in mind that rights are seldom sold, licensed, or transferred in their totality or nonspecifically.[8]

Generally Accepted Copyright Valuation Approaches and Methods

All three generally accepted intellectual property valuation approaches may be applicable to the analysis of copyrights. The cost approach is less commonly used than the income approach or the market approach. Because the copyright grants monopolistic rights to the owner, the cost approach is not always applicable to a copyright valuation analysis.

However, if properly performed, the cost approach does have application to copyrights in certain instances.

Cost Approach Methods

Both creation cost and re-creation cost methods may be used with regard to copyright valuation analysis. Since a copyright intellectual property represents a creative or artistic intellectual property, the term "creation cost" is used more commonly than the term "replacement cost new."

Likewise, the term "re-creation cost" is used more commonly than the term "reproduction cost new."

Nonetheless, there are conceptual and procedural similarities:

1. between creation cost and replacement cost new and
2. between re-creation cost and reproduction cost new.

In all cost approach valuation analyses of copyrights, the analyst should consider as cost components both:

1. developer's profit and
2. entrepreneurial incentive.

In the cost approach analysis of intellectual property, developer's profit and entrepreneurial incentive can sometimes represent the largest components of value.

"The cost approach is based on the economic principle of substitution. This principle suggests that an investor will typically pay no more for a fungible intellectual property asset than the cost to purchase or construct a substitute asset."

The cost approach does have certain limitations with regard to the analysis of a corporation-owned copyright. Because of these limitations, the cost approach is often considered to provide a floor (or minimum) estimate of value—as opposed to a ceiling (or maximum) estimate of value.

The application limitation of the cost approach relates to the fact that the copyright grants the intellectual property holder exclusive or monopolistic rights with regard to the subject work. The cost approach is based on the economic principle of substitution. This principle suggests that an investor will typically pay no more for a fungible intellectual property asset than the cost to purchase or construct a substitute asset.

However, it is not legally possible to purchase or construct a substitute intellectual property with regard to copyrights. Copyrights are only granted with regard to unique and original work. Therefore, the hypothetical investor who attempts to purchase or construct a substitute intellectual property is, by definition, guilty of copyright infringement.

Therefore, the "willing buyer" in a copyright market value transaction cannot legally re-create the subject

copyright. The "willing seller" in a copyright market value transaction will typically not sell for less than his or her cost (that is, the investment) in the subject copyright.

For this reason, the cost approach analysis often provides a minimum indication of the value of a copyright.

Market Approach Methods

Market approach methods are commonly used in a copyright valuation analysis. There is a fairly active market with regard to the fee simple sale of copyrights. This is true with regard to all of the types of copyrighted materials (for example, literary, musical, artistic, etc.) discussed above.

However, the transactional (particularly pricing) details regarding these copyright sales are not publicly disclosed. Also, it is often difficult for analysts to develop units of comparison in order to extract market-derived pricing multiples from these transactional data.

In other words, it is difficult to convert pricing data regarding the actual sale of a copyright into a meaningful "per picture," "per lyric," or "per word" pricing multiple .

There is a very active market with regard to the license of all types of copyrighted materials. Therefore, the most common market approach methods involve some form of royalty rate or similar license analysis.

Analysts sometimes have the problem of developing units of comparison if the selected empirical license agreements call for fixed periodic dollar payments—for example, $100,000 per year. However, many copyright license agreements are on either:

1. a royalty rate formula or
2. a per-use formula.

With regard to the royalty rate formula, the license agreement typically compensates the author by a percentage of the total revenues generated through the use of the copyrighted materials.

With regard to the per-use formula, the license agreement typically compensates the author as a dollar amount for each time the copyrighted material is performed, displayed, or otherwise used.

Income Approach Methods

Income approach methods are very commonly used in the valuation and economic analysis of copyright intellectual properties.

The various income approach methods typically involve some form of the following types of analysis:

1. Incremental income analysis—the estimation of the difference between:
   a. the amount of income that the owner/operator would generate with the use of the subject copyright, and
   b. the amount of income the same owner/operator would generate without the use of the subject copyright.
2. Profit split income analysis—the estimation of the total income that the owner/operator would generate from the use of the copyright where the total income estimate is allocated to (or split between):
   a. the copyright and
   b. all of the other tangible and intangible assets that contribute to the generation of the owner/operator total income estimate.
3. Residual (or excess) income analysis—the estimation of the residual owner/operator income with the ownership/operation of the copyright. This residual income analysis is accomplished by first estimating the total owner/operator income. The analyst then identifies and values all of the owner/operator tangible and intangible assets.

   A fair rate of return, which represents a capital charge or an economic rent, is then assigned to each category of the tangible and intangible assets.

   The analyst would then subtract the capital charge on contributory assets from the total owner/operator income estimate. Finally, the residual or excess income is assigned to the copyright.

With regard to all of these income approach analyses, the copyright income is projected over an estimate of the remaining useful life (RUL) of the copyright income stream. Typically, the RUL estimate is much shorter than the legal or statutory life of the copyright.

Most often, the RUL is an expectation of the period of popular and commercial acceptance of the book, movie, song, play, poem, or other copyrighted work. The present value of the owner/operator income (defined as excess, incremental, or residual income) over this expected RUL is an indication of the value of the copyright.

Illustrative Examples of a Copyright Valuation

This section will present two simple copyright valuation examples. Example 1 presents an illustration of a cost approach analysis. In Example 1, the analyst will estimate the value of the copyright associated with a video training file.

Example 2 presents an illustration of an income approach analysis. In Example 2, the analyst will estimate the value of a copyrighted musical composition.

Example 1—Cost Approach Valuation Analysis

Let's assume that Willamette Management Associates ("Willamette") is a prominent valuation consulting, economic analysis, and financial advisory firm. The firm's analysts are recognized for their experience and expertise in applied microeconomics.

However, some of the firm's analysts have not developed their more mundane skills. With this fact in mind, and in order to keep the Willamette offices properly illuminated, firm management produced a video training film entitled "How to Change a Light Bulb."

This training video proved to be remarkably successful at all of the Willamette offices. Let's assume that, in the jurisdiction in which Willamette is headquartered, this type of intellectual property is taxable for ad valorem property tax purposes.

The objective of this analysis is to estimate a fair transfer price for the subject copyright, as of January 1, 2009, for ad valorem property tax assessment purposes.

Fact Set and Illustrative Valuation Variables

The subject copyright relates to the original video "How to Change a Light Bulb" ("Light Bulb"). The video is a safety and training film of approximately 60 minutes in length. Universal Training Corporation, an independent producer of institutional training films, produced the video for Willamette.

The video represents the culmination of a safety research project conducted by the management of Willamette with the objective of reducing job-related injuries and resulting workers' compensation costs.

The findings of an extensive safety research project conducted by the management of Willamette are embodied within the copyrighted video. The research project related to an injury and illness prevention program that was developed to educate and train approximately 100 Willamette analysts.

At the time of its development, this video was the only training film produced exclusively for the promotion of safety and prevention of job-related injuries at economic consulting firms.

Application of the Copyright Valuation Approaches and Methods

Based on the availability of information and the relevant facts and circumstances, the analyst concluded that the cost approach is appropriate for estimating the value of the subject copyright.

Let's assume that the valuation analyst based this conclusion on the following facts:

- The video was developed specifically for the purpose of training and educating Willamette analysts in safety awareness and injury prevention.

  Accordingly, the intellectual property content of the video represents the culmination of knowledge and experience in safety awareness particularly relevant to Willamette operations.
- The costs (including direct, indirect, and opportunity-related costs) of creating the subject copyrighted video are readily determinable and traceable.
- The video represents the only known safety film produced specifically for economic consulting firms. Based upon this fact, transactions in comparative copyrights were not available for the analyst's market approach analysis.

  Therefore, the application of the market approach was not practical in this ad valorem property tax valuation analysis.
- The video was not created for income-producing purposes, that is re-sale. Therefore, it would be difficult to apply the income approach.

Exhibit 1 summarizes the illustrative cost approach analysis. As presented in Exhibit 1, the analysis considered the following factors with respect to estimating the value of the subject copyright:

- an estimate of the direct compensation, overhead, and benefits-related cost of the intellectual content of the video; and
- the accumulation of all direct costs incurred during the actual production of the video.

The cost of the intellectual property content of the training video is best described as the cost resulting from the requisite accumulation of safety-related knowledge and experiences that would facilitate the conceptual development of the video.

If faced with the task of replacing the video, management at Willamette would have to call upon individuals with considerable experience regarding both:

1. the operations of economic consulting firms and
2. job-related accidents and potential safety hazards.

As summarized in Exhibit 1, the analyst estimated the following indirect costs relating to the intellectual property content of the subject copyrighted video:

- [a] Annual costs of an "experience-appropriate" individual.

Exhibit 1
Willamette Management Associates
Copyright Related to the "How to Change a Light Bulb" Employee Training Video
Illustrative Cost Approach Valuation Analysis
As of January 1, 2009

Cost Approach Valuation Components	Employee Direct Compensation Costs	Full Absorption Overhead and Employee Benefits Costs	Total Direct of all Costs and Indirect Costs
Indirect copyright development costs:			
Estimate of the Cost of the Subject Video Intellectual Property Content:			
Total annual cost of an "experience-appropriate" individual [a]	$ 76,750	$ 34,538	
Percentage of the annual cost devoted to safety area [b]	40%	40%	
Estimate of the annual cost of the intellectual property development time [c]	30,700	13,815	
Estimate of the required intellectual property development period (years) [d]	10	10	
Estimate of the total intellectual property content development cost [e]	$ 307,000	$ 138,150	
Percentage of the intellectual property content development cost applicable to the subject "Light Bulb" video [f]	50%	50%	
Estimate of the cost of the intellectual property content [g]	$ 153,500	$ 69,075	
Total copyright development indirect costs (rounded)			$ 220,000
Direct copyright development costs:			
Estimate of the Cost of the Subject Video Production:			
Universal Training Corporation estimate of the replacement cost new of the script, video production, and the quick reference guide [h]		$ 242,000	
Owner/operator personnel direct labor costs [i]		143,000	
Additional direct expenses [j]		24,000	
Total copyright development direct costs (rounded)			$ 410,000
Total replacement cost new for the development of the "How to Change a Light Bulb" employee training video			$ 630,000
Less: Functional and technological obsolescence factor [k]			10%
Equals: Indicated value of the "How to Change a Light Bulb" Video Copyright			$ 567,000
Value of the "How to Change a Light Bulb" Video Copyright (rounded)			$ 600,000

An "experience-appropriate" individual is an owner/operator employee, in this case a Willamette employee, who is considered to have the necessary knowledge and experience regarding safety-related issued required for the development of the concepts and objective that are contained in the training video.

An employee with at least a 10-year history would possess the requisite experience and expertise. Let's assume that such employee would earn approximately $77,000 per year.

In order to reflect the full absorption cost of this individual's conceptual development time, the analyst included an estimate for corporate overhead and related employee benefits.

The overhead and employee benefits-related component of the conceptual development cost is approximately $35,000 per year or roughly 45 percent of annual employee compensation.

Included with the overhead component are the costs of the owner/operator support staff personnel and their work-related employee benefits.

- [b] Percentage of annual cost devoted to safety area.

The percentage of annual cost devoted safety area represents that portion of the experience-appropriate employee's time devoted to safety related issues.

The analyst's discussions with the Willamette safety and training director indicated that approximately 30 to 50 percent of her activities were related to the safety function.

- [c] Estimate of the annual cost of the intellectual development time.

The analyst projected a 40 percent safety-related annual time commitment.

Let's assume that this $45,000 cost is represented by approximately $31,000 in direct employee compensation and approximately $14,000 in overhead and employee benefits.

- [d] Estimate of the required intellectual property development period.

Based on the analyst's review of the employment history of the director of employee relations and development, the analyst concluded that a reasonable estimate of the intellectual property development period was 10 years.

This is the length of the period before technological innovation within the firm would render then-existing safety concepts and practices obsolete.

- [e] Estimate of the total intellectual property content cost.

The projection of a 10-year intellectual property development period and a total annual cost of $45,000 for the safety function resulted in an estimated total intellectual property cost of approximately $450,000.

Let's assume that approximately $307,000 in direct compensation and $138,000 in overhead and employee benefits comprise this total development cost.

- [f] Percentage of the intellectual property development cost applicable to the copyrighted video.

As previously discussed, 40 percent was estimated to be the time required of an experience-appropriate employee.

With regard to the subject training video, redundant activities and technological advancements during the 10 year intellectual property development period would render some of the experience and knowledge irrelevant.

Therefore, the analyst excluded portions of the attendant safety function costs from the total development cost.

Based on discussions with the director of employee relations and development and an estimate of a 10 year intellectual property development period, the analyst projected that 50 percent of total work commitment dedicated to the safety function would relate to concepts and information appropriately included within the contents of the training video.

- [g] Estimate of the cost of the intellectual property content.

Based on a 10 year projected intellectual property development period; a total intellectual property content cost of approximately $450,000, and a 50 percent safety function relevance factor, the estimated cost of the intellectual property content of the Willamette training video is approximately $220,000.

This cost includes approximately $154,000 indirect compensation and $69,000 in overhead and employee benefits.

As presented in Exhibit 1, the total indirect cost associated with the development of the intellectual property content of the training video is approximately $220,000.

The cost of actual video production represents all direct costs incurred to bring the training video to its functionally effective form.

The analyst estimated the following direct production costs related to the production of the training video:

- [h] Universal Training Corporation fee.

Willamette originally contracted with Universal Training Corporation ("UTC") for the actual product of the training video. UTC wrote the original script for the video, produced the video, and drafted the initial quick reference guide relating the training video.

The analyst contacted UTC in which they estimated a replacement cost new of the training video of $242,000.

- [i] Owner/operator direct labor costs.

  A task force comprised of Willamette employees was originally created to oversee activities of UTC. This employee task force was also responsible for reviewing and editing all of the materials produced by UTC.

  The analyst estimated the total direct labor replacement cost and the attendant overhead and employee benefits relating to the efforts of the task force at $143,000.

- [j] Additional direct expenses.

  Incidental direct expenses, in the form of miscellaneous support items, such as administrative costs, duplication, reproduction and postage charges, black belts, shirts, and voice-overs were incurred during the original production of the training video.

  The analyst estimated this expense to be $24,000.

As presented in Exhibit 1, the total direct costs associated with the development of the subject training video are $410,000 (rounded).

Based on the nature of the training film, the analyst concluded that the only relevant obsolescence factor in this particular instance is technological obsolescence. In the analyst's opinion, the subject training video would remain relevant for an estimated 10-year period.

The training video was one year old as of the valuation date. Let's assume that it is the analyst's opinion that a straight-line decay rate is reasonable regarding the technological relevance of the training video intellectual property content.

Example 1 Copyright Value Conclusion

Based on the analyst's procedures as described above, and in the analyst's opinion, the value of the copyright of the "Light Bulb" employee training video, as of January 1, 2009, is $600,000 (rounded).

Example 2—Income Approach Valuation Analysis

Drugs N. Booz ("Booz") is a composer of rock and roll music and lyrics. Last year, Booz composed the words and music to "Misogynous Memories" ("Memories"), a soulful rock and roll ballad. Booz is a contract employee of music producer Rock and Roll Corporation (RRC).

Memories was a work for hire and therefore the copyright is owned by RRC. The local taxing authority assesses the RRC on a unit valuation basis. The local taxing authority assessor estimated the total unit value of RRC, as of January 1, 2009.

In the taxing jurisdiction in which RRC is located, intangible personal property is exempt from ad valorem tax. In this case, a copyright intellectual property clearly qualifies as an exempt intangible asset.

Accordingly, RRC management will use this valuation to contest its ad valorem property tax assessment.

Fact Set and Illustrative Valuation Variables

The date of the copyright valuation is January 1, 2009. RRC management prepared a projection of the income it expects to earn from the recording and distribution of the "Memories" work.

For popular rock and roll songs like 'Memories," it is the RRC historical experience that the average life of consumer popularity is five years.

Also, according to RRC historical experience, consumer demand of such a successful popular musical composition approximates an exponential decay curve function.

Therefore, starting with the January 1, 2009, valuation date, the percent surviving in the consumer demand curve will be less than 10 percent (i.e., immaterial) after the year 2019.

This expected decay curve for consumer demand is based on:

1. a five-year average life and
2. an exponential decay function.

Based on the analyst's cost of capital analysis, the analyst concluded that the appropriate present value discount rate is 16 percent.

The analyst performed a comprehensive search for musical composition license agreements. Such license agreements are very common in the music recording industry. The analyst identified several guideline copyright license agreements with regard to commercially popular rock and roll musical compositions that had already been released.

Based on this research, the analyst concluded that the most applicable license royalty rate for "Memories" would be a 50 percent profit split. That is, in such copyright license agreements, the copyright licensor receives 50 percent of the composition-related net income, the copyright licensee also receives 50 percent.

In such license arrangements, the licensor is typically the copyright author or an owner/operator corporation copyright holder.

Also in such arrangements, the licensee is the recording artists and/or recording producers that actually record and distribute the recordings.

In this case, RRC corresponds to the typical copyright licensor in these musical composition license agreements. In the case of the RRC license agreement, let's assume that net income subject to the "profit split" royalty rate is defined as:

	Total revenue
Less:	Cost of goods sold
Less:	Selling, general, and administrative expenses
Equals:	Net income

Application of the Copyright Valuation Approaches and Methods

The income approach is the most applicable analysis, based on:

1. the information available to the analyst (including the RRC business plan) and
2. the objective of the analysis (i.e., to estimate the value of the subject copyright for an ad valorem property taxation appeal), the income approach is the most applicable analysis.

> *"This value is based on an income approach valuation method—the profit split method. In this particular application, the selected split profit was based on the analyst's study of selected guideline copyright license agreements."*

Exhibit 2 summarizes the RRC management-prepared business plan with regard to its recording and distribution of the "Memories" song. This Exhibit 2 summarizes:

1. the projection of total revenue generation,
2. the gross profit (i.e., total revenues less cost of goods sold), and
3. the net income (i.e., gross profit less selling, general, and administrative expense).

Based on the RRC projection of net income over the expected life cycle of the production and distribution of the "Memories" recordings, the analyst estimated the expected copyright license payments to the subject owner/operator corporation copyright holder.

Using a present value discount rate of 16 percent, Exhibit 2 presents the present value of the expected license payments to the subject owner/operator corporation of the "Memories" copyright.

Example 2 Copyright Value Conclusion

Based on the income approach valuation analysis summarized in Exhibit 2, the value of the RRC owner's intellectual property of the "Memories" copyright, as of January 1, 2009, is (rounded) $110,000,000. This amount represents the value of the subject corporation owner's intellectual property of the copyright on the subject musical composition.

This value is based on an income approach valuation method—the profit split method. In this particular application, the selected split profit was based on the analyst's study of selected guideline copyright license agreements.

Summary and Conclusion

This discussion introduced the valuation of copyrights. We first described the factors that are relevant to the identification and valuation of copyright-related intangible assets.

Second, we discussed the generally accepted copyright valuation approaches and methods. Finally we presented two simple examples, using two different analytical methods, to illustrate the valuation of copyright intellectual property.

As with any of the four types of intellectual property, it is important for the valuation analyst to consider the application of all generally accepted intangible asset valuation approaches and methods in the valuation of a copyright.

Notes:

1. Lloyd J. Jassin and Steven C. Schechter, *The Copyright Permission and Libel Handbook: A Step-by-Step Guide for Writers, Editors, and Publishers* (New York: John Wiley & Sons, 1998), pp. 10–11.
2. Richard Stim, *Patent, Copyright & Trademark*, 9th ed. (Berkeley, CA: Nolo Press, 2007), pp. 493.
3. Jassin and Schechter, pp. 14–15.
4. Stephen Fishman, *The Copyright Handbook—How to Protect & Use Written Works*, 9th ed. (Berkeley, CA: Nolo Press, 2006).
5. Ibid., p. 9.
6. Stim, pp. 186–187.
7. Ibid., p. 188.
8. Jassin and Schechter, pp. 15.

Katherine Gilbert is a senior associate in our Atlanta, Georgia, office. She can be reached at (404) 475-2312 or kagilbert@willamette.com.

This discussion is adapted from Chapter 23 of Guide to Property Tax Valuation, *by Robert F. Reilly and Robert P. Schweihs (Chicago: Willamette Management Associates Partners, 2008).*

Exhibit 2
Rock and Roll Corporation
Copyright Related to "Misogynous Memories"
Song Lyrics and Musical Composition
Illustrative Income Approach Valuation Analysis
As of January 1, 2009
(in 000s)

Projection Period	Prior Year 2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Income approach valuation analysis:												
Consumer demand expected decay function (average remaining useful life = 5 years)	0.9433	0.8052	0.6592	0.5397	0.4419	0.3618	0.2962	0.2425	0.1986	0.1626	0.1331	0.1090
Total recording and distribution revenue projection	$ 622,600	$ 956,570	$ 822,330	$ 706,930	$ 607,720	$ 522,440	$ 449,120	$ 386,100	$ 331,920	$ 285,340	$ 245,290	$ 210,870
Gross profit margin	14.99%	17.01%	17.75%	18.40%	18.84%	18.50%	18.50%	18.50%	18.50%	18.50%	18.50%	18.50%
Gross profit (revenue less cost of goods sold)	$ 93,320	$ 162,690	$ 145,960	$ 130,080	$ 114,470	$ 96,650	$ 83,090	$ 71,430	$ 61,400	$ 52,790	$ 45,380	$ 39,010
Selling, general, and administrative expense	88,020	122,940	96,470	76,570	60,680	48,300	38,810	31,470	25,770	21,100	17,270	14,140
Net income	5,300	39,760	49,490	53,520	53,780	48,350	44,280	39,950	35,640	31,690	28,110	24,870
Market-derived royalty profit split to copyright licensee	50%	50%	50%	50%	50%	50%	50%	50%	50%	50%	50%	50%
License payments to the copyright holder [a]	2,650	19,330	24,774	26,760	26,890	24,175	22,140	19,975	17,820	15,845	14,055	12,435
Present value discount factor at 16% discount rate	0.9576	0.8515	0.7340	0.6328	0.5455	0.4703	0.4054	0.3495	0.3013	0.2597	0.2239	0.1930
Discounted copyright license payments	2,535	16,925	18,160	16,930	14,670	11,370	8,975	6,980	5,370	4,115	3,145	2,400
Total present value of copyright license payments	$ 111,575											
Indicated Value of the "Misogynous Memories" copyright (rounded)	$ 110,000											

Note:
[a] The license payments are projected to be equal to the selected market-derived copyright license royalty rate "profit split" of 50 percent of net income.