Intellectual Property Valuations within Bankruptcy Controversies - Part 3

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INTRODUCTION

Part one of this article (*FVLE* 83, Feb./March 2020) examined the general nature and purpose of an intellectual property (IP) valuation in a bankruptcy controversy. It described the objective of such an analysis and presented resources for comparative benchmark analysis industry data. Part two (*FVLE* 84, April/May) introduced the three generally accepted valuation approaches applied by the analyst and summarizes the *cost* approach and the *market* approach and methods applied within each of these two approaches.

This third and final installment examines the *income* approach as it is used in intellectual property valuations within bankruptcy as well as the synthesis and conclusion in such a valuation. It also presents the attributes of an effective valuation expert report and identifies who should perform IP valuations.

INCOME APPROACH VALUATION METHODS

In the application of the income approach, value is estimated as the present value of the future income from the ownership/operation of the debtor company's intellectual property.

The present-value calculation has three principal components:

1) An estimate of the duration of the income projection period, typically measured as the debtor intellectual property's useful economic life (UEL)
2) An estimate of the intellectual property-related income for each period in the UEL projection, typically measured as either (a) owner income (e.g., license royalty income), (b) operator income (e.g., some portion of the total business enterprise income), or (c) both
3) An estimate of the appropriate present-value discount rate or indirect capitalization rate, typically measured as the required rate of return on an investment in the debtor's intellectual property

For purposes of the income approach, the UEL relates to the period of time over which the debtor company expects to receive the income metric related to the subject intellectual property:

1) license,
2) use, or
3) forbearance of use.

In addition to the term of the UEL, the analyst may also be interested in the shape of the UEL curve. That is, the analyst may be interested in the annual rate of decay of the debtor intellectual property's expected future income.

For purposes of the income approach analysis, many different income measures may be relevant. If properly applied, these different income measures can all be applied in the income approach analysis to conclude a value indication.

Some of the different income measures that may be applied in the income approach analysis include the following:

1) Gross or net revenues
2) Gross income (or gross profit)
3) Net operating income
4) Net income before tax
5) Net income after tax
6) Operating cash flow
7) Net cash flow
8) Incremental income
9) Differential income
10) Royalty income
11) Excess earnings income
12) Several others

Because there are different income measures that may be applied in the income approach, it is important for the capitalization rate (either the present-value discount rate or the direct capitalization rate) to be derived on a basis consistent with the level of income measure applied in the analysis.

Regardless of the measure of income considered in the income approach, there are several categories of valuation methods that may be applied to value the debtor company's intellectual property:

1) Valuation methods that quantify an incremental level of intellectual property income—that is, the debtor company may expect a greater level of revenue (however measured) by owning/operating the intellectual property as compared to not owning/operating the intellectual property.

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For all debtor company intellectual property valuations, analysts consider all of the generally accepted property valuation approaches. Each has the same objective: to arrive at a defined value indication for the debtor company's intellectual property.

Alternatively, the debtor company may expect a lower level of costs—such as capital costs, investment costs, or operating costs (expenses)—by owning/operating the intellectual property as compared to not owning/operating the intellectual property.

2) Valuation methods that estimate the present value of actual or hypothetical license royalty income—that is, these methods estimate the amount of actual or hypothetical royalty income that the debtor company (as licensor) would generate from the outbound license of the use of the subject intellectual property.
3) Valuation methods that estimate a residual measure of intellectual property income—that is, these methods typically start with the debtor company overall business enterprise income. Next, the analyst identifies all of the tangible assets and routine intangible assets (other than the subject intellectual property) that are used in the debtor company's overall business.

   These assets are typically called *contributory assets*. The analyst then multiples a fair rate of return times the value of each of the contributory assets. The product of this multiplication is the fair return on all of the contributory assets.

   The analyst then subtracts the fair return on the contributory assets from the business enterprise total income. This residual (or excess) income is the income related to the subject intellectual property.
4) Valuation methods that rely on a so-called profit split—that is, these methods typically also start with the debtor company business enterprise total income. The analyst then allocates or "splits" this total income between (a) the debtor company's tangible assets and routine intangible assets and (b) the subject intellectual property.

   The profit split percent (e.g., 20 percent, 25 percent, etc.) to the intellectual property is typically based on the analyst's functional analysis of the debtor company business operations. This functional analysis identifies the relative importance of (a) the intellectual property and (b) the routine (or contributory) assets—to the production of the debtor company business total income.
5) Valuation methods that quantify comparative income—that is, these methods compare the debtor income to a benchmark measure of income that, presumably, does not benefit from the use of the intellectual property.

   Such benchmark income measures typically include (a) the debtor company income before the intellectual property development, (b) industry average income levels, or (c) selected guideline publicly traded company income levels. One typical measure of income for these comparative analyses is the EBIT margin.

   When publicly traded companies are used as the comparative income benchmark, the method is sometimes called the *comparable profit margin method*.

All of these income approach valuation methods can be applied using either (1) the direct capitalization procedure or (2) the yield capitalization procedure.

In the direct capitalization procedure, the analyst:

1) estimates a normalized income measure for one future period (typically, one year) and
2) divides that measure by an appropriate investment rate of return.

The appropriate investment rate of return is called the *direct capitalization rate*. The direct capitalization rate may be derived for:

1) a perpetuity time period or
2) a specified finite time period.

This selection of the capitalization period depends on the analyst's estimate of the intellectual property's expected UEL. Typically, the analyst concludes that the intellectual property has a finite expected UEL. In that case, the analyst may use the yield capitalization procedure. Or, the analyst may use the direct capitalization procedure with a limited life direct capitalization rate. Mathematically, the limited life capitalization rate is typically based on a present value of annuity factor (PVAF) for the intellectual property's expected UEL.

In the yield capitalization procedure, the analyst projects the appropriate income measure for several future time periods. The discrete time period is typically based on the intellectual property's expected UEL. This income projection is converted into a present value by the use of a present-value discount rate. The present-value discount rate is the investor's required rate of return—or yield capitalization rate—over the expected term of the income projection.

The result of either the direct capitalization procedure or the yield capitalization procedure is the income approach value indication for the debtor's intellectual property.

Finally, **Exhibit 1** on the next page presents an illustrative example of an income approach intellectual property valuation analysis. In this example, the analyst is retained to estimate the fair market value of the Gamma Debtor Company (Gamma) intellectual property. The intellectual property is the

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EXHIBIT 1

Gamma Debtor Company
Fair Market Value
Delta Pharmaceutical Product Patent Valuation
Income Approach – Multiperiod Excess Earnings Method
Valuation Summary
As of January 1, 2020

		Pro Forma Years								
Delta Product Patent Valuation Variables	**12/31/20 $000**	**12/31/21 $000**	**12/31/22 $000**	**12/31/23 $000**	**12/31/24 $000**	**12/31/25 $000**	**12/31/26 $000**	**12/31/27 $000**	**12/31/28 $000**	**12/31/29 $000**
Gamma Total Product Line Projected Revenue	4,643,232	4,450,217	4,184,750	3,880,112	3,548,858	3,548,858	3,548,858	3,548,858	3,548,858	3,548,858
Annual Growth Rate Percent	–1.2%	–4.2%	–6.0%	–7.3%	–8.5%	0.0%	0.0%	0.0%	0.0%	0.0%
Customer Retention Rate	77%	55%	46%	35%	27%	19%	15%	11%	9%	7%
Estimated Delta Products Revenue Attrition Rate [a] 23%										
Revenue Attributable to the Delta Product Patent	3,575,289	2,604,350	1,849,994	1,289,821	883,047	679,946	523,559	403,140	310,418	239,022
Annual Growth Rate Percent [b]	NA	–27.2%	–29.0%	–30.3%	–31.5%	–23.0%	–23.0%	–23.0%	–23.0%	–23.0%
EBITDA	1,573,127	1,145,914	813,997	567,521	388,541	299,176	230,366	177,382	136,584	105,170
EBITDA Profit Margin [c]	44%	44%	44%	44%	44%	44%	44%	44%	44%	44%
Less: Depreciation/Amortization Expense	793,018	552,967	375,423	248,354	160,263	123,402	95,020	73,165	56,337	43,380
% of Revenue [d]	22.2%	21.2%	20.3%	19.3%	18.1%	18.1%	18.1%	18.1%	18.1%	18.1%
EBIT	780,109	592,947	438,575	319,167	228,278	175,774	135,346	104,216	80,247	61,790
EBIT Profit Margin	21.8%	22.8%	23.7%	24.7%	25.9%	25.9%	25.9%	25.9%	25.9%	25.9%
Less: Income Taxes @ 37%	288,640	219,390	162,273	118,092	84,463	65,036	50,078	38,560	29,691	22,862
Net Income	491,469	373,557	276,302	201,075	143,815	110,738	85,268	65,656	50,556	38,928
Net Income Profit Margin	13.7%	14.3%	14.9%	15.6%	16.3%	16.3%	16.3%	16.3%	16.3%	16.3%
Plus: Depreciation/Amortization Expense	793,018	552,967	375,423	248,354	160,263	123,402	95,020	73,165	56,337	43,380
Less: Contributory Asset Charge (CAC):										
Working Capital Assets CAC [e]	27,530	20,053	14,245	9,932	6,799	5,236	4,031	3,104	2,390	1,840
Tangible Assets CAC [f]	(823,022)	(599,454)	(425,589)	(296,467)	(202,736)	(156,107)	(120,202)	(92,556)	(71,268)	(54,876)
Routine Intangible Assets CAC [g]	(164,756)	(123,965)	(91,524)	(66,472)	(47,625)	(36,671)	(28,237)	(21,742)	(16,742)	(12,891)
Equals: Patent Excess Earnings	324,239	223,159	148,856	96,422	60,516	46,598	35,880	27,627	21,273	16,381
Discounting Periods [h]	0.5000	1.5000	2.5000	3.5000	4.5000	5.5000	6.5000	7.5000	8.5000	9.5000
Present Value Factor @ 11%	0.9492	0.8551	0.7704	0.6940	0.6252	0.5633	0.5075	0.4572	0.4119	0.3710
Present Value of Patent Excess Earnings	307,767	190,823	114,679	66,917	37,834	26,249	18,209	12,631	8,762	6,077
Total Present Value of Patent Excess Earnings	789,949									
Indicated Fair Market Value of Delta Product Patent	790,000									

Note: These data are hypothetical and are presented for illustrative purposes only.

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EXHIBIT 1 ENDNOTES

[a] Considers the historical weighted revenue decay rates for the Delta patented product revenue.

Delta Product Revenue	2017	2018	2019	Average
Weighted Annual Revenue Decay Rate	23.4%	23.6%	23.3%	23.4%

[b] Represents 77% of Delta product revenue in 2020 based on the estimated attrition rate. Thereafter, Delta product revenue is decreased annually based on (1) the estimated attrition rate and (2) the negative annual growth rate.

[c] The projected 2024 EBITDA profit margin is maintained after 2024.

[d] The projected 2024 depreciation expense as a percent of revenue is maintained after 2023.

[e] Based on (1) working capital requirement for the Delta product line and (2) the return on working capital estimated based on the Gamma Debtor Company 11% weighted average cost of capital (WACC). This CAC calculation is presented below.

Gamma Working Capital Assets CAC Analysis

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Working Capital – % of Total Gamma Revenue	–7%	–7%	–7%	–7%	–7%	–7%	–7%	–7%	–7%	–7%
Working Capital Requirement (times the Delta product revenue)	(250,270)	(182,305)	(129,500)	(90,287)	(61,813)	(47,596)	(36,649)	(28,220)	(21,729)	(16,732)
CAC – Return on Working Capital Assets 11%	(27,530)	(20,053)	(14,245)	(9,932)	(6,799)	(5,236)	(4,031)	(3,104)	(2,390)	(1,840)

[f] The tangible asset capital charge calculation has two distinct components: (1) the capital expenditure investments needed to generate the revenue attributable to the Delta product sales and (2) a fair rate of return multiplied by the tangible assets that are used in the generation of the patented product revenue.
The capital expenditure is based on (1) 22% of revenue (the historical capital expenditure ratio) times the projected revenue attributed to the Delta product patent.
The fair rate of return on revenue is based on the 11% WACC multiplied by the total tangible asset investment. This CAC calculation is presented below:

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Net Tangible Assets as % of Total Gamma Revenue (see Ex. 2)	113%	113%	113%	113%	113%	113%	113%	113%	113%	113%
Tangible Assets Requirement (times Delta product line revenue)	4,038,767	2,941,962	2,089,816	1,457,025	997,520	768,090	591,430	455,401	350,659	270,007
Return on Tangible Assets 11%	444,264	323,616	229,880	160,273	109,727	84,490	65,057	50,094	38,572	29,701

[g] The routine intangible assets contributory asset charge (CAC) as percent of consolidated revenue multiplied by the revenue attributable to the Delta patented product line (see Exhibit 2).

[h] Calculated as if the cash flow (i.e., excess earnings) is received at midyear.

Note: These data are hypothetical and are presented for illustrative purposes only.

patent on the Delta pharmaceutical product. The appropriate valuation date is January 1, 2020. Based on a highest and best use (HABU) analysis, the analyst concluded that the appropriate valuation premise is value in continued use. Based on the quantity and quality of available data, the analyst decided to apply the income approach and the multiperiod excess earnings method (or MEEM). Because the Delta patent product revenue is expected to change at a nonconstant rate over time, the analyst decided to use the yield capitalization procedure in the application of the MEEM valuation method.

Gamma owns the patent that is used to manufacture the Delta pharmaceutical product line. Based on the remaining legal life of the Delta patent and on the Delta product line revenue decay rate (considering the effect of a competitive drug product), the analyst estimates a 10-year expected UEL for the Delta patent.

Gamma management provided the analyst with a financial projection for the overall Gamma product line—that includes the Delta product revenue. The analyst performed a revenue decay rate analysis related to the Delta product in order to conclude a Delta patent revenue growth rate (or, in this case, a revenue decay rate).

Exhibit 1 presents the projection of the Delta product revenue and Delta product profit over its 10-year expected UEL. The analyst estimated an appropriate contributory asset charge (or CAC) on all of the Gamma contributory assets, including working capital assets, tangible assets, and routine (nonpatent) intangible assets. This CAC analysis is summarized in **Exhibit 2** on the next page.

The analyst has concluded that Gamma has an 11 percent weighted average cost of capital (WACC). Therefore, the analyst applied the 11 percent WACC as the Gamma present-value discount rate.

Based on the income approach and MEEM valuation analysis summarized in Exhibit 1, the analyst estimated that the fair market value of the Delta pharmaceutical product patent, as of January 1, 2020, was $790 million.

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EXHIBIT 2

Gamma Debtor Company
Fair Market Value
Delta Pharmaceutical Patent Valuation
Income Approach – Multiperiod Excess Earnings Method
Contributory Asset Charge Analysis

Gamma Tangible Assets Contributory Asset Charge:	FYE 12/31/18 $000
Beginning Tangible Assets [a]	12,034,000
Capital Expenditures [a]	1,162,971
Depreciation Expense [a]	(2,249,209)
Net Tangible Assets	10,947,762
Total Gamma Revenue [a]	9,691,426
Net Tangible Assets as % of Total Gamma Revenue	113%

Gamma Routine Intangible Assets Contributory Asset Charge:	[a] Fair Market Value $000	[b] Estimated Required Rate of Return	Annual Contributory Asset Return $000
Trademarks/Trade Names	970,000	11%	106,700
Internally Developed Computer Software Systems	2,510,000	11%	276,100
Trained and Assembled Workforce	580,000	11%	63,800
Total Contributory Intangible Assets			446,600

	12/31/19 $000	12/31/20 $000	12/31/21 $000	12/31/22 $000	12/31/23 $000
Total Gamma Revenue [a]	9,691,426	9,382,534	9,027,219	8,665,762	8,280,712
Intangible Assets Contributory Asset Charge (from above)	446,600	446,600	446,600	446,600	446,600
Intangible Assets Contributory Asset Charge as % of Total Gamma Revenue	4.6%	4.8%	4.9%	5.2%	5.4%

[a] From the Gamma Debtor Company business plan.
[b] Based on the Gamma Debtor Company WACC.

Note: These data are hypothetical and are presented for illustrative purposes only.

VALUATION SYNTHESIS AND CONCLUSION

In the valuation synthesis and conclusion, the analyst considers the following question: Do the selected valuation approach(es) and method(s) accomplish the analyst's assignment? That is, do the selected approach and the selected method actually quantify the intended objective of the analysis, such as:

- a defined value,
- a transaction price,
- a third-party license rate,
- an arm's-length intercompany transfer price,
- a damages measurement,
- an intellectual property bundle exchange ratio, or
- an opinion on the intellectual property transaction fairness?

With regard to a valuation analysis, the analyst also considers if the selected valuation approach and method analyze the appropriate intellectual property bundle of legal rights. The analyst also considers if there were sufficient empirical data available to perform the selected valuation approach and method.

The valuation synthesis considers if there were sufficient data available to make the analyst comfortable with the analysis conclusion. The analyst may also consider if the selected approach and method will be understandable to the intended audience for the valuation.

The analyst also considers which valuation approaches and

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methods deserve the greatest consideration with respect to the intellectual property's expected UEL. The intellectual property's expected UEL is an important consideration in each valuation approach. In the income approach, the expected UEL affects the projection period for the intellectual property income subject to either yield capitalization or direct capitalization. In the cost approach, the expected UEL affects the total amount of obsolescence, if any, from the estimated cost measure—whether that be the intellectual property reproduction cost new or replacement cost new. In the market approach, the expected UEL affects the selection, rejection, and/or adjustment of the comparable or guideline sale or license transactional data.

The following factors influence the analyst's consideration of the intellectual property's expected UEL:

- legal factors
- contractual factors
- functional factors
- technological factors
- economic factors
- analytical factors

Each of these factors is normally considered in the analyst's UEL estimation. Typically, the life factor that indicates the shortest UEL conclusion deserves the primary consideration in the bankruptcy-related valuation synthesis and conclusion.

Ultimately, the analyst applies professional judgment to weigh the various valuation approach and method value indications in order to reach a final value conclusion. The analyst's weighting of the value indications (whether quantitative or qualitative) is based on:

- the analyst's confidence in the quantity and quality of available data,
- the analyst's level of due diligence performed on those data,
- the relevance of the valuation method to the debtor company intellectual property's life cycle stage and degree of marketability, and
- the degree of variation in the range of the value indications.

Based on the valuation synthesis, the intellectual property final value conclusion can be a point estimate (which is typical for fair market value valuations) or a value range (which is typical for transaction negotiations or proposed license/sale transaction fairness opinions).

ATTRIBUTES OF AN EFFECTIVE VALUATION EXPERT REPORT

There are numerous objectives of any intellectual property valuation report that is prepared within a bankruptcy controversy environment.

First, the analyst wants to persuade the expert report reader (whether the reader is a potential transaction participant, the DIP management, a creditor, counsel for any party, a judge or other finder of fact, etc.). And, second, the analyst wants to defend the intellectual property value conclusion.

In order to accomplish these objectives, the content and the format of the valuation report should demonstrate that the analyst:

1) understood the specific intellectual property valuation assignment;
2) understood the debtor company subject intellectual property and the subject bundle of legal rights;
3) collected sufficient debtor company financial and operational data;
4) collected sufficient industry, market, and competitive data;
5) documented the specific intellectual property economic benefits to the debtor company;
6) performed adequate due diligence procedures related to all available data;
7) selected and applied all applicable income approach, market approach, and cost approach valuation methods; and
8) reconciled all value indications into a final value conclusion.

The final procedure in the entire bankruptcy controversy analysis is for the analyst to defend the value conclusion in a replicable and well-documented expert report.

The written expert report will typically:

- explain the intellectual property valuation assignment,
- describe the subject debtor company intellectual property and the subject bundle of legal rights,
- explain the selection of (and the rejection of) all generally accepted valuation approaches and methods,
- explain the selection and the application of all specific analysis procedures,
- describe the analyst's data gathering and due diligence procedures,
- list all documents and data considered by the analyst,
- include copies of all documents that were specifically relied on by the analyst,
- summarize all of the qualitative analyses performed,
- include schedules and exhibits documenting all of the quantitative analyses performed,
- avoid any unexplained or unsourced analysis variables or analysis assumptions, and
- allow the report reader to be able to replicate all of the analyses performed.

In order to encourage the reader's acceptance of the valuation conclusion, the expert report should be:

- clear, convincing, and cogent;
- well-organized, well-written, and well-presented; and
- free of grammatical, punctuation, spelling, and mathematical errors.

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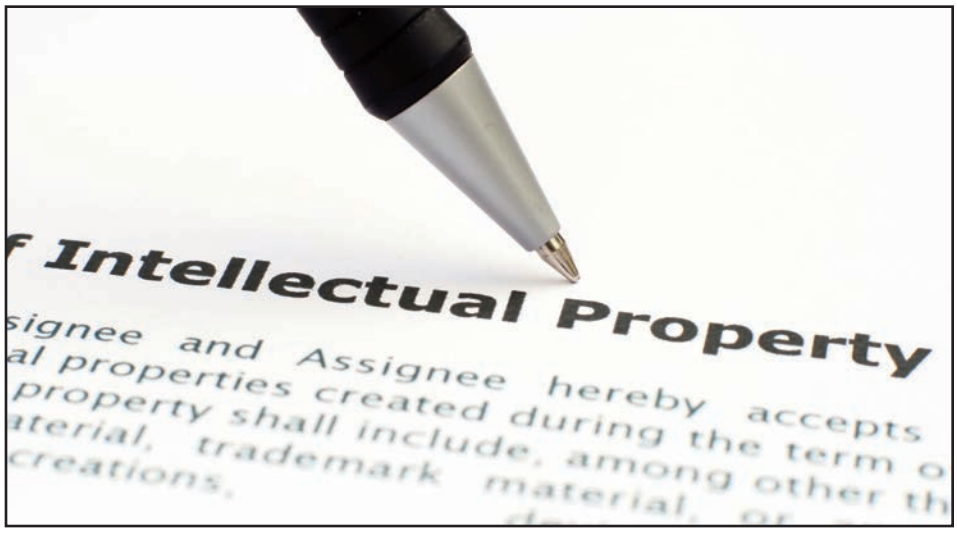
In summary, the effective (i.e., persuasive) intellectual property valuation report will tell a narrative story that:

1) defines the analyst's assignment,
2) describes the analyst's data gathering and due diligence procedures,
3) justifies the analyst's selection of the generally accepted intellectual property approaches, methods, and procedures,
4) explains how the analyst performed the valuation synthesis and reached the final value conclusion, and
5) defends the analyst's intellectual property value conclusion.



WHO SHOULD PERFORM THE INTELLECTUAL PROPERTY VALUATION

An important consideration for any bankruptcy party-in-interest—and counsel—is: What type of expert should perform the debtor company intellectual property valuation? There are many categories of professionals who may perform intellectual property valuation analyses. These various categories of experts include the following:

- accountants
- economists
- licensing executives
- intellectual property consultants
- industry specialists
- analysts

Typically, both the bankruptcy party-in-interest and counsel will be involved in the decision regarding which category of expert to retain. Typically, the party-in-interest and counsel need to decide on the appropriate category of professionals before they can interview and retain an individual expert.

Some parties may consider the relative costs of the professional service in selecting which category of expert to retain. However, the "cost" of being wrong in this decision process is typically much greater than the actual out-of-pocket expense of the expert's fee. Whether the bankruptcy party-in-interest and counsel need the intellectual property valuation for bankruptcy-related transaction, financing, or litigation purposes, they should retain the most qualified professional possible.

Because the effectiveness of the valuation analysis and expert report influences the decision of any buyer, seller, lender, licensor, licensee, judicial finder of fact, and so on, the party-in-interest and counsel should not be concerned about finding a budget-priced expert.

Each of the above-listed categories of professionals has strengths and weaknesses as an intellectual property valuation expert. One category of analyst may be preferred for one type of assignment (say, negotiating a DIP intellectual property license agreement) over another type of assignment (say, providing testifying expert services in a debtor company solvency dispute).

Accountants

Accountants (particularly CPAs) typically have a great deal of credibility with all parties to a bankruptcy controversy. Accountants (particularly CPAs) typically have the credentials to be qualified as a testifying expert. Accountants are typically familiar with the financial accounting and taxation aspect of intellectual property valuation.

Many accountants perform intellectual property valuations according to rule-based methods. These rule-based methods are often promulgated by the FASB or by the Internal Revenue Service. Such methods are particularly applicable for fair value measurement purposes or for Internal Revenue Code Section 482 compliance purposes.

However, some accountants are not particularly comfortable with judgment-based (compared to rule-based) valuation methods and procedures. Intellectual property valuations are a relatively small part of the professional practice of many accountants.

Economists

Economists (particularly Ph.Ds.) also have a great deal of credibility with parties to a bankruptcy controversy. They typically have the credentials to be qualified as testifying experts.

In fact, since valuation analysis is one particular type of economic analysis, many regulatory and taxation authorities (e.g., the Internal Revenue Service) often accept economists as experts. This acceptance is particularly true for intercompany transfer price analysis and for other rules-based intel-

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lectual property analyses.

Economists can sometimes perform very theoretical (and not empirically based) analyses. Economists are not always familiar with the above-described generally accepted valuation approaches, methods, and procedures.

Accordingly, the economist's valuation analyses are sometimes difficult for a layperson to understand. And, these analyses may not stand up to a contrarian challenge within a litigation environment.

Licensing Executives

Licensing executives typically have a great deal of *practical* experience in negotiating and structuring arm's-length intellectual property license agreements. This experience may cross many types of intellectual property and many types of industries.

Licensing executives often have a great deal of *personal* and/or anecdotal evidence regarding intellectual property values, royalty rates, and so forth. However, because it is anecdotal, this evidence often cannot be independently confirmed.

While licensing executives often know how intellectual property valuations are performed, these executives may not know (or be able to explain) why intellectual property valuations are performed that way. Licensing executives often rely on so-called industry rules of thumb and not on the generally accepted valuation approaches, methods, and procedures. Licensing executives are often more familiar with the licensing profession's practices and procedures than they are with the valuation profession's practices and standards.

Intellectual Property Consultants

Intellectual property consultants typically assist their employers and clients to develop strategic plans to maximize the value of intellectual property. These plans often start with the process of identifying the client's intellectual property. These plans often consider the competitive strengths, weaknesses, opportunities, and threats related to the intellectual property. The plans then analyze how the intellectual property is used by the debtor and how it can be commercialized outside of the current owner/operator.

These consultants often assist their employers or clients to finance, license, or otherwise monetize the intellectual property. Many intellectual property consultants prepare more qualitative valuation analyses than quantitative valuation analyses.

Many of the intellectual property analyses are high level (i.e., conceptual) rather than empirical (i.e., practical). These consultants often rely more on "black box" types of analyses and less on the replicable generally accepted valuation approaches, methods, and procedures. These consultants may not subscribe to any promulgated professional standards.

Industry Specialists

Industry specialists typically are not intellectual property specialists. Rather, they are electronics industry specialists, software industry specialists, telecommunications industry specialists, and so on.

Industry specialists are often retired industry executives or consultants who focus on consulting in one or two industries. They often provide industry clients with financial forecasting, strategic planning, competitive analysis, and other consulting expert services.

Often, industry specialists have been involved in business brokerage, business start-up, or bankruptcy transactions in their industry. And, these specialists may perform intellectual property valuations as one of their industry services.

While these industry specialists may know a great deal about their respective industry, they may not know a great deal about intellectual property or about intellectual property valuation. Accordingly, the justification for their valuation analysis and their value conclusion is typically "in my experience"—as opposed to an analysis based on empirical data and recognized (and replicable) valuation profession practices and standards.

Analysts

Valuation analysts may have varying academic or professional backgrounds. Individuals are typically included in this category if they have completed professional training and received professional recognition by one or more of the credentialing professional valuation organizations (VPOs).

These VPOs typically promulgate intangible asset valuation professional standards, conduct both pre-credential training and post-credential continuing professional education courses, and offer comprehensive examination programs leading to a professional credential or accreditation. Such VPOs include the American Institute of Certified Public Accountants (which grants the ABV credential), the American Society of Appraisers (which grants the ASA credential), and the National Association of Certified Valuators and Analysts (which grants the CVA credential).

These professionals typically have the training and the credentials to qualify as testifying experts. These professionals typically apply generally accepted valuation approaches, methods, and procedures. And, these professionals typically subscribe to—and comply with—the generally accepted VPO standards and practices.

Ultimately, the bankruptcy party-in-interest and counsel have to decide which type of professional

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is best suited to conduct the debtor company intellectual property valuation analysis. There should be a match (of experience and expertise) between the selected analyst and the purpose and objective of the bankruptcy controversy assignment. There should also be a match (of personalities and professional philosophies) between the selected analyst and the client.

In the final selection, the type of professional may be less important than the qualifications and the abilities of the individual analyst. Nonetheless, most bankruptcy controversy intellectual property valuations are (at least potentially) subject to a contrarian review.

Therefore, the party-in-interest and counsel should select an intellectual property analyst who can deliver a valuation analysis and valuation expert report (and expert testimony, if needed) that:

1) will convince the intended report (or testimony) audience and
2) will stand up to a rigorous contrarian challenge.

An analyst who has applied generally accepted valuation approaches, methods, and procedures and an analyst who has complied with generally accepted professional standards and practices may be best posed to meet that challenge.

SUMMARY AND CONCLUSION

This discussion considered the various types of intellectual property analyses that an analyst may be asked to perform within a bankruptcy controversy. For purposes of this discussion, the term *intellectual property* includes trademarks and trade names, patents, copyrights, and trade secrets.

For all debtor company intellectual property valuations, analysts consider all of the generally accepted property valuation approaches—the cost approach, the market approach, and the income approach. Each of these valuation approaches has the same objective: to arrive at a defined value indication for the debtor company's intellectual property. Within each of the generally accepted valuation approaches, there are generally accepted valuation methods and procedures that may be appropriate for the particular intellectual property valuation assignment.

The analyst's selection of the specific valuation approaches, methods, and procedures for the debtor company's intellectual property is based on the following factors:

1) the particular characteristics of the intellectual property,
2) the specific bundle of legal rights subject to analysis,
3) the quantity and the quality of available data,
4) the analyst's ability to perform sufficient due diligence related to that data,
5) the purpose and the objective of the specific analysis, and
6) the relevant professional experience and the informed judgment of the individual analyst.

The final value conclusion is typically based on the analyst's synthesis of the value indications from each applicable valuation approach and method.

The generally accepted valuation approaches, methods, and procedures summarized in this discussion are generally relevant to bankruptcy-related intellectual property analyses performed for transaction, financing, strategic planning, taxation, accounting, litigation, and other purposes. Accordingly, it is a best practice for both the bankruptcy party-in-interest and counsel to the bankruptcy proceeding to be familiar with the generally accepted intellectual property valuation approaches and procedures for purposes of:

1) selecting the appropriate analyst,
2) relying on the analyst's value conclusion, and
3) defending the analyst's value opinion and valuation work product.

The analyst should consider the best practices described in the valuation report development discussion. Those best practices should assist the analyst to prepare a well-supported intellectual property valuation report.