

# American Journal of Family Law

VOLUME 33 NUMBER 3 FALL 2019

## Intellectual Property Valuations for Family Law Purposes: Part II of II

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*Part I of this article discussed types of IP and IP analyses, royalty rate data, valuation approaches and methods, data gathering, due diligence, and financial projections.*

*Part II presents an IP valuation illustrative example.*

### INTELLECTUAL PROPERTY VALUATION ILLUSTRATIVE EXAMPLE

Let's consider the application of the RFR method to value a marital estate intellectual property for family law purposes. Wally White and Wilma White are involved in a marital dissolution. One of the issues in the family law dispute is the value of the marital assets on January 1, 2018, the date of the White's separation. Wally White, M.D., developed—and owns the patent on—a very successful pharmaceutical product called Wonder Drug. Wonder Drug is manufactured by Black & White Pharmaceutical Company, LLC ("Black & White"). Dr. White is also a member of the LLC.

Black & White manufactures several pharmaceutical products. The principal product manufactured at the company, however, is the patented and FDA-approved drug called Wonder. Family law counsel retained an independent valuation analyst to value the Wonder intellectual property owned by the White marital estate.

The analyst's valuation objective is to estimate the fair market value of the Wonder pharmaceutical patent and related know-how. The valuation date is January 1, 2018. Fair market value is the statutory definition of value used in the subject jurisdiction

for family law purposes. The analyst's valuation purpose is to assist the finder of fact in any legal dispute involving the White marital dissolution.

The analyst decided to use the market approach and the relief from royalty method to value the Wonder patent and related trade secret know-how.

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## ILLUSTRATIVE ROYALTY RATE SEARCH CRITERIA

The analyst searched for arm's-length intellectual property license agreements from which to extract market-derived royalty rate data to use in the RFR method valuation of the Wonder patent. The analyst selected (and documented) the following criteria for researching CUT intellectual property licenses:

- SIC code 2834, pharmaceuticals industry
- Technology intangible assets and manufacturing/process intangible assets
- Either the licensor or the licensee is a US company
- No geographic territory restrictions
- No restrictions on the type of the agreement (other than it must be patent or technology related)
- License start date must be after January 1, 2013, and the license has to still be in effect as of January 1, 2018

### The Initial License Royalty Rate Search Results

In this illustrative example, the analyst searched both the ktMINE database and the RoyaltySource database to identify pharmaceutical industry patent and technology license agreements. The analyst will use the royalty rate data extracted from the commercial databases to apply the RFR valuation method and to value the Wonder patent intellectual property. Using the ktMINE database, the analyst's initial search identified 72 potential CUT license agreements for further consideration. Using the RoyaltySource database, the analyst requested 30 randomly selected pharmaceutical industry technology license agreements for future consideration. The license royalty rates indicated by the 102 potential CUT licenses ranged from 2 percent of the licensee's product revenue up to 100 percent of the licensee's product sublicense revenue.

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*Some of the potential CUT license agreements were "Goldilocks" licenses.*

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After reviewing each of the 102 pharmaceutical industry technology license agreements, the analyst

noticed that numerous license royalty rates were expressed as:

- A percentage of licensee gross profits
- A percentage of licensee net profits
- Dollars per kilogram of product produced
- A percentage of the license product manufacturing costs
- A fixed dollar amount per time period, or
- A fixed dollar amount for the term of the license

In selecting the appropriate royalty rate to use in the Wonder patent valuation, the analyst had to make sense of over 100 divergent intellectual property license royalty rate data points.

### Types of License Agreements Included in the Commercial Databases

The analyst noted that there were numerous types of intellectual-property-related agreements included in the commercial databases. In order to assemble a reasonable amount of usable pharmaceutical product patent royalty data, the analyst concluded that the following types of agreements could be eliminated (from consideration), adjusted (quantitatively normalized), or assessed (qualitatively normalized):

- Territory production/manufacturing agreements
- Territory product distribution agreements
- Sublicense agreements
- Trademark license agreements
- Intercompany transfer price agreements
- Nonpatent technology licenses
- Intangible asset sale agreements
- Joint product development agreements
- Joint venture commercialization agreements

- Access to product data and library research agreements
- Intellectual property infringement settlement and court order agreements
- Stockholder litigation settlement agreements
- Technical assistance agreements

### **Types of Products Included in the Commercial Databases**

Even though the analyst restricted the database searches to pharmaceutical industry patents, a wide array of license agreements was captured in the intellectual property royalty rate search. To achieve a manageable number of useable royalty rate observations, the analyst concluded that the following products could be eliminated (from consideration), adjusted (quantitatively normalized), or assessed (qualitatively normalized):

- Generic drug products
- Cosmetic products
- Nonhuman drug products
- Medical and surgical device products
- Radiation delivery systems
- Over-the-counter products
- Dietary supplement products
- Nonprescription skin care products
- Multiple pharmaceutical products (multiple product portfolios)
- Multiple patents and know-how (multiple intellectual property portfolios)

### **Types of License Compensation Methods Included in the Commercial Databases**

Ideally, the analyst is searching for license agreements that have a royalty rate expressed as a percent of the licensee's product revenue. Such

royalty rates are easier to apply in the RFR valuation method. Also, such royalty rates would be easy to apply to the RFR valuation of the Wonder patent and related know-how intellectual property. The analyst's initial search of the 102 license agreements, however, produced a very wide range of royalty rate compensation formula, plans, and methods. In order to achieve a reasonable number of useful royalty rate observations, the analyst decided that these license royalty consideration arrangements could be eliminated (from consideration), adjusted (quantitatively normalized), or assessed (qualitatively normalized):

- A profit split percentage of the licensee gross profits
- A profit split percentage of the licensee net profits
- A profit split percentage of the licensee product profits
- A percentage of the sublicensee revenue/income
- A percentage of the licensee product manufacturing costs
- A percentage of the licensee total costs
- A percentage of some specified exit event price or consideration
- A percentage of the FMV assigned to the subject intellectual property
- A dollar amount per unit volume/weight of product produced

The analyst noted that some of these license consideration arrangements could be useful in the application of profit split valuation methods or of cost plus valuation methods. These license consideration methods were not particularly applicable in the application of the RFR valuation method, however. The analyst also noted that, with some supplemental analysis, some of these license consideration arrangements could be converted into a percent of revenue royalty rate equivalent—that could be used in the application of the RFR valuation method.

*Exhibit 8*

White Marital Estate  
Wonder Patent Valuation  
Elimination of Royalty Rate Observations

<b>Intellectual Property Licensors</b>	<b>Intellectual Property Licensee</b>	<b>Intellectual Property License Rights Transferred</b>	<b>License Royalty Consideration Formula</b>
Cypress Pharmaceuticals	Pediatrix	Rights to distribute the product Granisol	\$1,000/month
Allergan	Nektar Therapeutics	Collaboration agreement to develop the product Levadex	50% of the product profits/loss
Arius Pharmaceuticals	Biodelivery Sciences	Rights to the BEMA patent and to develop new related products	\$375,000/quarter
Epicept Corp.	Epicept GmbH	Cooperation agreement to develop Caplene for AML remission treatment	\$2,000/day/employee
Columbia Laboratories	Scientelle	Right to use the patent to develop a diabetes drug for the licensor	150% of the product development expenses—to the licensee
Pharmos Corp.	Reperico Pharmaceuticals	Product development agreement—right to use the patent to develop small molecular drugs	50% of the FMV of an exit (sale) event

*Exhibit 9*

White Marital Estate  
Wonder Patent Valuation  
Adjustment of Royalty Rate Observations

<b>Intellectual Property Licensors</b>	<b>Intellectual Property Licensee</b>	<b>Intellectual Property License Rights Transferred</b>	<b>License Royalty Consideration Formula</b>	<b>Analyst's Quantitative Royalty Rate Adjustment</b>
Glycomed	Paringenix	Patent rights to develop variations of the named products	100% of sublicense revenue	8% of revenue [a]
Keryx Biopharma	Torii Pharma	Right to use patent and technology to manufacture products to treat inflammatory cutaneous disorders	15% of manufacturing cost	7.5% of revenue [b]
Deponed	Solvany Pharma	Right to use patent and technology to develop and manufacture pain medicine delivery device	15% of revenue	7.5% of revenue [c]
Impax Labs	Medicis Pharma	Right to use patents, know-how, and technology to develop products for treatment of oral acne	25% of gross profit	10% of revenue [d]
Columbia Labs	Coventry Pharma	Rights to patents and patent applications to develop small modular immune-pharmaceutical products	50% of pretax profit	7.5% of revenue [e]
DVSA Pharma	River's Edge Pharma	Rights to use patents and technology to develop and manufacture products for stated gastro-intestinal disease	\$5,000,000 plus 25% of gross profit	10% of revenue [f]

## Footnotes:

[a] Assumes that 100% of the sublicense revenue becomes pretax margin; 8% is the average pretax margin in this industry sector.

[b] Manufacturing cost equals about 50% of product revenue in this industry sector.

[c] As a rule of thumb, medical device licenses generally generate about twice the royalty rate as pharmaceutical product licenses.

[d] Gross profit margin is approximately equal to 40% of revenue in this industry sector.

[e] Pretax margin is approximately 15% of revenue in this industry sector.

[f] Gross profit margin is approximately 40% of revenue; the \$5,000,000 upfront payment settled a patent infringement lawsuit between the licensor and the licensee.

### EXAMPLES OF THE ELIMINATION OF ROYALTY RATE NOISE

*Exhibit 8* illustrates several of the many license agreements that the analyst had to eliminate from future consideration. The type of license agreement compensation arrangements did not lend themselves to use in the RFR valuation method. That is, the analyst was searching for intellectual property license agreements where the royalty rate was expressed as a percent of the licensee's pharmaceutical product revenue.

### EXAMPLES OF THE QUANTITATIVE ADJUSTMENT (NORMALIZATION) OF ROYALTY RATE NOISE

The analyst's search produced numerous license agreements that had complex royalty compensation

arrangements. With additional due diligence and research, however, the analyst could adjust the complex royalty arrangements to indicate an equivalent royalty rate expressed as a percent of licensee's revenue. *Exhibit 9* illustrates several of these quantitative adjustments that the analyst made to reduce the "noise" in the raw license agreement royalty rate data.

### EXAMPLES OF QUALITATIVE ASSESSMENT (NORMALIZATION) OF ROYALTY RATE NOISE

The analyst noted that many of the license royalty consideration formula were expressed as a percent of the licensee's product revenue. Some of these licenses were also complex agreements, however. That is, the intellectual property license agreements were tied to manufacturing, joint venture, distribution, or other agreements. In some of the agreements, a

#### *Exhibit 10*

White Marital Estate  
Wonder Patent Valuation  
Assessment of Royalty Rate Observations

Intellectual Property Licensor	Intellectual Property Licensee	Intellectual Property License Rights Transferred	License Royalty Consideration Formula	License Agreement Contract Term	Analyst's Qualitative Royalty Rate Adjustment
Hoffman-La Roche	Meda AB	Rights to patents, trademarks, and all intellectual property, inventory, contracts, and manufacturing technology—in an asset purchase agreement	10% of revenue	6 years	Less than 10% of revenue [a]
Combinatorix	Fovea Pharma	Collaboration agreement—right to collaborate to develop ophthalmic medicine to treat BOE diseases	4% of revenue	10 years	More than 4% of revenue [b]
CIBA Vision	Novartis Pharma	Right to use technology to develop a benzoporphyrin derivative mono acid ring for use in cataract surgery	20% of revenue	10 years	Less than 20% of revenue [c]
Coventry Pharma	Watson Pharma	Right to use patent, trademark, copyrights, regulatory filings, and promotional materials to develop Progesterone products	10% of revenue	Until last intellectual property expires	Less than 10% of revenue [d]
PDL Biopharma	Alexion Pharma	Right to use PDL antibody patent family in the development and manufacture of other licensed pharmaceutical products	4% of revenue	Term of other licenses	More than 4% of revenue [e]
Footnotes:					
[a] The licensee is paying for the acquisition of a going-concern business.					
[b] Both the licensor and the licensee have to contribute to the development of any new drug product.					
[c] Medical devices typically extract higher royalty rates; this license also gives the licensee the right to buy materials from the licensor at cost.					
[d] Includes multiple intellectual property assets and the right to operate a going-concern business.					
[e] Patent can only be used with other licensed products; that contract arrangement also generates license royalty income to the licensor.					

*Exhibit 11*

White Marital Estate  
Wonder Patent Valuation  
Selected Royalty Rate Observations

Intellectual Property Licensor	Intellectual Property Licensee	Intellectual Property License Rights Transferred	License Agreement Contract Term	Licensor Royalty Rate Compensation
Cominatrix	Black & White Plan	Right to use patent and clinical research to adopt Prednisporin to treat glaucoma	6 years	8% of revenue
Cosmo Pharma	Santorus	Right to use patents and know-how to develop products containing Budesonide to treat ulcerative colitis	6 years	7% of revenue
Eli Lilly	United Therapeutics	Right to use patents and technology to develop and commercialize prescription products for treatment of pulmonary hypertension	20 years	6% of revenue
Baxter International	Eleisin Pharma	Right to patent and technology to improve Glufosfamide related to the treatment of cancer	9 years	8% of revenue
Auxilium Pharma	Biospecifics	Right to use BTC patents in the development of the next generation of products to treat Peyronie's Disease	8 years	8.5% of revenue

more fulsome bundle of assets was being licensed. In these cases, the analyst applied experience and judgment—as well as quantitative industry research—to qualitatively assess and adjust the license royalty rate arrangement. As illustrated in *Exhibit 10*, many of these assessments involve the analyst's royalty rate conclusion that is "less than" or "more than" the CUT license agreement stated royalty rate.

#### EXAMPLES OF SELECTED CUT ROYALTY RATE DATA FOR THE WONDER VALUATION

The analyst noted that some (although relatively few) of the potential CUT license agreements were, in fact, "Goldilocks" licenses. That is, for the most part, these selected license agreements were "just right." That is, they provided particularly useful market-derived arm's-length agreement royalty rate data that could be used to value the White marital estate intellectual property. *Exhibit 11* presents the CUT licenses that the analyst selected for use in the RFR method valuation of the Wonder patent and proprietary know-how intellectual property.

#### APPLICATION OF THE RELIEF FROM ROYALTY VALUATION METHOD

At this point in the analysis, the analyst has accessed intellectual property license databases,

developed license agreement selection criteria, selected and reviewed 102 license agreements, and assembled (and normalized) empirical royalty rate data. Based on the analyst's assessment of the market-derived royalty rate data, the analyst has to answer the question: what is the appropriate market-derived royalty rate to use in the Wonder patent valuation? That is, what is the market-derived royalty rate for the valuation of the White marital estate intellectual property?

As part of the RFR method valuation, the analyst eliminated royalty rate data that did not present meaningful license royalty consideration. Then, the analyst adjusted the royalty rate data to indicate an adjusted range of royalty rates of 7.5 percent to 10 percent of licensee product revenue. This adjustment procedure produced the following royalty rate indications:

- Mean royalty rate—8.4 percent of revenue
- Median royalty rate—8 percent of revenue
- Mode royalty rate—7.5 percent of revenue

As illustrated above, the analyst assessed royalty rate data that indicated a greater than/less than royalty rate range. Those data were the result of the analyst's qualitative assessment of the royalty rate noise in the entire sample of intellectual property licenses. With regard to the Wonder intellectual



*Exhibit 12*

White Marital Estate  
Wonder Patent Valuation  
Market Approach—Relief from Royalty Valuation Method  
As of January 1, 2018  
(in \$ millions)

Wonder Patent and Related Know-How Valuation Analysis [a]	Projection Period								
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9
Wonder Product Expected Revenue Growth Rate [b]	10%	10%	10%	0%	0%	0%	-12%	-12%	-12%
Wonder Revenue Amount (year 0 base revenue = 400)	440	484	532	532	532	532	469	412	363
Selected Patent License Royalty Rate	<u>8%</u>	<u>8%</u>	<u>8%</u>	<u>8%</u>	<u>8%</u>	<u>8%</u>	<u>8%</u>	<u>8%</u>	<u>8%</u>
Projected "Relief from Royalty" License Expense (rounded)	35	39	43	43	43	43	38	33	29
Projected Income Tax Expense (40% income tax rate) [c]	<u>14</u>	<u>16</u>	<u>17</u>	<u>17</u>	<u>17</u>	<u>17</u>	<u>15</u>	<u>13</u>	<u>12</u>
Projected Net "Relief from Royalty" License Expense (rounded)	21	23	26	26	26	26	23	20	18
Present Value Discount Factor (at a 12% rate, using the midyear convention) [d]	<u>.94</u>	<u>.84</u>	<u>.75</u>	<u>.67</u>	<u>.60</u>	<u>.54</u>	<u>.48</u>	<u>.43</u>	<u>.38</u>
Present Value of "Relief from Royalty" License Expense	20	19	20	17	16	14	11	9	7
Total Present Value of "Relief from Royalty" License Expense	<u>133</u>								
Fair Market Value of the Wonder Product Patent (rounded)	<u>130</u>								
Footnotes:									
[a] The expected RUL of the Wonder product patent is 9 years; this RUL is based on the Black & White management's projection of the Wonder product economic life. Black & White management is currently developing a replacement product. Also, there are competitive pharmaceutical products that are beginning to enjoy market acceptance in competition to Wonder.									
[b] The analyst derived the projected revenue growth/decline rates (in conjunction with Black & White management) based on an analysis of similar drug product revenue growth/decline rates during the last half of their respective product patent life cycles.									
[c] Assumes a 40% combined (federal and state) effective income tax rate, consistent with the Black & White income tax rate.									
[d] Assumes a 12% after-tax present value discount rate, consistent with the Black & White after-tax weighted average cost of capital.									

property, the greater than/less than range of royalty rates indicated the following:

- Royalty rate greater than 4 percent of revenue
- Royalty rate less than 20 percent of revenue
- Modes—greater than 4 percent of revenue, less than 10 percent of revenue

Based on the most comparable of the sample of license agreements, the analyst selected CUT royalty rate data that indicated a range of 6 percent to 8.5 percent of revenue. These selected license agreements are sometimes referred to as "Goldilocks" agreements. Based on the similarities of these selected licenses to the Wonder intellectual property, these individually selected agreements are "just right." The final selection of CUT license agreements indicated the following royalty rate range:

- Royalty rate mean—7.5 percent of revenue
- Royalty rate median—8 percent of revenue
- Royalty rate mode—8 percent of revenue

Based on all of the above-described empirical royalty rate data, the analyst selected a royalty rate of 8 percent of revenue for use in the RFR method valuation of the Wonder intellectual property.

In addition to applying the selection criteria described above, the analyst considered the following factors in the final selection of the 8 percent of revenue royalty rate for the Wonder intellectual property valuation:

- The relative profitability of the Wonder product compared to the CUT patent products, including consideration of the relative profit margins of Wonder versus the CUTs and the relative returns on investment of Wonder versus the CUTs
- The relative total size of the Wonder market compared to the market sizes of the CUT patent markets
- The relative growth rate of the Wonder market compared to the growth rates of the CUT patent markets
- The relative position of the Wonder product in its market compared to relative position of the CUT patent products in their respective markets
- The relative availability of substitutes for the Wonder product compared to relative availability of substitutes for the CUT patent products
- The relative age of the Wonder product in its life cycle compared to relative ages of the CUT patent products in their life cycles

The analyst recognized that, ideally, these comparative analyses are prepared on a patent-to-patent (or product-by-product) basis. Based on data constraints, however, these comparative subject/CUT intellectual property analyses may have to be performed on either (1) a company-to-company basis or (2) an industry-to-industry basis.

## RELIEF FROM ROYALTY VALUATION METHOD ILLUSTRATIVE EXAMPLE

*Exhibit 12* presents the analyst's application of the RFR valuation method analysis. The analyst used this method to estimate the fair market value of the Wonder patent and related know-how. This intellectual property valuation is based on the market-derived intellectual property license analysis described above.

The analyst derived the other valuation variables use in the RFR analysis after rigorous due diligence and consultation with Black & White management. A summary description of the selected valuation variables is presented in the footnotes to *Exhibit 12*.

## RELIEF FROM ROYALTY VALUATION METHOD SUMMARY

Family law counsel retained the analyst to estimate the fair market value of the Wonder intellectual property (patent and related know-how trade secrets), as of January 1, 2018. This intellectual property is owned by the White marital estate and is operated by Black & White.

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*IP can be commercialized.*

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The analyst concluded that the market approach and the relief from royalty method was most appropriate to value the Black & White intellectual property. The analyst performed a comprehensive search—and a rigorous analysis—of CUT pharmaceutical product patent license agreements. Based on both quantitative and qualitative factors, the analyst selected a market-derived royalty rate to apply to the RFR method valuation. Working with Black & White management, the analyst developed the other valuation variables needed to complete the RFR method valuation.

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*IP could be transferred between the parties.*

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Based on the results of the RFR method valuation, and as summarized in *Exhibit 12*, the analyst concluded that the fair market value of the Wonder



intellectual property, as of January 1, 2018, was: \$130 million. Family law counsel included this intellectual property valuation as part of the overall valuation of the White marital estate.

## INTELLECTUAL PROPERTY VALUATION ANALYST CAVEATS

There are several caveats that family law counsel should be aware of with regard to the use of the RFR method to value company intellectual property for family law purposes. First, analysts should use several intellectual property license databases, if possible. Of course, there is a cost to using multiple databases. The use of several databases, however, typically results in a more comprehensive sample of CUT license agreements.

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*The relief from royalty method is commonly used.*

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Second, it is also important for the analyst to understand what intellectual property is included in the valuation subject, what owner/operator industry is included in the valuation subject, and what bundle of intellectual property legal rights is included in the valuation subject.

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*To maintain confidentiality, trade secrets are rarely licensed.*

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Third, it is a best practice for the analyst to print and read each individual license agreement that may provide empirical royalty rate data.

Fourth, it is also a best practice for the analyst to examine each selected license agreement for terms and conditions that may justify the elimination, adjustment, or assessment of—or the analyst's reliance on—the market-derived license royalty rate data.

Fifth, the analyst should be aware that the commercial license databases may include documents other than arm's-length intellectual property license agreements. For example, these commercial databases may also include the following types of transactional documents related to intellectual property:

- Business acquisition asset purchase agreements
- Intangible property intercompany transfer price agreements
- Product sale, manufacturing, or distribution agreements
- Joint venture, collaboration, development, etc., agreements

Sixth, the analyst should be aware that there are various types of license royalty compensation formula that are not particularly useful to an RFR valuation method royalty rate analysis. That is, these royalty formula present compensation methods other than a royalty expressed as a percent of licensee revenue. Examples of these other license compensation formula include the following:

- A dollar amount per unit sold or produced
- A dollar amount per time period
- Equity (stock shares) as a license payment
- A percentage of licensee gross profit or net profit

Seventh, and finally, the analyst should be prepared to eliminate, adjust, and assess the market-derived license royalty rate data in order to extract the most meaningful intellectual property pricing metrics. Intellectual property valuation analysts should be comfortable with this generally accepted valuation procedure. For example, real estate appraisers regularly eliminate, adjust, and assess empirical sales data in performing real estate appraisals. Also, business valuation analysts regularly eliminate, adjust, and assess guideline company pricing multiple data in performing market approach business valuations. Therefore, the procedure to eliminate, adjust, and assess empirical royalty rate data should be a well-used tool in the intellectual property valuation analyst's toolbox.

## THE EFFECTIVE INTELLECTUAL PROPERTY VALUATION REPORT

In addition to preparing the family law intellectual property valuation analysis, the analyst

typically has to prepare a narrative valuation report. In order to encourage the intellectual property valuation report reader's acceptance, the effective report should be:

- Clear, convincing, and cogent
- Well organized, well written, and well presented
- Free of grammar, punctuation, spelling, and mathematical errors
- Procedurally and mathematically replicable, without the use of any unexplained or unsourced valuation variables

Particularly with regard to an intellectual property valuation report prepared for family law purposes, the persuasive report should tell a narrative story that:

- Defines the valuation analyst's assignment
- Describes the analyst's data gathering and due diligence procedures
- Justifies the analyst's selection of (and rejection of) the generally accepted intangible asset valuation approaches, methods, and procedures
- Explains how the analyst performed the valuation reconciliation and synthesis and how the analyst reached the final valuation conclusion
- Defends the analyst's intellectual property value conclusion
- Describes all of the data sources that the analyst relied on in the valuation (and includes copies of nonpublic source documents)

Particularly with regard to an intellectual property valuation report prepared for family law purposes, an effective report will avoid these common errors:

- Failure to apply the defined standard of value
- Failure to apply the defined premise of value
- Analytical internal inconsistencies

- Arithmetic errors in the intellectual property valuation analysis
- Insufficient support for the selected valuation variables
- Reliance on industry or other rules of thumb
- Insufficient data and inadequate market research
- Inadequate due diligence procedures

In particular, expert reports prepared for family law controversy purposes should be comprehensive. Typically, all of the analyst's valuation procedures and thought processes will be documented in the expert report. Analysts who prepare valuation analyses in family law controversy cases may be familiar with the valuation report guideline "if it's not in your report, you didn't do it."

## SUMMARY AND CONCLUSION

Intellectual property is often included in the marital estate. The intellectual property may be owned directly by the invention, author, artist, etc. Or, the intellectual property may be owned indirectly through a closely held company or professional practice. In either case, the intellectual property value may be a material component of the value of the marital estate.

Accordingly, family law counsel may have to retain valuation analysts, rely on such analysts, or cross-examine such analysts with regard to the valuation of the marital estate intellectual property.

Analysts often use the market approach—and the relief from royalty method—to value intellectual property for family law purposes. The RFR method is based on the collection and analysis of third-party license agreements regarding the arm's-length license of guideline or comparable intellectual property. Analysts often access commercial databases to extract such CUT license agreements.

Analysts (and legal counsel) understand that there is a lot of "noise" included in the intellectual property license database royalty rate raw data. Nonetheless, analysts can effectively use these empirical royalty rate data to perform intellectual

property valuations for family law (and for other) purposes.

Analysts often use the “eliminate, adjust, and assess” procedures summarized in this discussion to reach a reasonable range of royalty rates—and a supportable intellectual property royalty rate conclusion. Analysts should not use the so-called “Goldilocks” procedure, however. That is, analysts should not (1) select a predetermined intellectual property royalty rate that is “just right” for the subject valuation and then (2) eliminate, adjust, and assess the empirical data in order to justify the predetermined “just right” intellectual property royalty rate.

This article focused on what family law counsel need to know about the application of the relief from royalty method of the market approach to

value intellectual property. In applying the RFR valuation method, analysts typically access various commercial databases. These databases are used to extract market-derived royalty rate from the arm’s-length licenses of intellectual property assets that are sufficiently similar to the marital estate intellectual property. These arm’s-length intellectual property licenses are frequently referred to as comparable uncontrolled transactions—or CUTs.

The discussion also presented an illustrative example of the application of the RFR method to value a marital estate intellectual property. This illustrative example considered the analyst’s valuation of the hypothetical Wonder patent and related know-how intellectual property for purposes of the White marital dissolution.

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