

THE VALUE AND VALUATION OF TRADE MARKS

by Owen H Dean

A brand has been described as the marketing asset that exists in customers' minds. There can indeed be no more vivid and vibrant evidence of the creativity and energy of modern commercial life than the flow of ideas expressed in brands and branding.

The value of trade marks and other forms of intellectual property such as patents, designs and copyright is particularly evident in two contexts. The first is the contribution which intellectual property makes to economic growth in general and to commerce in particular. The second is the contribution which it makes to the wealth of specific stakeholder groups in society by generating jobs, as well as shareholder and consumer value. Without intellectual property the world would be a much poorer place.

Who owns ideas? Although the gossamer idea from which a brand is born is the patrimony of all mankind it may nevertheless have commercial value for a single person or company. Provided that an idea complies with the requirements of the law the commercial rights of the owner of an idea will be protected and others will be prevented from exploiting that idea. In the case of brands this is achieved by protecting a brand as a trade mark. The value of the brand consists both of the trade mark and the equity attaching to the brand. Legal protection of trade marks is essential if brands are to serve their purpose and fulfil their economic function. Intellectual property law in relation to brands is indeed of major importance to every firm's marketing function.

Trade marks are assets

In 1997 the three top American brands were worth close to US\$120 billion. Although intellectual property assets are a unique kind of asset they

nevertheless have many characteristics in common with ordinary physical assets. Some of these characteristics are the following:

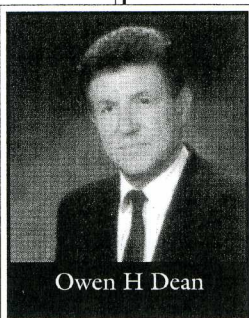
- their value is financially quantifiable
- they can be acquired and alienated
- they are subject to various kinds of risk
- they must be accounted for
- they play a role in achieving shareholder value
- they are often critical to the company's competitive edge
- their value can easily exceed the value of the company's physical assets
- they have a measurable productivity
- they attract the interest of the tax man.

Characteristics which distinguish trade marks from other assets must also be recognised. A trade mark may, for example, be used in such a manner as to become the common name by which the goods are known or, in other words, it may become generic and fall into the public domain. In such a case the manufacturer might lose all rights in the

trade mark. Many words in the English language, such as aspirin, linoleum, and escalator, to name only a few, were originally trade marks signifying the product of one source. Thermos, Jacuzzi and Windsurfer have met with a similar fate in some countries.

A number of manufacturers of well known trade marks, such as Levi's for jeans, Kleenex for facial tissues and Vaseline for petroleum jelly take active and expensive steps to educate their own dealers, newspaper editors, publishers of encyclopaedias and the public at large to appreciate that the trade mark identifies their products alone, and to use it in the proper manner.

The fact that intellectual property, like ordinary tangible assets, is subject to various kinds of risk



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means that the nature and probability of the risk exposure of intellectual property assets must be established and managed. It is, for example, necessary to ensure that the trade mark is legally secure and impervious to legal attack or infringement by a competitor. Another risk is the risk that the brand may become the target of counterfeiting. What will the impact be of parallel importation on the strength of the brand? Steps may, for example, be required to defend the brand against counterfeiting, passing off or parallel importation.

Reasons for determining the value of brands

The value of the firm's assets is one of the variables which may affect management decision making. As with other assets, the value of intellectual property must therefore also be known.

There are many multinational companies owning assets and conducting operations in numerous countries. The legal nature of intellectual property as well as the reasons for valuing intellectual property may differ from country to country. Corporate decisions affecting intellectual property must take into account these national differences.

The care and maintenance of trade marks may absorb substantial management resources. It is not only necessary to justify the use of management resources, but the firm's management should also be interested to know the relative contribution which particular assets make to the current and future profitability of the firm. It is therefore necessary that the value of these assets must be determined as accurately as possible. Management decisions, resource allocation and strategic planning will all be flawed if the overall picture is skewed because the value of intellectual property is incorrectly stated.

There are many specific situations requiring the availability and application of accurate data concerning the value of intellectual property. A firm may, for example, not only acquire or alienate assets, including intellectual property, but may also acquire or merge with other firms, be the subject of

an acquisition itself or form joint ventures. The intellectual property of the firm may be its single most important asset. The valuation of all assets and obviously also intellectual property is of critical importance to any such exercise. A fair value for the firm which is being sold can only be realised if all the firm's assets, including its intellectual property, are adequately valued. The acquiring firm has an equally valid reason for determining the value of the assets that are the target of the acquisition.

The use of the firm's intellectual property is often licensed to other firms. Determining a reasonable royalty to be charged will again require the calculation of the value of the particular intellectual property asset, more particularly its future income stream.

The impact of the tax regime on the value of the brand must be taken into account. Significant tax advantages may, for example, accrue when intellectual property is acquired. The purchase price may be depreciated over the period of the probable duration of use, i.e. the probable economic life of the intellectual property in question.

A firm may have to take action against a third party to protect its intellectual property rights or may be faced itself with claims that it is infringing the intellectual property rights of another. In the course of such legal proceedings the need may arise to estimate damages or determine royalties which are invariably based on fair market conditions.

On the financial side the inclusion of realistic values for intellectual property may substantially enhance the symmetry of the balance sheet, improving unattractive leverage ratios. Banks have started to consider the value of intellectual property as collateral when negotiating the terms of loans.

Perhaps the most important reason for establishing the real value of a firm's intellectual property is, however, the contribution which this will make to the firm's strategic as well as financial decision making, budgeting procedures and resource allocation. In the absence of determinate values of all a firm's assets and liabilities no realistic

decision making can take place. Establishing the value of the firm's intellectual property is thus central to effective decision making.

Conducting a valuation study

Depending on the quality of previous trade mark valuation exercises it may be necessary to conduct a special valuation study. This must be regularly updated.

Valuation studies may range from a simple valuation involving only one or two brands in one country to major exercises involving different brands in many countries. A recent study carried out on behalf of Imperial Chemical Industries UK to determine the value of the company's corporate symbol was carried out in relation to a range of goods and services and trade marks registered in over 120 countries.

A proper valuation study will require the involvement of and input from a variety of sources, namely marketing, legal and financial. The study needs to be properly prioritised and adequately resourced. Decisions should be taken as to the role of consultants.

There are many different methods of actually calculating the value of a trade mark or other intellectual property. Irrespective of the method used it will be necessary to determine the likely future income from products or services bearing the trade mark. This necessitates an evaluation of the competitive strengths and weaknesses of the particular brand, likely technological changes and changes in consumer preferences. Because of the inherent variability of many of these factors the value of the trade mark is likely to fluctuate over time.

Trade mark audit

The success and effectiveness of undertaking a valuation study will be substantially enhanced if the trade mark administration of the firm is up to date

and well organised.

In order to properly administer and manage their trade marks many businesses annually review their portfolio of trade marks to check whether, for example:

- adequate protection has been obtained for trade marks currently in use or proposed to be used
- existing registrations adequately cover all relevant goods or services
- licensees using a trade mark have been recorded as registered users
- any changes have occurred which may affect existing registrations
- adequate control is being exercised over the quality of goods or services provided by a licensee
- registrations are due for renewal, and
- additional registrations in neighbouring territories or export markets are desirable.

The annual trade mark audit and regular maintenance of the trade mark portfolio are prerequisites for accurate trade mark valuation.

Conclusion

Creating and maintaining brands is both an art and a science. Brands and branding are primarily a function of the firm's marketing department. Successful brands, like so many things in life, nevertheless require a team effort employing the multi-disciplinary skills of various departments. The firm's brands and other intellectual property may constitute a significant proportion of the value of the firm's total assets. Accurate information about the value of the firm's assets, specifically its brands and other intellectual property, is required for effective management decision making.

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