Intellectual property valuation methodologies are constantly changing and adapting to the fast pace of technology. An increased level of scrutiny has recently been placed on intellectual property portfolios. The need for increased professionalism in valuation, oversight, and security continues to grow. In addition, as the court system, especially the Supreme Court, has become more active in IP law, and IP law and regulations continue to change with the pace of technology, there is a heightened need for more accurate and creative methods to value intellectual property.

Valuation methodologies have also changed. Standards for valuation are certainly higher today than they were a decade ago; simple methods of valuation have been dismissed in favor of more sophisticated thinking and analysis. For example, the 25 percent rule is no longer being used (calculating an appropriate royalty as 25 percent of gross profits). Instead, we use concepts like the SSPPU, the smallest saleable practicing patent unit, a concept born out of litigation, now increasingly being used as a basis for establishing royalty rates both in transactions and litigation.

The major changes we’ve seen in the last 10 years are in the types of intellectual property; the standards used to value them; the context in which they’re valued and the methodologies used to value, as well as the broader range of structures in which intellectual property is managed. Also, social media has blossomed in the last decade to generate new and different ways to use IP, both in its primary vehicle to disseminate concepts and ideas, as well as a delivery vehicle, (e.g. Amazon Prime or Instagram).

This is the background against which this article is being presented: millennial changes in intellectual property and its valuation.

The Three Great Drivers of Change in Intellectual Property in the New Millenium

The groundswell of forces for change comes from three areas:

- The legal landscape: Congress, The Supreme Court, Federal Courts, Bankruptcy Courts, Tax Court
- The emergence of new forms of IP, driven by technology and as a result of legal changes, interpreting patents, trademarks, copyrights, and rights of publicity.
- Greater precision, transparency, and professionalism in the process and standards of valuation—as well as closer scrutiny of the process.

Intellectual Property Law From the Supreme Court to the State Courts to Congress—the Changing Landscape

Going back just 25 years ago, the U.S. Supreme Court heard about 150 cases a year, and rarely did any of those cases involve IP. By contrast, in the term beginning October 2013, the court heard 67 cases and 15 percent of its total workload involved cases dealing with IP. Six of those cases dealt with patent issues, two had implications for copyrights, and two were Lanham Act, also known as Trademark Act, which governs trademarks, service marks, and unfair competition cases in the world. This level of activity in IP cases continued through 2017.

Two major pieces of legislation have affected the value and valuation of IP. The Leahy-Smith America Invents Act (AIA), signed into law in 2013, and the Uniform Trade Secrets Act (UTSA), which provides substantial strength and reinforcement to the value of trade secrets at the Federal level. This Act not only gives new enforcement muscle, but it is also a step forward in adding substance and value to trade secret assets.

On the legislative front, the reinvigoration of the Patent Trial and Appeal Board (PTAB) in 2013 created the IPR (inter partes review)—which to some extent potentially weakens patents and shortens their longevity. The IPR allows challenges to almost any new patent that comes to issuance. While it aids greatly in the ability of corporations as well as inventors and creators to challenge the claims of a new patent, it does have one chilling side effect: it can end the lifespan of a promising new patent. Thus, one has to be cautious in the valuation of these assets.

The America Invents Acts or the Patent Reform Act of 2013 was a major overhaul of our patent laws; harmonizing the U.S. patent law with Europe and the majority of the world. One of the major changes was a shift from a first to invent system to a “first-to-file”
Technology And Courts Changing IP Valuation

system which went into effect in March 2013. The system is based on three key principles:

• The first person who files a letter application is the one who generally has the prime position in receiving the registration unless it can be proved that the subject matter disclosed in the application was derived from a venture that files a later application.

• The second major change is that inventors will still have a one year grace period where their own disclosures or other derivation disclosures may not be used as prior art if they occurred in the prior 12 months.

• Third, foreign public use and offer for sales will now be considered prior art, which was not the case under our former law.

In general, the effect of the law allows companies, NPEs, and others who are aware of an independent inventor’s progress to step in and file a first application. Many claim that this new act has worked contrary to the best interest of independent inventors and creators.

The Emergence of New Forms of Intellectual Property

New forms of intellectual property have appeared based on technological activity, social media and necessity; while others have become more circumscribed—such as business method patents. In effect, the territory of business method patents has become increasingly narrow. The courts and the intellectual property community itself are constantly pushing to develop new forms of intellectual property along multiple fronts. These forms include:

• Patents and technology
• Copyrighted materials, ideas, and concepts
• Trademarks
• Social media

Each of these have added elements to the family of IP.

On the patent and technology front, we see new approaches to packaging technologies, encapsulating trade secrets with patents, and increasing use of trademarks and brands to wrap around a patent or technology family in order to offer a complete bundle of intellectual property assets for sale or licensing. In addition, software implemented inventions continue to grow in spite of relatively recent court decisions. (Remember the Alice and Bilski decisions, which at first glance seem to limit all software implemented inventions—but in fact, simply limit those that patent an abstract idea, or a “law of nature.”)

In the world of trademarks, change has been constant over the last decade. From holographic trademarks, to 3-D trademarks, to the increasing use of colors, smells, sounds, and other sensory perceptions in trademarks, the world continues to expand. This changing world of trademarks means that multiple trademark elements are often to be included in a valuation and value must often be allocated to individual trademark elements.

Nowhere has change been more evident than in the world of copyrights and social media. Facebook, YouTube, Twitter, Instagram, and Snapchat, continue to offer up a never-ending landscape of copyrighted materials and usages—as well as trademark uses. Social media is also the new battleground for use and misuse of rights of publicity and copyright.

Rights of publicity, the right of an individual to control the commercial use of aspects of their identity such as their name, image or likeness is an area of growth and change. Many states have added new specific right of publicity statutes in the last 10 years; others have added post mortem rights of publicity statutes. Still, others have expanded the scope of right of publicity coverage beyond just a name and likeness.

In the middle of 2016, a media frenzy fed a right of publicity case that was watched on TV every night for two weeks: The Hulk Hogan v Gawker.com case. The classic battle between an established social media presence and a longtime entertainment personality. The confrontation centered first on the right of a personality to protect their ROP; and second, the right of a website to post embarrassing personal material in the name of First Amendment Fair Use right of free speech.

Finally, the importance of trade secrets has grown from a stepchild form of IP. It was not often valued a decade ago, but now has moved firmly into the forefront of the intellectual property discussion—and moved to center stage in terms of valuation and valuation methodologies.

Greater Need for Precision, Professionalism, And Transparency in the Valuation Process

A major trend in the value and valuation process is the greater need for professionalism. While intellectual property valuation professionals have not yet come together to ensure a single standard of financial professionalism in their work, there has been some broader agreement on the acceptable methodologies for the valuation of IP and intangible assets.

Credentials and credentialing of IP Valuation professionals is not standardized, and spotty at best. There are at least 25 organizations that hand out valuation credentials. When checking on the credentials of a valuation professional, make sure to examine not only the credentials, but also those of the credentialing institution.

Credentialing Groups:
• American Bankruptcy Institute (ABI)

Valuation Methodologies are Changing

Older, simplistic methodologies are leaving us

- Income, market, and cost approach are becoming more sophisticated
  - Variations on these three are being used more frequency with (e.g. Cost Analysis, Income Premiums, Market Multiple Approaches)
- Increased scrutiny of comparable transactions and benchmarking analysis
- Royalty rate analyses continue to dominate, particularly in litigation
  - However, a much more in-depth understanding of royalty rates, and the other issues in royalty agreements, is necessary
- Old rules of thumb are history, including the 25 percent Rule of Thumb and the five percent Rule of Thumb
- Comparables from outside “the footprint of the patent” can now be used in damages cases
- The Georgia-Pacific factors, after nearly 45 years, have been buried in landmark cases, such as the one which CONSOR acted as experts (StoneEagle Services, Inc. v. Pay-Plus Solutions, Inc.) and others, and are no longer required in patent valuation of damages cases

Greater Scrutiny, More Stakeholders

Another important change affecting intellectual property in general and valuation in particular, is the greater realization by corporations of the value and importance of their IP portfolios. As a result, an increasing number of constituencies or stakeholders who have an interest in their portfolios and their value are reaching out to IP valuation experts. Ten years ago, when CONSOR wrote The Original Primer on intellectual property value, two things had not occurred (among others of course): the first was the Great Recession of 2008; and as a corollary, the Dodd-Frank Act of 2010 was not yet in place.

The Dodd-Frank bill had one major effect on corporations IP and their IP value: boards of directors and individual directors now have a greater responsibility to see that IP portfolios are well managed and value extraction is maximized. Because intellectual property assets tend to comprise a high percentage of most company values, the management of these assets will generally fall within the scope of a director’s fiduciary duties.

All of this has had three consequences on IP and its value:

- Greater oversight and scrutiny by multiple parties
- Greater awareness of IP value and the need to maximize value extraction
- More transactions, financings and securitization involve IP

However, oversight of IP management is difficult because of several issues. First, enforcement of a patent portfolio is risky and expensive. Litigation is a high risk alternative. On the other hand, patent licensing is also high risk; more than that, it’s opaque, secretive, and difficult to implement. At the same time, patent values are opaque. What do we mean by opaque? With patents (and all IP to some extent) value is situational and context specific at the best of time.
And so, corporate boards and other stakeholders today are looking for value extraction alternatives. This has led to companies asking for valuations of their portfolios. A new process for many and a difficult concept, unless one knows the context of the valuation: sale, license, securitization, joint venture. Licensing strategies and budgets are constantly being reexamined. Internal licensing teams are being set up to explore sales and licensing alternatives. Recently, sales of entire portfolios have taken place. Also, the increase of patent litigation in the past five years is constant, the only exception being a dip in that trend line in 2014.

The same issues arise with large brand and copyright portfolios. The pressure is now on: extend, license or sell. Single product brands are virtually non-existent. Extend, extend, extend is the mantra of today's trademark-based brands. Copyright-based companies, such as Disney, or any of the other entertainment or sports related conglomerates are all practicing the same strategy. They build on their intellectual property by extending or licensing an ever widening family of licensed products and services.

Finally, as we wrap up this overview on changes in IP and IP valuation, it is interesting to point out that Daubert challenges against intellectual property experts are on the rise. The rate of challenges for experts now exceeds 75 percent in some circuits and the rate of successful challenges can exceed 55 percent. As the amount of intellectual property litigation continues to increase, so does the rate of challenge for valuation experts.

This surely is a clear sign of the increasing importance of accurate intellectual property valuation—and a clear signal that accurate valuation work by intellectual property experts is more important than ever as we move deeper into the millennium—accuracy both in litigation and in transactions.

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