Navigating the Value of Intangible Assets

SILVERPINE
GROUP
VALUATION OPINIONS AND CONSULTING

AGENDA

Background

Defining Intangibles

Identifying Intangibles

Valuing Intangibles

Strategies and Insights

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13 years of valuation experience

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Notable valuations:

- Oakland Raiders
- Silver Lake (Private Equity)
- Ulta Beauty
- Buoy Brewery

Exploring the Definition of Intangible Assets

What is an Intangible Asset?

Value is derived from a bundle of legal rights, not physical qualities.

Six defining characteristics:

1. Can be identified and reasonably described
2. Subject to legal existence and legal protection
3. Subject to transferrable private ownership rights
4. Documented by some tangible evidence of its existence
5. Created at an identifiable time where it came into existence
6. Subject to being destroyed or terminated

Intangible Assets vs. Economic Phenomena

<u>Intangible Assets</u>

- Patented Manufacturing Process
- Internally Developed Software
- Exclusivity Agreements
- Trademarks and Brand

<u>Economic Phenomena</u>

- Economies of Scale
- Technological Superiority
- High Market Share
- Positive Image

Economic phenomena may indicate an intangible asset but are not an intangible asset.

Identification of Intangibles

Evidence of Existence

“Physical” Evidence

Documents provide evidence of the existence of intangibles:

- Presence of leasehold agreements
- Licensing arrangements and agreements
- Filed and/or approved patents and copyrights

Superior Income

Exclusive deals with customers provide guaranteed income over a period.

Brand is well known among consumers, influencing purchasing decisions among competitors.

Proprietary software allows the company to bill more efficiently and collect receivables at a higher rate than the industry.

Special exclusive license granted by government held by company to operate in its line of business.

Mitigation of Expenses

The company has a long-term lease at a below-market rate of rent.

Long-lasting relationships with customers require lower marketing costs to retain those customers.

Multiple product lines can utilize the same proprietary manufacturing processes.

Well-trained workforce has led to less spoilage than industry average.

Mechanisms of Creation

General Creation

Creation through general course of business…

Customer Relationships

Supplier Contracts

Assembled Workforce

Internal Systems

Focused Creation

The company makes an effort to create an intangible asset…

Copyrights

Patents (Use/Utility/Etc.)

Trademarks and Logos

Trade Secrets

KFC Secret Recipe

Categorizing Intangibility

	Realty Assets (Immovable)	Personal Property (Movable)
Tangible	Land Buildings Building Improvements	Machinery and Equipment Vehicles Office Equipment
Intangible	Leasehold Agreements Easements and Right of Way Mineral Rights	Financial Assets Intellectual Property Customer Relationships Goodwill

Goodwill

Three Types of Goodwill

Enterprise (Institutional) Goodwill

- Results from ongoing operations of the business
- May also be created from the efforts of the professionals

Professional Practice Goodwill

- Usually relates to medical, dental, legal, accounting firms
- Borne out of the relationships developed by the professional

Celebrity Goodwill

- Derived from a person’s fame and influence
- Related to value of name, image, and likeness (NIL)

<u>Identifying Notes</u>

Types of services provided

Personal relationships with customers

Individual’s direct impact on the management of the entity

Goodwill Attribution

Enterprise Goodwill

No single professional is typically required for the business to continue to reap the benefits of its goodwill.

More transferable because it is not separable from the business entity.

Professional Practice Goodwill

One person makes practically all management decisions for the business.

The success of the business is driven by a professional's reputation and activities of that person.

Valuation of Intangibles

Scoping

Why Do We Perform these Valuations?

Taxation

- Direct Sale of IP
- Corporate Restructuring
- Estate and Gifting
- Charitable Contributions

Accounting

- Acquisitions of IP or Company
- Testing for Impairment
- Annual Recordkeeping
- Licensing Arrangements

Also…

Intercompany Usage

Transaction Pricing

Lost Profits / Damages

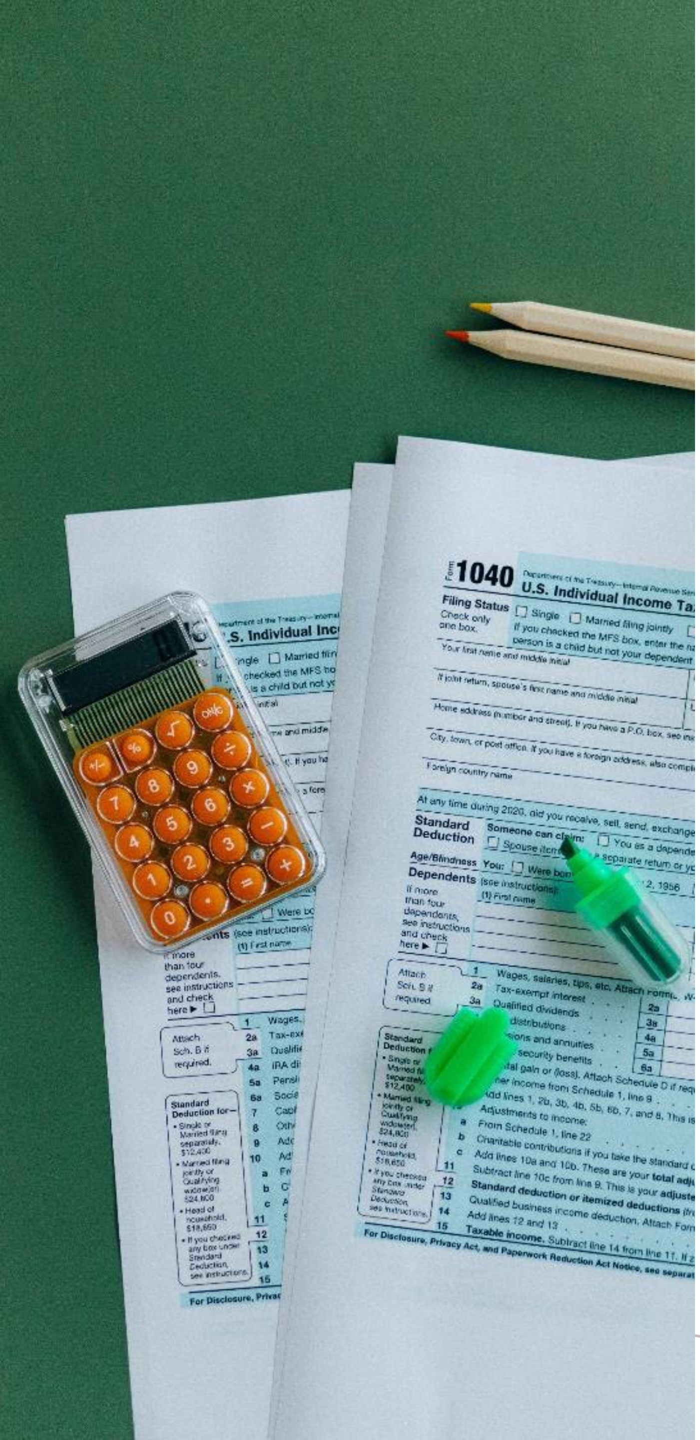
Corporate Governance

Infringement

Sale-Leasebacks

Transfer Pricing

Strategic Planning



The Adjusted Tax Basis

Considerations must be made when an intangible asset is transferred for calculating the adjusted tax basis:

1. The cost to originally acquire or create the asset
2. Amortization or consumption of the asset prior to transfer
3. Additional capitalized costs to enhance or maintain it
4. Impairments (technical or economic obsolescence)
5. Investments to improve or enhance the intangible
6. Recapture of prior deductions (Section 179)

26 U.S. Code § 197

The adjusted basis of eligible intangible assets are amortized over a 15-year period.

Eligible Assets Include

Goodwill
Workforce
Books and Records
Patents / Copyrights
Customer Intangibles
Supplier Intangibles
Licenses / Permits
Non-Competes
Franchise Agreements
Trademarks / Tradenames

Preliminary Scoping

What is the standard of value?

Fair Market Value	Fair Value (Financial Reporting)	Market/Exit Value
Acquisition Value	Value in Use	Investment Value
Collateral Value	Insurable Value	Ad Valorem Value

Preliminary Scoping

What is the premise of value?

Highest and Best Use (HABU) ← Most common

- Value in continued use as part of the ongoing business.
- Value in place but not being used to produce income.
- Value in exchange as part of an orderly disposition
- Value in exchange as part of a voluntary liquidation.
- Value in exchange as part of an involuntary liquidation.

Valuation Techniques

Income Approach

Incremental Income Analysis

- Measures the increase in revenue or reduction in cost if the intangible asset is owned.
- May also reduce the risk profile of the business by owning the intangible asset.

Direct Royalty Methods

- Relies on actual licensing rates of existing contracts and agreements.
- Uses the royalty rate and licensing maintenance costs to determine value.

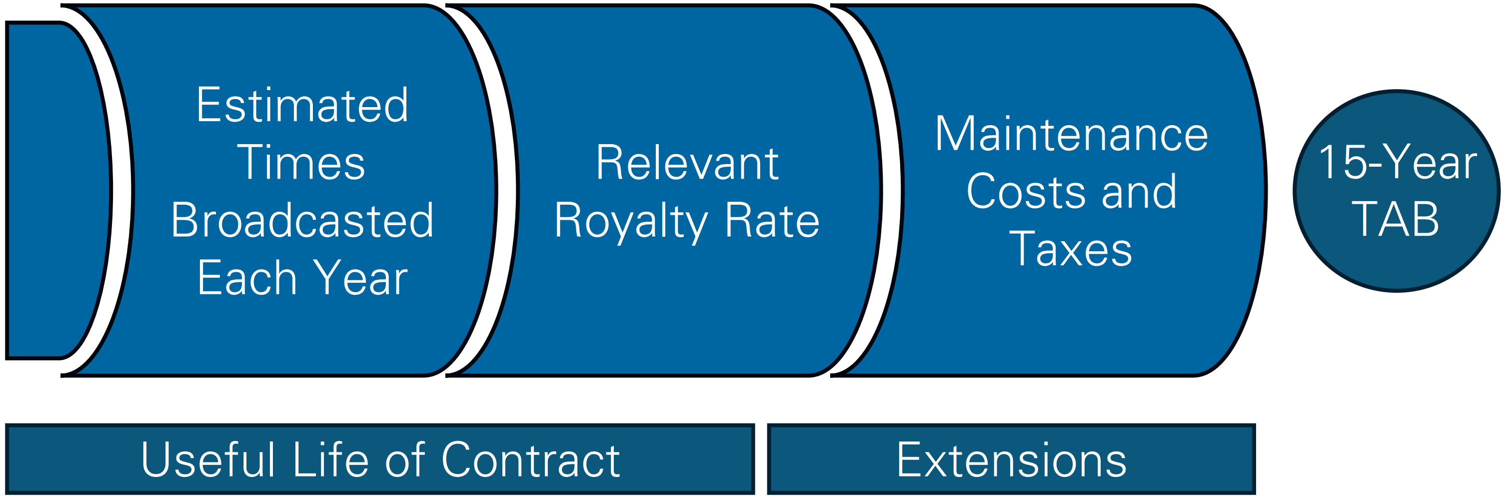
Profit Split Analysis

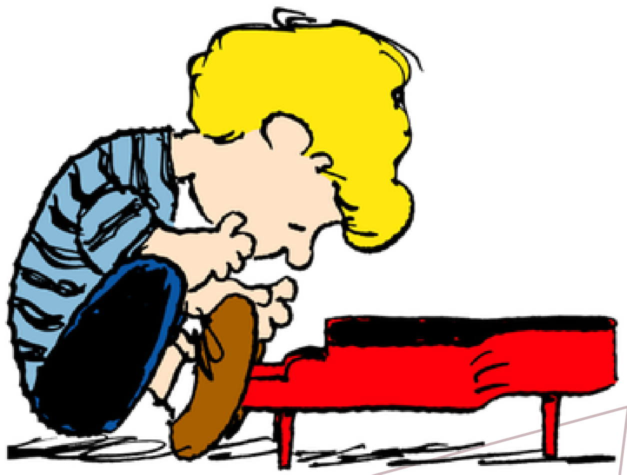
- Allocates a percentage of revenues, expenses, and/or profits to an intangible asset.
- Considers other contributory assets (i.e. real estate, workforce) as a required cost to achieve the profits generated by the intangible.

Case Study 1: Peanuts Specials

Background

Rights owner’s wants to transfer contracts that allowed broadcasting rights to 14 Peanuts cartoon specials and certain Garfield cartoons to a trust for estate planning.





Case Study 1: Peanuts Specials

ABC Contract Value	Year 1	Year 2	Year 3	Year 4	Year 5
Contract Period		*Existing Contract Period*		*Extension Period*	
Anticipated Broadcasts	18	16	14	14	14
Royalties Per Broadcast	$10,000	$10,000	$10,000	$8,000	$8,000
Total Royalties	$180,000	$160,000	$140,000	$112,000	$112,000
Less: Maintenance Costs	$3,000	$3,500	$4,000	$4,500	$5,000
Pre-Tax Royalties	$177,000	$156,500	$136,000	$107,500	$107,000
Less: Taxes (28.0%)	$49,560	$43,820	$38,080	$30,100	$29,960
Net Royalties	**$127,440**	**$112,680**	**$97,920**	**$77,400**	**$77,040**

Note: Numbers and values have been changed for confidentiality purposes.

Case Study 1: Peanuts Specials

ABC Contract Value	Year 1	Year 2	Year 3	Year 4	Year 5
Net Royalties	$127,440	$112,680	$97,920	$77,400	$77,040
Discount Rate	15%	15%	15%	15%	15%
Discount Period	1.0	2.0	3.0	4.0	5.0
PV of Royalties	$110,817	$85,202	$64,384	$44,254	$38,303

Note: Numbers and values have been changed for confidentiality purposes.

NPV of Royalties	$342,960
TAB (5-Year, Non-Sec. 197)	$79,259
FMV of Royalty Contract	**$422,000**

Market Approach

Comparable Sales Method

- Relies on comparable uncontrolled transaction (CUT) data to form a basis for value.
- Most applicable to “naked” intangible transactions such as FCC licenses or mortgage portfolios.

Relief from Royalty Methods

- Establishes a hypothetical or market-based royalty or licensing rate.
- Uses the royalty rate and licensing maintenance costs to determine value.

Comparable Profit Margin Method

- Usually relevant when there is an extraordinary intangible asset and other “normal” ones.
- Assumes that the intangible value is derived from excess profits over market comps.

Case Study 2: College Athlete NIL

Background

The college athlete's celebrity value, captured through name, image, and likeness is measured through regression analysis to then sell it to an SPV in a sale-leaseback arrangement for tax planning benefits.

Identify Deal Values and Primary Variable Drivers → Perform and Assess Multivariate Analysis → Apply Multivariate Formula to Subject Athlete

Case Study 2: College Athlete NIL

Dependent Variable

- Aggregate Deal Value

Independent Variables

- Player and Team Performance
- Influence (Social Media Followers)
- Exposure (Player Position / Accolades)

Case Study 2: College Athlete NIL

Variable	Coefficient	Standard Error
Intercept	496,572.21	33,359.98***
Social Media Followers	11,126.40	3,487.86**
Position: QB	145,638.57	30,803.47***
Position: FB	130,478.34	32,984.72***
Position: WR	146,375.44	38,397.44***
Team Rank	-19,282.72	882.7***

$* \; P \leq 0.05$

$** \; P \leq 0.01$

$*** \; P \leq 0.001$

Case Study 2: College Athlete NIL

Athlete Profile

Followers: 7.42m
Quarterback
Team Rank: 4

Intercept	Followers	QB	Team Rank

$$496{,}572 + (11{,}126 * 7.42) + 145{,}639 - (19{,}282 * 4)$$

Implied Athlete NIL Value

$648,000

Cost Approach

Types of Cost

- Cost to reproduce the asset as new: duplicate or identical asset.
- Cost to replace the asset as new: asset with same utility and functionality.

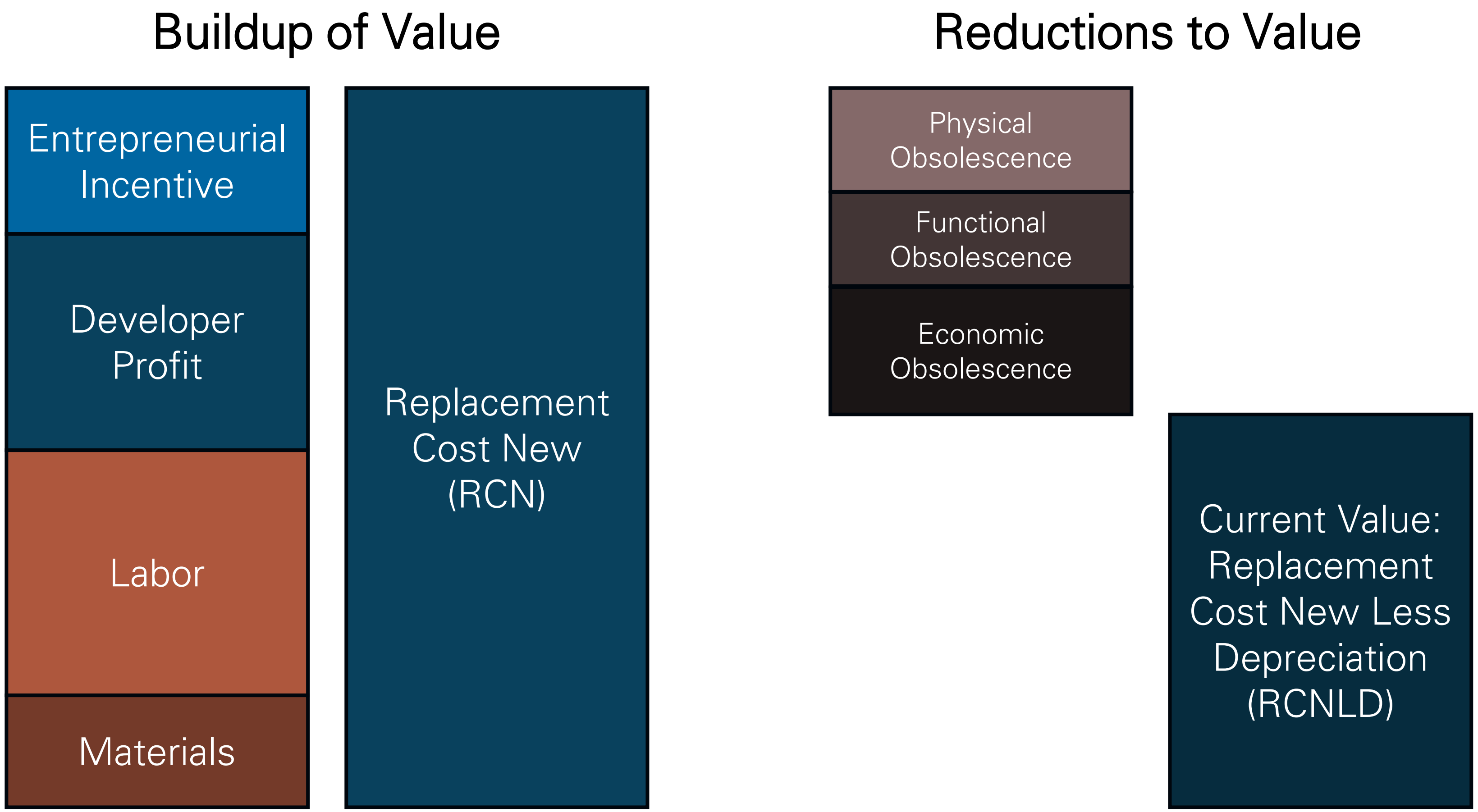
Components of Cost

1. Direct costs
2. Indirect costs
3. Developer's profit
4. Entrepreneurial incentive

Reductions to Value

1. Physical Obsolescence
2. Functional Obsolescence
3. Economic Obsolescence

Cost Approach



Estate and Wealth Planning Strategies

Estate Planning Mechanisms

Grantor Retained Annuity Trusts

- Grantor transfers intangible asset to trust for a set period.
- Retains right to receive an annual payment from trust.
- Increase in value of the trust's assets pass to the beneficiaries tax-free.

Example: Copyright for music rights transferred to a GRAT.

Charitable Remainder Trusts

- Grantor puts intangible in trust and receives a tax reduction.
- Ideal for assets with low tax basis and high appreciation.
- At the end of the trust term, remaining assets go to a designated charity.

Example: Patent that appreciates over time.

Wealth Planning Mechanisms

Athlete / Celebrity NIL Leaseback

- Athlete sells right to their NIL to an SPV or collective.
- SPV or collective has rights to deal/endorsement income.
- Athlete receives a lump sum or annualized payments.

Allows for structured guaranteed income for athletes who would otherwise not be guaranteed income to play their sport.

Professional Practice Goodwill

- Practitioner sells their goodwill to an investment entity or SPV.
- Practitioner gets an infusion of cash and enters into a leaseback, paying a regular lease payment.
- Can also be a mechanism to estate planning by smoothing the transfer of assets to a trust.

Various tax and estate planning benefits can be recognized.

THANK YOU

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