

How valuing IP could assist in divorce cases

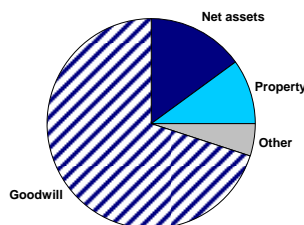
Introduction

- 1.1. In divorces where one party owns shares in a business it is likely that an IP-driven valuation will identify the true value required for ancillary relief. This paper outlines briefly how an IP valuation could assist you in such divorce cases.

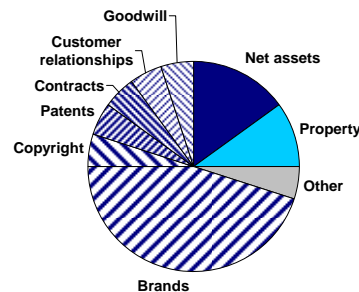
What is IP?

- 1.2. Traditionally, for a valuation all forms of IP were bundled together under the term goodwill, defined as enterprise value less net tangible asset value.
- 1.3. Since the introduction of new financial reporting standards acquired IP has been required to be put on balance sheets of companies when acquired.
- 1.4. These changes reflect modern valuation methodologies and IP's increased importance to business value. These changes are also recognised by the courts and the components of what used to be called 'reputation' or 'goodwill' can now be isolated and valued individually, producing a more thorough valuation:

Business value pre 1988



Business value post 1988



IP valuation methodologies

- 1.5. Valuing IP is similar to valuing other tangible assets, with three main approaches:
- **Income approach:** methods that convert future anticipated economic benefits into a present single amount.
 - **Market approach:** methods that compare the subject to transactions or market values of similar businesses.
 - **Cost approach:** quantifying the amount required to replace the asset or the amount previously invested in creating it.
- 1.6. In general, the income approach, based on discounted cash flow analysis, is the best approach, supported heavily by benchmarks from the market approach and the cost approach acting largely as a sense check.

Illustration 1: bestselling author

- 1.7. In this case, an author is being divorced. He is successful, publishes about a book every two years and receives royalties from new releases, back catalogue, films, TV and personal appearances. He is also due to retire. An initial valuation of the company was approximately £10m, based largely on the historical sales which have been consistently about £8m for many years.
- 1.8. A closer analysis of the copyright revealed that 80% of income came from new releases. Further investigation revealed that the back catalogue, which comprised the majority of the remaining 20%, was buoyed by the new releases; i.e. without new releases, the company lost the majority of its value. The IP-focused valuation produced a better researched value of under £1m.

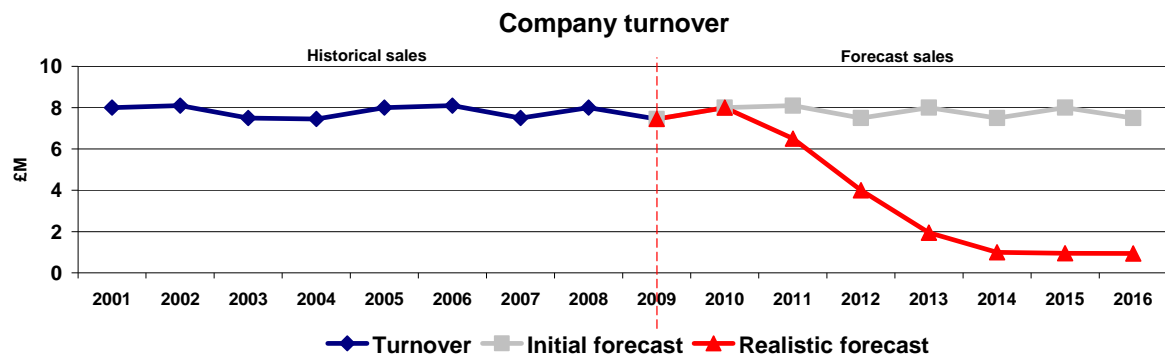


Illustration 2: regional estate agent chain

- 1.9. In this case, the owner of a chain of regional estate agents is being divorced. As the company is unprofitable, the owner claims its value is negligible. A closer look reveals the reason the company is unprofitable is because investment has been made into expanding the number of owned premises, franchising the business into other regions and building a recognised brand (thereby deflating the profits).
- 1.10. Further investigation found that the investment behind the chain was about to lead to profitability; a significant proportion of the business – and the franchising income - was found to be driven by the brand name. It also demonstrated there was an active market for similar brands and businesses in support of the valuation.
- 1.11. The brand, franchise contracts and the business were valued separately, demonstrating the significant value of the business.

Conclusion

- 1.12. The value of IP in business is often overlooked and specialist skills are required to value it. If this is carried out, a more thorough valuation can be presented to the court to resolve marital disputes and ancillary relief.