Valuation of intangible assets

International Valuation Standards

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IVSC in brief

- IVSC stands for International Valuation Standards Council
- Non profit organization created in 1981 and restructured in 1987-1988
- Develop robust and transparent procedures for performing international valuations through a single set of globally recognized valuation standards
- 3 boards:
  - Board of trustees responsible for strategic direction and funding
  - Standards Board issues international valuation standards
  - Professional Board issues guidance and promote professional standards and training
- Open to users, providers, professional institutes, educators and regulators of valuation services
International Valuation Standards

• Valuation is an estimate based on judgment: IVS do not tell people how to value
• IVS set a robust framework for the exercise of judgment
  – Identify financial conventions
  – Describe basics of commonly used valuation methodologies
  – Sets the minimum information to be included in a report
• IVS are applicable to all valuation purposes (not only IFRS) and types of assets
  – General standards
  – Application Standards (specific purposes)
  – Assets Standards (matters that influence the value of different types of assets)
Intangibles valuation in IVS

- IVSC has worked extensively on the subject
  - ED Revised international valuation guidance note n°4 - Valuation of intangible assets (January 2009)
  - ED Proposed new International Valuation Guidance Note No. 16 - Valuation of Intangible Assets for IFRS Reporting Purposes (January 2009)
  - ED IVS – IVS 301-02 – Valuation of intangible assets (June 2010)
- In 2011 IVSC will issue its final IVS and a TIP on intangibles valuation
Definition of Intangible assets

• Non monetary asset that manifests itself by its economic properties
  – No physical substance, but
  – Grants rights and economic benefits to its owner
• Identifiable if it is either :
  – Separable, or
  – Arises from contractual or legal other legal rights
• Goodwill is an unidentifiable intangible asset:
  – residual amount ...
  – ...remaining after the value of the identifiable assets adjusted for liabilities have been deducted from the value of the business
Examples of Intangibles

Marketing Related
• Trademarks
• Trade names
• Certification marks
• Trade dress (unique color, shape or package design)
• Internet domains
• Non-compete agreements
• ...

Customer or supplier related
• Advertising agreements
• Licensing, royalty agreements
• Servicing contracts
• Franchise agreements
• Customer relationships
• Customer lists
• ...

Technology Related
• Contractual or non contractual rights to use:
  • Patented or unpatented technologies
  • Data bases
  • Formulae
  • Designs
  • Softwares
  • Processes
  • Recipes

Artistic related
• Royalties from artistic works:
  • Plays
  • Books
  • Films
  • Music
• Royalties from non-contractual copyright protection
Valuation approaches for intangible assets

• Direct market comparison with transaction involving identical or similar assets

• Income approach : value is determined by reference to present value of income, cash flows or cost savings generated by the asset
  – Relief-from royalty : value of the hypothetical payments that would be saved through owning the asset compared with licensing it from a third party
  – Premium profit method : comparison of forecasted profits earned by a business using the asset with those that would be earned without
  – Excess earning method : Present value of the cash-flows attributable to the intangible asset after excluding the proportion of the cash flow attributable to other assets (contributory assets)
    • Single period
    • Multi period excess earnings method (MPEE)

• Cost approach for internally generated intangible assets that have no identifiable income streams
  – Replacement cost
  – Cost of developing a similar asset
Practical valuation issues

• Heterogeneous nature of intangible assets
  – Insufficient market data (or wide range) makes it difficult to rely on only one valuation method
  – Direct market approach delicate to use
  – Adjustments frequently needed (subjectivity risk)

• Estimating the remaining useful life of the asset
  – Consider legal, technological, functional and economic factors

• Forecasting cash flows and measuring risk
  – Identify cash flows specifically attributable to the asset (separability issue)
  – Uncertainty on future cash flow (risk factor issue)
Conclusion

• Valuation is more an art than a science
  – Nature of the exercise: replicate the market behavior
  – Complexity and uncertainty of assets
  – Evolution of valuation techniques
• As it is a highly subjective exercise, standards are useful to:
  – Frame the expert judgment
  – Set the proper due diligence process
  – Define the type of disclosure
• The quality of a valuation rests on the expertise, the internal processes and the independence of the valuer, all elements to be checked by the company