

Collaboration Between Company's Tax And IP Experts: Part 1

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The protection and management of intellectual property within a multinational enterprise (MNE) is complex and expensive. Internal coordination, particularly between the tax, legal and IP management professionals in an MNE, is essential to ensure that the strategic and financial objectives for IP assets are achieved while minimizing potential risks. In this first article of a two-part series, we discuss the benefits of collaboration between the various internal professionals of an MNE responsible for managing and enhancing the MNE's valuable IP.



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Managing IP Value Streams

There is no question that IP is a valuable corporate asset class. Recent estimates indicate that intangible assets, including IP, make up over 80 percent of the S&P 500's market value.[1] For public companies acquired in 2015, intangible assets (including developed technology, in-process research and development, patents, trademarks, etc., but excluding goodwill), made up about 34 percent of the purchase price.[2] The value of IP is also illustrated by recent sales, for example, the 2011 sale of Nortel's patent portfolio for \$4.5 billion[3] and the sale and license of AOL patents to Microsoft in 2012 for over \$1 billion[4] are two notable transactions. Marketing intangibles, including brands and trademarks, are also valuable, with each of Google, Apple and Amazon having brand values in excess of \$100 billion in 2017.[5] The stewards largely responsible for managing IP in these contexts are the IP professionals and licensing executives of an MNE.



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IP is an important strategic asset because it is a legally protectable, exclusionary right to its owners that can help to provide a competitive advantage in the marketplace. The numerous settlements and damages awards in IP litigation throughout the world demonstrate one measure of the value of these exclusionary rights. Recent notable settlements include Apple's settlement of patent litigation with Nokia in July 2017 for at least \$2 billion,[6] an award of nearly \$500 million to Dow by a Canadian court in July 2017 stemming from a patent infringement case involving polyethylene compositions used in packaging,[7] and the April 2016 award of \$940 million to Epic Systems stemming from the theft of its trade secrets relating to health care



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software.[8] The stewards largely responsible for enforcing IP rights are the MNE's IP legal team, supported by outside litigation counsel.

Another area under scrutiny by tax authorities and in the headlines is the valuation of IP for tax structures and transfer pricing purposes. This is highlighted in cases involving Amazon[9] and Apple.[10] The tax and transfer pricing professionals of an MNE are the stewards largely responsible for implementing tax structures involving the transfer and valuation of IP from one corporate entity to another.

While the IP assets may be the same, the valuation contexts for the IP asset and professionals responsible for each of these IP value streams (strategic/transactional value, enforcement value, and tax value), are potentially different. In many MNEs, these stewards, or IP experts, may be siloed and unaware of the strategies, valuation, and contexts of the IP considered by other stewards. This can lead to inefficiencies, the preparation of valuations that are not well documented and supported, and risks that can have an unintended impact on the value of the IP assets.

Leveraging Your Company's Different IP Experts

For purposes of this article, we divide an MNE's IP experts into three categories: (1) IP managers; (2) IP legal; and (3) tax/transfer pricing. Each of these IP experts has access to certain types of documents, utilizes context-specific and appropriate valuation methodologies, and has insights into the strategic benefits of the MNE's IP from their perspective. MNEs stand to realize benefits when its IP experts communicate and collaborate.

Leveraging Information Leads to Cost Savings and Better IP Valuations

The IP experts may have access to information specific to their areas of responsibility. For example, IP managers may have access to operational information that supported a valuation related to negotiation of a recent transaction or license, or may be a repository for in-licensed and out-licensed IP agreements. Tax/transfer pricing experts have transfer pricing documentation or other analysis that details publicly disclosed license agreements and transactions that are used to develop an arm's-length royalty range for intercompany licenses.

Sharing existing information within a specific IP expert's functional area with others can avoid duplication of effort and save money. In addition, the quality of valuation results could be improved (i.e., made more defensible) by sharing information. To illustrate, assume an IP manager conducted a valuation analysis and due diligence in support of a recent joint venture negotiation. As part of her involvement, she worked with engineers and manufacturing personnel to develop detailed financial analyses demonstrating the value the IP will contribute to the JV. If the IP manager was in communication with the MNE's tax/transfer pricing professionals, the study already performed for the JV transaction could be included as a supporting analysis in the transfer pricing documentation. This type of information may be important to help justify the MNE's position if challenged by tax authorities on the value of the IP. Further, it may benefit IP legal professionals in the event of IP litigation where damages resulting from alleged infringement by a competitor are sought.

Given the economic importance of an MNE's tax and transfer pricing structure and increased scrutiny from tax authorities, it is more important than ever that the IP experts leverage one another's expertise and knowledge bases.

Understanding the Context of Valuations Leads to Better Defense

A company's IP experts can also benefit from gaining a better understanding of the similarities and differences between the valuation contexts, requirements, data and approaches used in the different functional areas within an MNE.

Common IP valuation approaches (i.e., cost, market, and income approaches) are used in many contexts. However, the valuation results may vary based upon the unique facts and circumstances surrounding a valuation event (i.e., a transaction, a damages award, an intercompany royalty rate, etc.), such as the scope of IP rights being valued or the parties involved in the IP transaction.

It can be important when defending or leveraging a valuation to understand the differences in valuations, and how they can be reconciled. The confusion between the apparently different results can stem from inquiries from senior corporate executives in tax-related controversies or IP litigation. Having knowledge of the underlying similarities and differences, and how to reconcile the valuations provides all IP experts, regardless of their functional area, with the requisite understanding to respond to inquiries from others.

Examples of why there may be differences between valuations prepared for different contexts include:

- the premise of value required for the context (e.g., no less than a reasonable royalty for patent damages, arm's-length range for transfer pricing, etc.);
- the differing valuation methods favored by the user of the valuation report (e.g., a tax authority, a U.S. district court in a patent infringement litigation, or a counterparty to an IP-rich transaction);
- the assumptions that are made in the various contexts (e.g., assumed validity and infringement for patent damages);
- the available sources (public or internal) of financial information used to value the IP;
- the criteria for identifying comparables to the IP to determine its value; and
- the scope of the IP rights being valued (e.g., what IP is included, territorial rights, exclusivity, relationship between the parties, etc.).

Regular communication between the IP experts provides the forum for discussing and documenting, as appropriate, any apparent differences between valuations performed in different contexts.

Conclusion

Proactive measures and communication among all IP experts within an MNE can improve efficiency, provide strategic insight to other IP value streams, and help explain any apparent differences in IP value results that are prepared for different purposes.

In the second article of this two-part series we will elaborate on what can go wrong without collaboration between IP experts and offer suggestions to mitigate these risks.

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