

many businesses' brand protection strategy – not only since the packaging itself can be protected as a three-dimensional trade mark if the requirements are met²⁹³ but also because the packaging, by means of the abovementioned technical protection features, increasingly serves as an instrument to guarantee authenticity of the product along the entire distribution chain.

Next to such factual measures, legal means are also crucial elements of any brand protection strategy. These mainly include online and offline search for trade mark infringers and trade mark surveillance in order to prevent genericide. These law-related elements of a brand protection strategy will be dealt with in more detail below at 5.13.

In the brand protection strategy context, forecasting brand valuation, if carried out comprehensively, can be helpful for early detection and monitoring of possible factual and legal challenges as well as for singling out those brands for which investment (amongst others in the form of monitoring for protection strategy purposes) is expected to be profitable.

2.3.4.2 Assessment of Damages and Amount in Dispute

In trade mark cases brought before the courts, particularly in infringement and contractual disputes, legal dispute related valuations are generally carried out on the basis of past circumstances, for instance in context of assessment of damages, in which the aggrieved party, as a general rule, has to be put in a position as if the hurtful event would not have taken place. Furthermore, a trade mark-based amount in dispute needs to be determined in each case in which the main object of conflict is one or several trade mark rights.

Establishing the amount of brand value to be used in litigation is not a question of law but one of fact. As a consequence, since there is no room for legal argumentation in the area of fact finding, a specific fixed legal rule or practice relating to determination of brand value in litigation contexts cannot exist. Judges are therefore not bound by a certain valuation method or rule.²⁹⁴ Rather, trade mark or brand value, if needed, is established in the course of discovery or evidence stages of a legal proceeding.

293 As to three-dimensional marks cf. below at 5.2.3.2.

294 Cf., with respect to business valuation, BGH, judgment of 1 July 1982, Case IX ZR 34/81; *Großfeld*, Unternehmens- und Anteilsbewertung im Gesellschaftsrecht, p. 44. These business valuation statements are sometimes being adapted for IP valuation

In general, damages for violation of intellectual property rights can be calculated according to the actually occurred damage (including lost profits), on the basis of profits made by the infringer or by way of licence analogy (how much would the proprietor have earned as a licensor during the time of infringement?).²⁹⁵ The amount of damages may only be calculated by means of one method whereby the plaintiff has the right to choose the method most favourable to him.²⁹⁶

The amount of damages specified by the plaintiff – or, if he has left it undetermined, by the court – merely reflects part of the value of an asset as it would be identified by means of a future-related strategic and comprehensive valuation tool. This is due to the circumstance that damages, whether assessed for a past and/or future event, merely refer to a limited time span in the life of the asset in question. Furthermore, an appraiser in a strategic valuation context would very likely utilise a licence analogy, but merely as a rough indicator of value.²⁹⁷

Hence, there is no room for comprehensive strategic forecasting valuations in the field of damages assessment; its purpose and the way it is carried out differs considerably from the purpose and procedure of damages calculation. This shall not belie the fact that determined damages reflect a certain value of the asset concerned. However, this value is merely related to utilisation of the asset in a limited time period (the time of infringement) and mirrors merely one aspect of a comprehensive forecasting value, such as profits derived directly from the asset.

without proper reasoning, cf. *Reese*, Die Bewertung von Immaterialgüterrechten, p. 30. However, it is possible to look at business valuation in this context due to the facts that a number of valuation tools are utilised for both purposes and that IP is an important part of all of a company's assets.

295 This threefold possibility of damages calculation had, in Germany, initially been developed by the courts, cf. e.g. BGH, judgment of 29 May 1962, Case I ZR 132/60 – *Dia-Rähmchen II*; IIC 2002, 900 – *Gemeinkostenanteil* (with regard to patents and industrial designs respectively); BGH, judgment of 12 January 1966, Case Ib ZR 5/64 – *Messmer-Tee II* (for trade mark rights); *Kraßer*, GRUR Int. 1980, 259, 260; *Schaub*, GRUR 2005, 918, 919. With the 'Gesetz zur Verbesserung der Durchsetzung von Rechten des geistigen Eigentums vom 7. Juli 2008' (BGBl I p. 1191), in force since September 1, 2008, which mainly serves to implement Directive 2004/48/EC (Directive 2004/48/EC of the European Parliament and of the Council of 29 April 2004 on the enforcement of intellectual property rights, OJ L 157 of April 30, 2004, pp. 45-86), the German lawmaker codified this possibility in its specific IP laws, e.g. in § 14 (6) MarkenG.

296 BGH, above fn. 295 – *Dia-Rähmchen II*.

297 Cf. below at 3.2.2.2.2.

As far as the assessment of the amount in dispute is concerned, the amount as brought forward by the plaintiff is generally accepted by the courts.²⁹⁸ Cases in which this is challenged and an actual valuation has to take place are rare (strategic forecasting valuations could be utilised in this connection, but are probably of little practical relevance due to the fact that they are relatively elaborate compared to the purpose they are supposed to serve). For instance, the German Federal Supreme Court recently upheld the amount of € 50.000 which is usually fixed by default.²⁹⁹ The court acknowledged the possibility of existence of particular circumstances justifying a higher or lower amount but denied them in that specific case.

It follows that comprehensive, quantitative and qualitative forecasting valuations are not needed for assessment of damages but could theoretically be utilised for assessing the amount in dispute (in Germany, one could use them to prove a certain value justifying a higher or lower amount in dispute than the default € 50.000).

2.3.5 Accounting and Tax

Valuation for accounting and tax purposes is imbedded in a framework of legal provisions, which are increasingly being internationally harmonised, especially in the accounting field.

Unlike future-related valuation for strategic purposes, accounting and tax valuations generally operate on the basis of circumstances bygone. The focus lies on documentation rather than on planning and strategy.

2.3.5.1 Accounting

Whenever an item appears on a balance sheet, it does so with a monetary figure. Hence, accounting necessarily presupposes valuation. The following paragraphs will give a brief overview of accounting rules relating to intangible assets as well as of possible implications thereof on the valuation of such assets.

298 *Mayer/Kroiß*, Rechtsanwaltsvergütungsgesetz, at no. 394.

299 BGH, judgment of 16 March 2006, Case I ZB 48/05. As to determination of attorney's fees in trade mark litigation, cf. BPatG, judgment of 7 December 2004, W (pat) 263/03.

As a general rule, all assets making up a business are supposed to be readable off the balance sheet. Hereby, it is common practice in a number of jurisdictions to distinguish between tangible and intangible assets and – within the group of intangible assets – between internally developed and acquired ones. Furthermore, internal, or management, and external accounting (also called financial accounting) need to be distinguished. In the course of internal accounting, which is utilised within the respective organisation to provide information to management, kind and scope of all asset valuation is at free discretion. This is not so with respect to external accounting, which is concerned with preparation of (publicly available) financial statements. The following paragraphs relate to external accounting only.³⁰⁰

2.3.5.1.1 International

Traditionally, intangible assets generally appeared on balance sheets solely in form of goodwill. In the course of the majority of acquisitions, the excess purchase price over the tangible assets' fair value had often been entirely allocated to goodwill. Assets such as patents and trade marks were therefore hidden behind the veil of goodwill as hidden reserves. Correspondingly, many businesses argued that intangible assets were neither measurable nor controllable.³⁰¹

However, the International Financial Reporting Standards (IFRS)³⁰² have

300 A concentrated overview of external accounting in the light of valuation will be given hereafter for reasons of clarity and completeness. Subsequently, accounting will not be addressed any more since this work is concerned with IP valuation for strategic purposes. For more information on accounting for intangible assets, in addition to the literature cited in the following, cf. e.g. *Benker*, Bewertung und Bilanzierung von Marken nach HGB, IAS und US-GAAP; *Bentele*, Immaterielle Vermögenswerte in der Unternehmensberichterstattung; *Förster*, Immaterielle Vermögenswerte nach IAS 38. Firmenwerte mit Zukunft und deren Behandlung nach IFRS; *Greinert*, Die bilanzielle Behandlung von Marken; *Grüner*, Behandlung der immateriellen Vermögenswerte im Rahmen der Erstkonsolidierung nach IAS/IFRS and *Schütte*, Aktivierungskonzepte immaterieller Vermögenswerte.

301 *PricewaterhouseCoopers*, Shedding light on IFRS: International Financial Reporting Standard 3 – The new Business Combinations standard, p. 2.

302 IFRS is a collection of international accounting standards for profit-oriented enterprises developed by private standard setters. It comprises the International Accounting Standards (IAS), which are issued by the *International Accounting Standards Committee (IASC)*, the *International Accounting Standards Board (IASB)* standards as well as the interpretations by the *International Financial Reporting Interpretations Committee (IFRIC)* and those of the former *Standing Interpretations Committee (SIC)*. The denotation 'IFRS' is used both as a generic term for all these accounting rules

required all listed companies³⁰³ to report acquired intangible assets on their balance sheets, if their fair value³⁰⁴ can be measured reliably, from the year 2005.³⁰⁵

In detail, IFRS 3 and IAS 38 (“Intangible Assets”) stipulate that all such assets need to be recognised and their fair value measured if they are identifiable (in order to distinguish them from goodwill) and controlled by an entity.³⁰⁶ In addition, there needs to be reliably measurable probable inflow of economic benefits, such as sales revenue.³⁰⁷

The identifiability criterion is met if the respective intellectual asset is separable (i.e. capable of being separated or divided from the entity and sold, transferred, licenced, rented or exchanged, either individually or together with a related contract, asset or liability) or arises from contractual or other legal rights (regardless of whether those rights are transferable or separable from the entity or from other rights and obligations).³⁰⁸

IFRS 3 includes an extensive list of intangible assets satisfying these criteria, which comprises trade marks, trade names, domain names as well as licencing, royalty and standstill agreements.

The mandatory recognition of acquired trade mark rights, separately from goodwill, makes these and other intangible assets more visible, improves their appreciation and consequently the status of those responsible for them. Additionally, intangible asset valuation for accounting purposes is of considerably increased importance. Positive communication of this will improve relationships with stakeholders, shareholders and investors which can help in the

and for a number of standards contained therein. The standards applicable to business combinations are IFRS 3.

303 Business entities which are not capital market oriented have the possibility to choose IFRS.

304 The term ‘fair value’ is not a uniform, separate term. Rather, it can be filled by other value terms such as market value, current or replacement costs, depending on the respective case, cf. *Hüttche/von Brandis*, Lexikon Rechnungslegung Bilanzanalyse Bilanzpolitik, p. 153.

305 This means from the transitional date on which the financial year 2005 starts – only for a few companies, a transition period until 2007 applies. Many large German corporations like e.g. *Volkswagen AG* and *Allianz AG* have already applied IFRS standards before 2005, cf. *Accounting Standards Committee of Germany*, FAQ (Frequently asked questions). According to § 292a HGB, this was allowed but not mandatory.

306 IAS 38.11 et seq. and IAS 38.13. A company exercises such control if it has the power to obtain the future economic benefit arising from the respective asset.

307 IAS 38.17.

308 IAS 38.12.

generation of positive PR, procurement of funds and be reflected in the share price.³⁰⁹ Reporting certain intangible assets separately contributes to greater transparency in accounting, not only for business combinations.

According to IAS 38.24 in connection with IAS 38.65, intangible assets shall be measured initially at cost of acquisition or production. If an intangible asset is acquired in the course of a business combination, the cost of that asset is its fair value at the date of acquisition. Subsequent valuations shall be conducted using either the cost or the revaluation model. Utilising the former, the respective asset shall be carried at its cost less amortisation and impairment losses. The revaluation model provides for the intangible asset to be carried at a revalued amount.³¹⁰

This shows that valuation for accounting purposes follows its own rules, focussing on defined values and accuracy. This is mainly necessitated by accounting prudence. The fact that a balance sheet does not fully reflect a company's value is, in return, tolerated. In consequence, there is no room for future-related comprehensive valuations as introduced in this work.³¹¹ Such valuations are by definition estimates and generally arrive at a value spread, not a fixed amount as it is required for accounting.

Now that acquired trade mark rights can be reported separately, it would seem logical to report internally generated ones as well. However, in the light of the factual circumstances and of valuation techniques currently in place it seems very unlikely that such rights can be valued reliably enough to satisfy international accounting standards.³¹² In the case of an internally generated brand, for example, it would be very difficult to allocate expenses to the specific corresponding trade mark.³¹³ Hence, accounting for internally generated intangibles would open up possibilities of abuse. Accounting prudence, therefore, keeps standard setters and lawmakers from allowing such accounting practice. It is said that at least one market transaction serves to objectify the value sufficiently for balance sheet purposes yet without it uncertainty would be too dominating.

309 *Caldwell*, How IFRSs put brands on the balance sheet, pp. 2-3.

310 This revalued amount is the asset's fair value (to be assessed with reference to an active market, which means that this model is difficult to apply for intangible assets) at the date of revaluation less amortisation and impairment losses.

311 Cf. chapter four.

312 According to IAS 38.21, intangible assets' acquisition- or production cost needs to be reliably measurable.

313 *Schmidbauer*, DStR 2004, 1442, 1443.

However, internally generated brands and intellectual property rights not separately appearing on the balance sheet can still be valued and referenced in publications such as the director's report or a so-called 'Intellectual Property Statement'.³¹⁴ Such valuation would be part of strategic communication as mentioned above rather than of accounting.

2.3.5.1.2 European Community

By means of Regulation 1606/2002 (IAS-Regulation),³¹⁵ the European Community has adopted IFRS for its jurisdiction. Art. 4 of this Regulation stipulates that companies the securities of which are traded on any stock market within the EC and which are subject to an EC jurisdiction are required to "prepare their consolidated accounts in conformity with the international accounting standards" for financial years starting on or after January 1st, 2005.

In addition, member states may permit or prescribe these publicly traded companies to prepare their annual accounts on the basis of IFRS as well and all other companies to utilise IFRS for the consolidated accounts and/or the annual accounts (Art. 5 IAS-Regulation). This provision aims to avoid fragmentation of applicable accounting rules in the light of harmonisation of the EC internal market.

2.3.5.1.3 Germany

On the basis of the IAS-Regulation, the German lawmaker has adapted national rules accordingly.³¹⁶ Subject to § 315a(1) HGB,³¹⁷ all publicly traded parent companies are required to prepare their consolidated accounts according to IFRS.³¹⁸ All other companies are allowed to choose IFRS for their consolidated accounts, § 315a(2) HGB. The traditional HGB rules will continue

314 *Menninger/Kunowski*, DStR 2003, 1180, 1182.

315 Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards, OJ L 243, September 11, 2002, pp. 1-4.

316 By way of the Gesetz zur Einführung internationaler Rechnungslegungsstandards und zur Sicherung der Qualität der Abschlussprüfung (Bilanzrechtsreformgesetz - BilReG), BGBl. I 2004, pp. 3166 et seq.

317 Handelsgesetzbuch – German Commercial Code.

318 § 315a(2) HGB stipulates similarly for parent companies which have applied for admission of shares to official trade.

to apply for annual accounts for purposes of assessment of disbursements and tax. However, in addition to this, businesses have the possibility to create an individual financial statement according to IFRS rules, cf. § 325(2a) HGB.

2.3.5.2 Tax

The field of taxation has a number of different points of contact with IP valuation. These include disputes between corporate taxpayers and tax authorities regarding the extent of tax due (which is affected by the figures of assets appearing on the balance sheet, of which certain IP is part), tax planning strategies (e.g. investment holding companies, charitable donations) and tax regulation compliance, the most prominent subgroup of which is the issue of transfer pricing.³¹⁹

2.3.5.2.1 Transfer Pricing

Transfer pricing refers to transactions across jurisdictional borders between related entities. These are usually entities under common control, e.g. companies part of one international group.³²⁰ Transactions falling into the realm of transfer pricing are not only cross-border delivery of goods, but also and particularly cross-border cost allocation, services and assignment or surrender of use of intangible assets.³²¹ In fact, the arrangement of international transfer prices belongs to the economically most prominent tax law issues for multinational enterprises.³²²

319 Like accounting, taxation issues will not be dealt with in this work apart from the following paragraphs due to the fact that tax issues do not fall into the realm of valuation for strategic purposes as focussed on in this work. Apart from the sources cited below, more literature on IP valuation and taxation can be found at *Bauer*, Verrechnungspreise für immaterielle Wirtschaftsgüter des Anlagevermögens; *Casley*, Tax. Introduction to tax and IP; *Dürrfeld/Wingendorf*, IStR 2005, 464.; *Herve/Stock/Bodenstein*, BC 2005, 268; *Hughes/Borzumato*, 17 Managing Intellectual Property, iss. 8, 35 (2006) and *Weber/Stoffels/Kleindienst*, Internationale Verrechnungspreise im Konzern.

320 *Dürrfeld/Wingendorf*, IStR 2005, 464, 464.

321 *Brügger/Streibel*, Steuer Revue 2003, 598. The intra-concern assignment and surrender of use of intangible assets is becoming increasingly popular due to the fact that these instruments enable parent company and subsidiaries to strengthen their equity by unveiling hidden reserves (e.g. through an intra-concern sale of an internally generated brand), to use the respective IP by one or several units at a time, and other; cf. slides by *Dr. Anke Nestler* from May 19, 2006, accompanying her speech “Bewertung von Intellectual Property bei konzerninternen Übertragungen bzw. Nutzungsüberlassung” at the conference “Bewertung von IPRs” in Königswinter, Germany.

Transfer pricing rules are applied in order to calculate the amount of profits which are liable to tax. These special rules are needed because in the case of transactions between related entities, the motivations for arriving at a certain price may be different from and not as balanced as two unrelated parties negotiating. For this reason, transfer pricing rules adjust the actual results to the results that would have occurred had the parties negotiated ‘at arm’s length’.³²³

The arm’s length principle is based on a comparison of the internal transfer price under scrutiny with a price independent third parties would have arrived at. This can be achieved either by comparison with agreements between two independent third parties conducted under the same or comparable conditions (so-called external comparison) or by comparison with agreements concluded by one of the dependent parties with one independent party, for example a licensee (so-called internal comparison).³²⁴ Finding such comparable agreements with regard to intellectual property assets is generally extremely difficult and sometimes impossible, because such transactions either do not exist (there is no comparable IP asset) or are rarely publicised (e.g. licencing agreements).³²⁵ The valuator needs to realise this and adjust his calculations accordingly.

There are a number of rules and guidelines on national and international levels which deal with this complex of issues. The OECD has issued transfer pricing guidelines³²⁶ which are – together with the American IRC sec. 482 rules³²⁷ – the practically most important ones.³²⁸ Even though these rules do not concretely stipulate how the arm’s length principle is to be operationalised, they lay down a number of methods by which an arm’s length price can be calculated, such as the licence-based methods ‘Comparable Un-

322 *Ernst&Young*, 2005-2006 Global Transfer Pricing Surveys – Global Transfer Pricing Trends, Practices, and Analysis, November 2005, p. 4.

323 This arm’s length principle is the foundation of all international rules on transfer prices, cf. *Ernst&Young*, Business Restructuring – Three Taxation Issues, p. 4.

324 *Wurzer/Reinhardt*, Bewertung technischer Schutzrechte. Praxis der Patentbewertung, p. 142.

325 Cf. 2.2.2.1.

326 *Organisation for Economic Co-operation and Development (OECD)*, Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. These guidelines are of such central importance that even some non-OECD member countries such as China and Chile orient by them.

327 The *Internal Revenue Service (IRS)* issues the Internal Revenue Code (IRC).

328 *Wurzer/Reinhardt*, Bewertung technischer Schutzrechte. Praxis der Patentbewertung, p. 142.