

Brand Valuation in Business Practice – Part 1

This article, the first of a two-part series, sets forth the results of an empirical study on current brand valuation practice in more than 120 European companies and across a broad range of different industry sectors.

This article sets forth the results of an empirical study on current brand valuation practice in more than 120 European companies and across a broad range of different industry sectors. The study considers issues such as why a company is valuing its brands (or why not), who is doing the valuation and which valuation methods are employed. The opinions of respondents on brand valuation as such and on recent international standardization efforts in the field are also presented. The valuation of brands and other intangibles, as well as brand definition and ownership issues have received fresh attention in the context of the ongoing project to revise chapter VI, Transfer Pricing Aspects of Intangibles, in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (hereinafter OECD Guidelines).

1. Introduction

1.1. Purpose and rationale for the research

Brands and their underlying trademarks are important elements of the value of a business. They are intangible assets that contribute to the increasing gap between observed market capitalizations versus reported book values of companies over the last 30 to 40 years.¹ Due to legal requirements or internationally accepted accounting standards like IAS 38 and IFRS 3, brands may not be recognized on a company's balance sheets if they have been self created, but not acquired. Nevertheless, brands can have a substantial impact on the creation of a sustainable competitive advantage and the long-term business success of companies in all industry sectors, as they constitute valuable elements of differentiation strategies and provide an anchor for customer recognition and demand.²

With respect to the monetary valuation of brands, a host of different methods have been described in literature over

the last 20-25 years.³ However, these methods may yield grossly varying values for the same brand at a given point in time. For example, the value of the Google brand in 2007 is reported to be either USD 17, 24 or 66 billion, according to different appraisers and their valuation methods.⁴ The application of different valuation methods by the same appraiser for the same brand at a certain point in time may also provide a broad range of brand values.⁵ Even if a brand is valued within a predefined "experimental" framework, the valuation outcomes vary widely. This is well documented by a case study published in 2004 by Absatzwirtschaft et al. in Germany. Here, the imaginary brands DT_{Wash} , DT_{Oil} and DT_{Shop} owned by a fictitious mineral oil company DT (*fuel stations*) were given to seven major valuation providers in Germany together with a uniform comprehensive briefing and a set of financial data for the determination of brand value. However, the resulting total DT brand values⁶ cover a range of EUR 173 to 958 million.

Nevertheless, brand valuation is a popular topic, as reflected by various annual global rankings, presenting the monetary value of well known brands.⁷ Last but not least, tax authorities have also developed a keen interest in the value of brands and other intangibles. This does not come as a surprise, as those intangibles can be – more or less – valuable assets for companies in many, if not all businesses. However, intangibles may provide not only a source for economic success stories, but also an anchor for taxable income, which is chased by tax authorities in all countries, due to sharply increasing state debt levels as a consequence of the financial and economic crisis during and after 2008.

Yet, the question remains valid if and why companies should invest any resources in a valuation of their (prospective) brands at all. In response, a range of monetary brand valuation purposes such as the sale or licensing of individual brands or trademarks (between related and/or unrelated parties), brand management (e.g. valuation of brand extensions), managerial incentivization (brand value as performance measure) or brand-backed credit

* © Martin Lagarden. Head of Global Transfer Pricing, Global Tax & Trade Group, Henkel AG & Co. KGaA, Düsseldorf. He can be contacted at martin.lagarden@henkel.com. The views expressed in this article are those of the author and do not necessarily reflect those of Henkel.

1. See for example J. Gerzema, *The Brand Bubble*, 21 Marketing Research 1 (Spring 2009), at 6-11. However, to be fair, such statements disregard the impact of sale and lease-back transactions related to brands and other intangibles, which should also have contributed to the development of the market vs. book value gap, at least over the last two decades.
2. Compare P. Kotler and K.L. Keller, *Marketing Management*, 12th edition (Pearson Prentice Hall, 2006), at 274-275.

3. Compare G. Salinas, *The International Brand Valuation Manual* (John Wiley & Sons 2009).
4. J. Knowles, *Varying Perspectives on Brand Equity*, 17 Marketing Management 4 (July/August 2008), at 20-26.
5. A. Damodaran, *Dealing with Intangibles: Valuing Brand Names, Flexibility and Patents* (2006), available at <http://pages.stern.nyu.edu/~adamodar/pdfiles/papers/intangibles.pdf> (accessed 1 January 2010).
6. Total brand value ($DT_{fuel\ stations}$) = $\Sigma (DT_{Wash} + DT_{Oil} + DT_{Shop})$ brand values. Compare Absatzwirtschaft, *PricewaterhouseCoopers, GfK, Markenbewertung: Die Tank AG* (Düsseldorf, Verlagsgruppe Handelsblatt, 2004).
7. See, for example, Interbrand, *Best Global Brands 2011 – Top 100 Brands* (2011), available at www.interbrand.com/ja/best-global-brands/best-global-brands-2008/best-global-brands-2011.aspx (accessed 16 Apr. 2011).

securitization, are cited in literature as being good indicators of why it may be worthwhile for companies to engage in brand valuation. Moreover, domestic and international accounting and financial reporting requirements related to acquired brands, as well as various domestic tax documentation rules related to arm's length pricing for the exploitation of brands in cross-border transactions between affiliated companies in a multinational group may serve as sound reasons for companies to value their brands and/or other intangibles.

Now, given the diverse context of different brand valuation requirements, purposes, methods and varying brand values, this empirical study has investigated why companies may (or may not) perform a monetary valuation of self-created brands, as well as a valuation of their acquired brands. Moreover, even if one were to assume that monetary brand valuation is done mainly for external accounting (and/or also for tax and transfer pricing purposes), it is interesting to determine whether consumer-related data or other market research information is considered in the valuation process, or whether only purely financial input data are considered. Lastly, the present research strives to highlight which monetary valuation methods are preferred by companies for self-created and acquired brands, and which benefits or weaknesses of brand valuation and the standardization thereof are perceived by managers today.

1.2. Research objectives

First, the objective of this study is to provide a critical review of general brand valuation characteristics and specific valuation approaches and methods as described in literature, thus adding to the body of current managerial knowledge in the field. Second, building on prior empirical studies of brand valuation in individual countries, most notably in Germany, it will be investigated how the topic has developed in business practice over time. Third, in addition to the high relevance of brands and other intangibles to companies, it will be set out that this investigation seems worthwhile, as various initiatives have recently been undertaken by various stakeholders, such as the International Accounting Standards Board (IASB), the German Institute of Auditors (*Institut der Wirtschaftsprüfer*, IDW), the International Organization for Standardization (ISO) and the International Valuation Standards Council (IVSC), in order to achieve a standardization of the valuation of brands and other intangibles.⁸

8. Compare IASB, *IFRS 13 Fair Value Measurement*, International Financial Reporting Standards Foundation/International Accounting Standards Board (2011); IDW, *IDW Standard: Grundsätze zur Bewertung immaterieller Vermögenswerte (IDW S 5)*, Die Wirtschaftsprüfung, Supplement 4 (2007), at 64-75; *Fachnachrichten IDW*, No. 11/2007, at 610-621, supplemented by principles for the valuation of customer-related intangibles (2009) and by technology-based intangibles valuation principles (2011); cf. *IDW Standard: Grundsätze zur Bewertung immaterieller Vermögenswerte (IDW S 5, 2011 version)*, *Fachnachrichten IDW*, No. 7/2011, at 467; ISO, *Brand valuation – Requirements for monetary brand valuation*, International Standard ISO 10668, 1st Edition (International Organization for Standardization 1 Sept. 2010); IVSC, *International Valuation Standard 210 Intangible Assets*, International Valuation Standards Council (London 2011). For a brief overview,

Also, the valuation of brands and other intangibles, their definition and ownership issues have received fresh attention in the context of the OECD Working Party No. 6's current efforts devoted to a revision of chapter VI, Transfer Pricing Aspects of Intangibles,⁹ in the OECD Transfer Pricing Guidelines by 2013, following the establishment of chapter IX, Transfer Pricing Aspects of Business Restructurings, in 2010. And finally, the valuation of brands and other intangibles is one important aspect in the framework of a cross-border exploitation of those intangibles among affiliated companies in a transfer pricing context, for example, by an acquisition/sale, licensing or business restructuring, in alignment with the arm's length principle.

With regard to these general objectives, the overarching research question is:

Why do companies value their brands – or why not?

More specifically, this empirical study strives to shed more light on the following issues:

- what relevance do brands have for companies as compared to other intangible assets;
- how important is brand value in relation to company value;
- which brand valuation purposes are relevant for companies;
- which valuation methods are employed in practice;
- who is doing the valuation and for whom;
- what benefits and drawbacks of brand valuation and respective results are considered by managers; and
- what is the managerial attitude towards a standardization of brand valuation.

Based on the author's research findings and the discussion thereof in view of existing literature, this article will provide some practical advice for managers who are considering a monetary valuation of their companies' brands and/or for tax authorities who are faced with (or request) a valuation of brands and other intangibles from corporate taxpayers.

1.3. Scope, structure and methodology of the study

This empirical study focuses on the monetary valuation of brands, as opposed to a purely behavioural, consumer- or expert-related assessment of brand value, which may be expressed in qualitative terms or as a certain score on an index scale. The stakeholder perspective taken is that of the management of a (potentially) brand(s)-owning company. From a geographic perspective, mostly large and listed companies all over Europe were targeted, with a focus on, but not limited to, Austria, Germany, Switzerland and the United Kingdom. Different industry sectors have been taken into account for the study, defined

see M. Lagarden and J. Menninger, *Brand valuation – a transfer pricing essential*, 13 *Transfer Pricing Intl. J.* 4 (Apr. 2012).

9. Compare OECD Working Party No. 6's recent discussion draft, Ctr. for Tax Policy and Admin., *Revision of the special considerations for intangibles in Chapter VI of the OECD Transfer Pricing Guidelines and related provisions* (2012), released 6 June 2012, available at www.oecd.org/dataoecd/39/61/50526258.pdf (accessed 27 June 2012).

according to the German Federal Statistical Office,¹⁰ as brands are considered to be relevant for advertising and differentiation purposes to a higher or lesser degree in all industry sectors.

The nature of the research conducted in this study is descriptive and explanatory, as main approaches to brand valuation have been extensively described in literature earlier, relying on established financial valuation theory.¹¹ Moreover, comparable empirical studies on brand valuation in business practice have already been performed in individual countries, as mentioned in section 1.2. Therefore, this study is reliant on a deductive approach and applying a quantitative research strategy to a current cross-sectional sample of companies in terms of industry sectors, and a snapshot view in terms of the timeline of this study.¹²

Section 1 of this article has provided an overview of the general topic of *brand valuation*, and serves as a stage-setter for the empirical investigation. The review of critical literature in section 2 forms the basis of deriving a model framework for the study to answer the research question(s). Chapter 3 briefly describes the research methodology and plan. And Section 4 presents the study findings and suitable statistical analysis to check for relationships and/or interdependencies in the data obtained. Alongside their presentation, the empirical results are discussed in more detail here, referring to the research questions and a review of critical literature, as well as their practical relevance in a transfer pricing context, where applicable. Finally, section 5 summarizes the main findings and provides concise recommendations and conclusions for management and tax authorities considering monetary brand valuation.

2. Literature Review

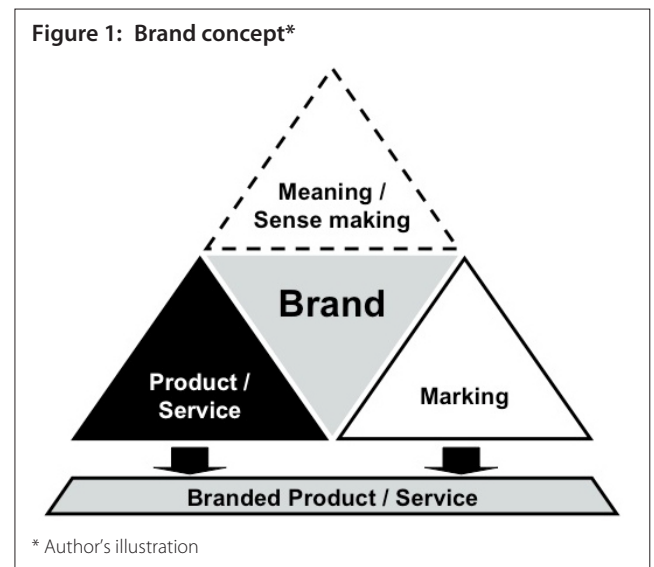
After a discussion of key concepts (the *what*) this section critically reviews main brand valuation purposes (the *why*), the stakeholders in brand valuation (the *who* or *for whom*) and brand valuation approaches/methods (the *how*). Finally, the main findings of prior empirical studies on brand valuation are analysed. This constitutes the foundation for research.

2.1. Key concepts

2.1.1. Brands

Before an asset is valued, it needs to be defined.¹³ This is especially important in the case of brands, which turn

out to be rather diverse concepts.¹⁴ In literature, a broad range of definitions has been provided over time to answer the question, “What constitutes a brand?”. Bentele et al., for example explain brands as the outcome of a two-step brand-building process. In the first step, a service (or product) is combined with distinct marking (for example, a trademark), leading to a branded service (or product). In a second step, this branded service (or product) together with an element of meaning (or sense making) ultimately results in the brand.¹⁵ Figure 1 illustrates this idea as a basis for the empirical study, from a static (modular) perspective.



The product/service element is the tangible offer to the customer, but it may also comprise elements such as underlying patents, processes, technology, product formulations, packaging, service descriptions and knowledge/information, on which the product/service is built. While the marking element reflects the legal definition of trademarks¹⁶ and points to the etymological origin of the term “brand”,¹⁷ it also comprises two main brand functions, namely information transmission (to customers; risk reduction) and identification (i.e. recognition and/

10. Destatis, *German Classification of Economic Activities*, Edition 2008 (WZ 2008), (German Federal Statistical Office (Destatis) 2008), following the European provisions of NACE Rev. 2 industry sector classification (Nomenclature générale des Activités économiques dans les Communautés Européennes Revision 2 (2006)); compare www.destatis.de/DE/Methoden/Klassifikationen/GueterWirtschaftsklassifikationen/Content75/KlassifikationWZ08.html?nn=173772 (accessed 20 Apr. 2012).
11. Compare A. Damodaran, *Investment Valuation*, 2nd edition (John Wiley & Sons 2002); A. Damodaran (2006), *supra* n. 5.
12. M. Saunders, P. Lewis and A. Thornhill, *Research Methods for Business Students* (4th edition, Prentice Hall 2007).
13. Compare M. Lagarden and J. Menninger, *supra* n. 8.

14. See G. Bentele, M.S. Buchele, J. Hoepfner and T. Liebert, *Markenwert und Markenwertermittlung*, 3. Auflage (Wiesbaden: Gabler 2009); Salinas, *supra* n. 3, at 1, 12; V. Trommsdorff, *Verfahren der Markenbewertung*, in Bruhn, M (editor) *Handbuch Markenführung*, 2. Auflage, volume 2 (Gabler 2004), at 1853-1875.
15. Bentele et al., *supra* n. 14, at 4.
16. Compare for example article 3 (1) of the German Trademark Code (*Markengesetz*): “Trademarks are all signs that are suited to distinguish a company’s goods or services from other companies’ goods or services [...]”; compare Köhler (at XIX) and Kriegbaum (at 27-30). See H. Köhler, *Einführung – II. Das Markenrecht*, in Beck-Texte/Deutscher Taschenbuch Verlag (2009) *Wettbewerbsrecht, Markenrecht und Kartellrecht*, at 30, Auflage (Munich: DTV 1 Sept. 2009); C. Kriegbaum, *Markencontrolling – Bewertung und Steuerung von Marken als immaterielle Vermögenswerte im Rahmen eines unternehmenswertorientierten Controlling* (Verlag Vahlen (Doctoral Thesis, University of Dresden 2001).
17. The Oxford Advanced Learner’s Dictionary of Current English (1992), at 106, defines a brand as “particular make of goods or their trade mark” and also refers to a “mark of identification [on animals] with a hot iron [...] also branding-iron”. And the Oxford Thesaurus (1991), at 38, provides “trade name, trademark, label, mark, [and] identify” as synonyms (noun or verb) for brand.

or differentiation versus competing offers).¹⁸ Finally, the additional meaning/sense-making element refers to brand images and perceptions in customers' minds (behavioural perspective),¹⁹ as well as to corporate reputation or image and to relations between stakeholders and organizations beyond a branded product/service on offer (for example communication, and public relations features, as well as sociological aspects²⁰).

This brief outline illustrates the dynamic and multifaceted nature of a brand as a bundle of intellectual property components. Other brand definitions found in literature address certain elements shown in Figure 1. Moreover, different types of brands can be distinguished, namely product or service brands, umbrella (house) brands, corporate brands or private labels, and no-name brands.²¹ Different approaches are suggested for the valuation of corporate brands as opposed to product/service brands.²² Likewise, different parameters (for example regarding the weighted average cost of capital (WACC) or useful life) need to be chosen for a valuation of different types of brands.²³ For the purpose of this study, however, brands are thought to comprise all brand types mentioned and they are considered as assets in the holistic sense of Figure 1.

2.1.2. Value and valuation

Value may have different meanings to different people. Indeed, it is not an objective concept.²⁴ And even though mathematical valuation models may intuitively be perceived as something objective or quantitative, many authors agree that this is not the case: Valuation and value always imply a subjective element.²⁵ The decisive determinants of value are *utility* and *desirability* or *preferability*, for example, of the brands or goods under consideration. In this context, value-driving factors are subjective need satisfaction conveyed by the brands, as well as their relative scarcity and demand for the brands in the marketplace. However, an absolute value may not be attributable to the brands, but only a relative value, for example, in the sense of a practical or utility value, which is subjective,

related to certain situational factors and to the level of demand.

Consequently, valuation requires a valuation object and a measurement scale for that object, related to the determinants of value (value-driving factors).²⁶ Moreover, different valuation methods can be employed to determine the value of a given brand. Therefore, valuation cross-checks based on different methods are advisable in order to increase the validity of the brand valuation result.²⁷ Also, an appropriate value concept needs to be defined as an underlying basis for the valuation of a brand,²⁸ such as (fair) market value, decision value, investment value or liquidation value.²⁹ The purpose of valuation determines the value concept and the choice of a suitable valuation method for a given brand.³⁰

Valuation is essentially a workflow, in which a result (output) is generated, based on certain input data (for example, asset-related sales, risk assessments, useful life of the asset to be valued) via a transformation process (for example, the choice of a value concept, valuation approach and specific method). And on the basis of the valuation result(s) decisions are taken by which management – or regulatory requirements will be fulfilled. Valuations always take place within a certain situational framework, which has been investigated in depth in the author's empirical study and will be discussed in more detail in sections 3 and 4.

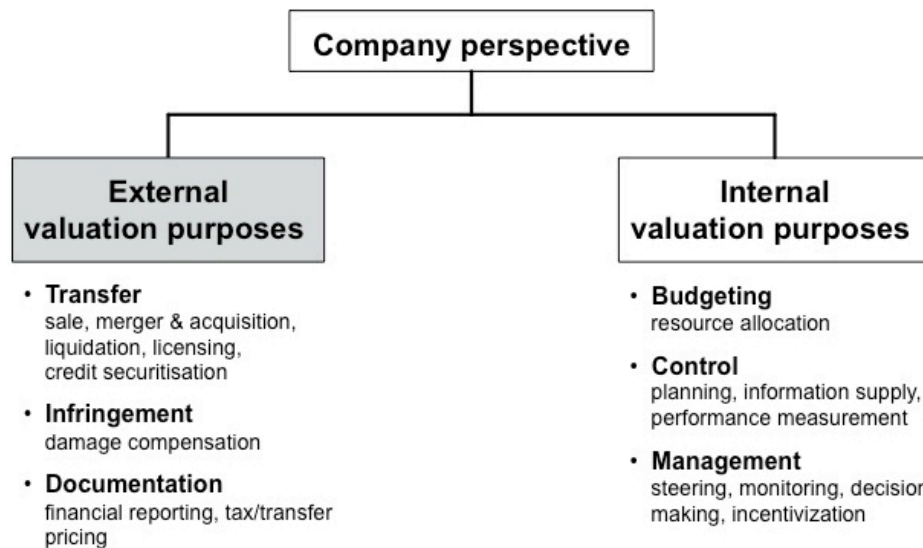
Cost, *value* and *price* are three terms that are often mentioned in this context. Costs are considered to be only a poor value indicator. A common example would be R&D expenses for projects, which may not always lead to successful products or services that add value to the company. Nevertheless, cost is normally considered in the pricing of goods, for example, in the determination of a minimum price from a seller's perspective.³¹ Finally, value may be reflected in a certain price at least partially, as this will depend upon the value-driving factors mentioned above.

Finally, one should bear in mind that valuations provide only estimations.³² The results of valuations should yield an approximation of real market conditions as good as possible, following well established valuation standards and practice, of course. But valuations should not be inter-

18. P. Sandner, *The Valuation of Intangible Assets – An Exploration of Patent and Trademark Portfolios*, 1. Auflage (Gabler, Doctoral Thesis, Ludwig-Maximilians-University Munich 2009), at 12-14; Kotler and Keller, *supra* n. 2, at 274-275.
 19. Trommsdorff, *supra* n. 14, at 1857.
 20. This may be illustrated by (but is not limited to) the example of the brands of non-profit organizations (for example, the Red Cross, Greenpeace). See for example, Bentele et al., *supra* n. 14, at 9.
 21. Kriegbaum, *supra* n. 16, at 39-45.
 22. Salinas, *supra* n. 3, at 109 and 363.
 23. Compare S. Beyer and J. Menninger, *Bewertung immaterieller Werte – das Konzept der Wirtschaftsprüfer (IDW S 5)*, in, *Immaterielle Vermögenswerte – Bewertung, Berichterstattung und Kommunikation* (K. Möller, M. Piwinger and A. Zerfuß eds., Schäffer-Pöschel 2009), at 113-123.
 24. R. Mills, *Brand Valuation*, Henley Management College, Manager Update Database, Accounting and Finance Section (Spring 2005, volume 16/3).
 25. P. Hammann, *Der Wert einer Marke aus betriebswirtschaftlicher und rechtlicher Sicht*, in, *Marke und Markenartikel als Instrumente des Wettbewerbs* (E. Dichtl and W. Eggers eds, Beck Verlag 1992), at 217; Damodaran, *supra* n. 11, at 2; D. Andriessen, *Making Sense of Intellectual Capital* (Elsevier Butterworth-Heinemann 2004), at 11; Trommsdorff, *supra* n. 14, at 1858-1859.

26. D. Andriessen, *IC valuation and measurement: classifying the state of the art*, 5 J. of Intellectual Capital 2 (2004), at 230-242.
 27. Compare R.F. Reilly and R.P. Schweihs, *Valuation of Trademarks and Trade Names*, 25 J. of Pension Planning and Compliance 4 (Winter 2000), at 35-49; Absatzwirtschaft et al., *supra* n. 6, at 164-168; IDW (2007), *supra* n. 8, at 619; ISO, *supra* n. 8, at 7.
 28. Compare Absatzwirtschaft et al., *supra* n. 6, at 13; IDW, *supra* n. 8, at 611-612; Beyer and Menninger, *supra* n. 23, at 117; ISO, *supra* n. 8, at 3.
 29. Compare IVSC, *IVS Framework*, International Valuation Standards Council (London, 2011), para. 26 et seq.; M. Lagarden, *Markenbewertung in der Unternehmenspraxis*, 1. Auflage (Wiesbaden, Gabler Verlag, 2011), at 23; P. Barwise, C. Higson, A. Likierman and P. Marsh, *Accounting for Brands* (London: London Business School and The Institute of Chartered Accountants in England and Wales, 1989), at 56.
 30. Compare Hammann, *supra* n. 25, at 217; IDW, *supra* n. 8, at 616.
 31. While the "suggested price" known from retail settings also includes a certain profit element and is a deliberate element of pricing strategy within the portfolio of marketing mix instruments.
 32. IVSC, *Valuation Uncertainty*, Discussion Paper, International Valuation Standards Council (London, Sept. 2010), at 4.

Figure 2: Brand valuation purposes*



* Author's illustration

preted as “true” or “given” in an absolute sense. It is the diversity of valuation situations and framework conditions, in parallel to the subjectivity element mentioned, which is the underlying reason why brand valuation will inevitably lead to varying valuation results, i.e. depending on stakeholders involved and their respective valuation purposes.³³

2.2. Valuation purposes

According to legal requirements and internationally accepted accounting standards (for example IAS 38, IFRS 3), brands must be separately recognized on a company's balance sheets if they have been acquired either as individual intangible assets or as part of a business combination. Moreover, the OECD Guidelines as well as various domestic tax regulations³⁴ call for a monetary valuation of intangibles like brand names or trademarks to establish their (fair) market value upon respective cross-border transfers between affiliated companies at arm's length. In addition to these major financial and tax accounting-related brand valuation purposes, prior empirical studies have investigated additional purposes of brand valuation in business practice.³⁵

Several authors have discussed a range of conceivable brand valuation purposes over time which, ultimately, may apply not only for brands, but for other intangible assets³⁶ as well. And Sattler, for example, pleads in favour of establishing a monetary brand value for all purposes, due to an enhanced information content compared to non-monetary measures. He also provides a framework to distinguish external and internal brand valuation purposes, and considers the value dimension (monetary or non-monetary), time frame (short or long term), brand-transfer potential (with or without considering product line extensions) and special elements (cause and effect analyses) with respect to brand valuation requirements and valuation purposes.³⁷

Moreover, various authors have pointed out that monitoring shareholder value and value-based management constitute important purposes for the valuation of brands as a basis for managerial decision making.³⁸ However, valuation for accounting or tax purposes, merely relying on financial input parameters, will have little explanatory or predictive potential. As this kind of valuation is detached from customer-related input data, it cannot shed light on the root-causes of brand value.³⁹ Therefore, it may be well suited to satisfy external valuation requirements, but it

33. Trommsdorff, *supra* n. 14, at 1858-1859; O. Heil and K.-H. Maul, *Pro und Contra – Brauchen wir eine Standardisierung der Markenbewertung?*, Absatzwirtschaft, No. 2 (2004), at 30-32.

34. OECD, *Special Considerations for Intangible Property (chapter VI and annex)*, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, revised edition (Organisation For Economic Co-Operation And Development, OECD Publishing July 2010); US Treasury Regulations section 1-428-4 (Methods to determine taxable income in connection with a transfer of intangible property), Internal Revenue Code, section 482, title 26, chapter I, part 1, 26 CFR 1.482-4; German Federal Ministry of Finance (*Bundesministerium der Finanzen*, BMF), *Verwaltungsgrundsätze Funktionsverlagerung* (Berlin: 13 Oct. 2010).

35. Compare, for example, PricewaterhouseCoopers, H. Sattler, GfK Marktforschung and Markenverband e.V., *Praxis von Markenbewertung und Markenmanagement in Deutschen Unternehmen – Neue Befragung 2005* (PricewaterhouseCoopers, 2006).

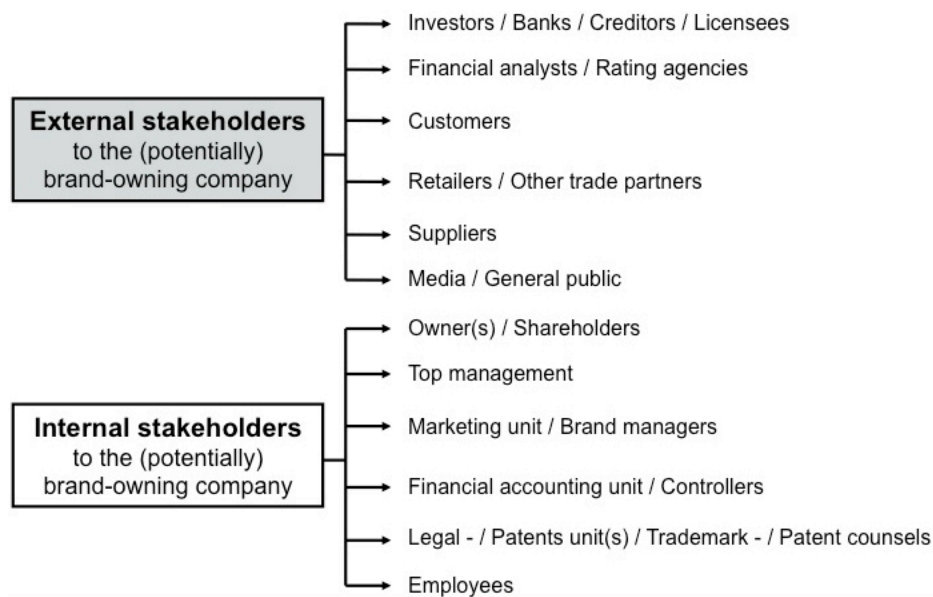
36. For example, H. Sattler, *Markenbewertung*, 65 Zeitschrift für Betriebswirtschaft 6 (1995), at 663-682; M. Kranz, *Markenbewertung – Bestandsaufnahme und kritische Würdigung*, in *Markenmanagement*, 1. Auflage (H. Meffert, C. Burmann and M. Koers eds., Gabler 2002) at 429-458; J. Menninger, *Markenbewertung: Methoden und Standards*, in *Wertschöpfung durch Kommunikation* (J. Pfannenberg and A. Zerfaß eds., Frankfurter Allgemeine Zeitung 2010), at 140-152.

37. See Sattler (1995), *supra* n. 36, at 667, 669; Kranz, *supra* n. 36, at 439.

38. For example, T. Jenner, *Markenführung in Zeiten des Shareholder Value*, 23 Harvard Business Manager 3 (2001), at 54-63; Trommsdorff, *supra* n. 14, at 1855-1856, 1861; Mills, *supra* n. 24; Beyer and Menninger, *supra* n. 23, at 114-115.

39. Compare for example Hammann, *supra* n. 25, at 249; Sattler (1995), *supra* n. 36, at 668; Kranz, *supra* n. 36, at 438; or T. Tomczak, S. Reinecke and P. Kaetzke, *Markencontrolling*, in *Handbuch Markenführung*, 2. Auflage, volume 2, (M. Bruhn ed., Gabler 2004), at 1833-1852.

Figure 3: Brand valuation stakeholders*



* Author's illustration

will not add much value regarding internal brand management. Finally, the categorization into *external* and *internal* valuation purposes is elaborated upon in the following illustration and analysed within the framework of the author's empirical study in more detail (see section 4), to learn more about why companies may (or may not) engage in brand valuation.

2.3. Valuation stakeholders

An important group of institutional brand valuation stakeholders consists of *governments* as providers of a respective legal framework (for example, tax or trade laws, transfer pricing regulations), *fiscal and tax authorities*, *legal bodies* and *standard setters* (for example, IASB, IDW, ISO). These stakeholders have a public and/or professional interest in the valuation of brands and other intangible assets, along the lines of general value concepts, for example, *(fair) market value* and in line with the arm's length principle, as well as laws or public regulations.

Menninger and Robers provide a comprehensive categorization into *external* and *internal* stakeholders interested in monetary brand valuation.⁴⁰ Nevertheless, their stakeholder list can be extended by a company's legal or patent unit(s) as internal stakeholders, and retailers or other trade partners and suppliers as external stakeholders, as shown in Figure 3, where the mentioned institutional stakeholders may be subsumed under the heading "general public".

Other authors discuss individual brand valuation stakeholder groups, their features and potential interests in

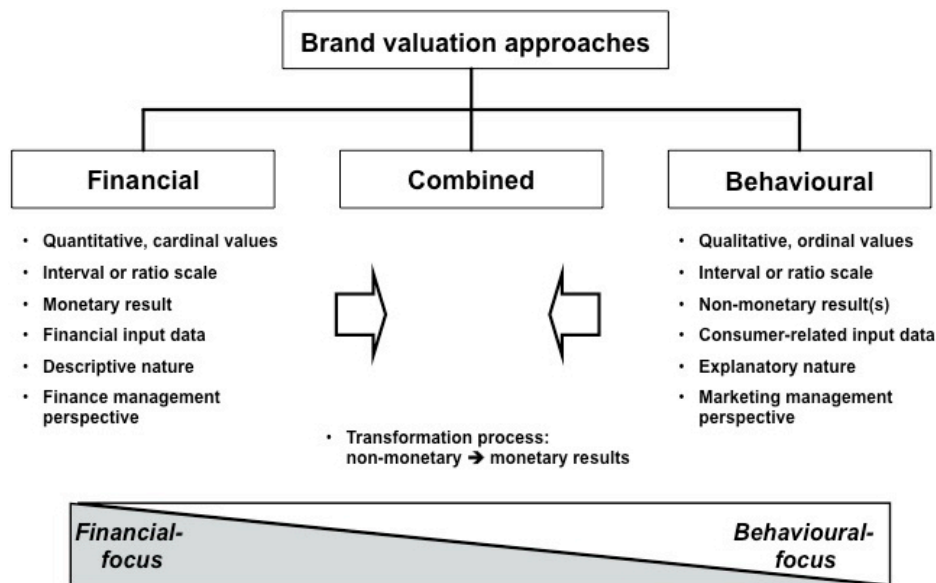
more detail.⁴¹ In this context, Kranz touches upon a valid point, with regard to (brand) valuation providers as stakeholders. Their promotion of the valuation of intangibles is, of course, driven by vital business interests, for as providers "strive to set (their) standards for brand valuation [...] the one who succeeds in establishing such standard in the market will open up an enormous sales potential for himself".⁴² Even though it will largely depend on one's viewpoint what an enormous sales potential could mean in reality, the latter argument may explain why a large number of brand valuation methods have been published during the last 20 years, and that the move to standardized brand valuation has been (and is) rather sluggish.⁴³ At the same time, such standardization is welcomed by commercial brand valuation providers as well, in order to add to the credibility of valuation providers and their growing audience.⁴⁴

Also, it should be obvious that the institutional stakeholders mentioned will request a transparent valuation of intangibles with their respective national and public interests in mind, to support an arm's length pricing of these assets in cross-border intercompany transactions. While this is easy to understand, it will inevitably contribute to an increased number of bilateral or multilateral dispute resolution processes, like mutual agreement procedures or advance pricing agreements. This is due to the simple reason that the understanding of what constitutes an arm's length price (and thus, a (fair) share of taxable income) will vary from one jurisdiction to the next, depending not only

40. J. Menninger and D. Robers, *Markenwert – Paradigmenwechsel im Marketing?*, in *Die Bedeutung der Tradition für die Markenkommunikation*, 1. Auflage (N. Herbrand, and S. Röhrig eds, Edition Neues Fachwissen 2006).

41. See Barwise et al. (1989) *supra* n. 29, *Accounting for Brands*, at 6-7 and 49-51; M. Bourke, *Is Brand Valuation of Any Use to the Investor?*, in *Brand Valuation*, 2nd edition (J. Murphy ed., Business Books Limited, 1991), at 90, 99, 101.
 42. Kranz, *supra* n. 36, at 432-433 (author's translation).
 43. See for example D. Haigh, *Valuation: Setting a Standard of Value*, Brand Strategy (London: 8 Sept. 2008), at 38-39; Bentele et al., *supra* n. 14, at 178-191.
 44. See Haigh, in Salinas, *supra* n. 3, at xxii.

Figure 4: General brand valuation approaches*



* Author's illustration

on the factual basis as established by the taxpayer, but also on the different fiscal parties involved.

In the author's empirical study the focus is on (potentially) brand-owning companies as stakeholders, and more specifically on managers in the finance function in these companies. The author's assumption is that finance managers will be involved in monetary brand valuation, either due to their potential expertise in valuation methods or their managerial responsibility for this matter.⁴⁵ This focus is to some extent different from prior empirical studies which have often targeted companies' marketing managers and functions.⁴⁶

As all stakeholders will have their own subjective ideas of a brand's value and differing objectives regarding brand utilization and brand valuation, this is leading the way to a closer look at brand valuation approaches and methods.

2.4. Valuation approaches and methods

Below, several perspectives for a categorization of general brand valuation approaches provided in literature are critically reviewed. Within this framework, specific brand valuation methods frequently encountered in practice are discussed. Finally, the present status of brand valuation standardization efforts is analysed.

2.4.1. Taxonomy of brand valuation approaches

A basic taxonomy of brand valuation may distinguish between quantitative financially-oriented, qualitative behavioural/consumer-oriented approaches and a combination of the former two, as shown in Figure 4.⁴⁷ While purely financially oriented, descriptive valuation approaches deliver a brand value in monetary terms, pure behavioural explanatory approaches do not aim for monetary brand values, but try to explain consumer-related elements of brand equity⁴⁸ and deliver values on an ordinal level, that is, relative rankings or indices. Combined approaches often work in a two-step fashion. First, a qualitative behavioural measure is determined, which is then transformed into a monetary value in the second step, for example, via purchasing probabilities and prices for branded goods.⁴⁹ Such transformation of qualitative information into monetary terms will also be required when reflecting other value-relevant information in the final value of the intangible asset under consideration (for example, legal protection for a given brand, in terms of contractual (codified) protection, geographic scope and/or duration of the protection).

45. Compare A. Voegelé, S. Harshbarger and N. Mert-Beydilli, *How to Use Transfer Pricing to Calculate the Value of a Brand*, International Tax Review (Dec. 2006), at 3-6; D. Green and A. Hughes, *What's in a brand? Getting the most out of a group brand*, Transfer Pricing International Journal (24 June 2010).

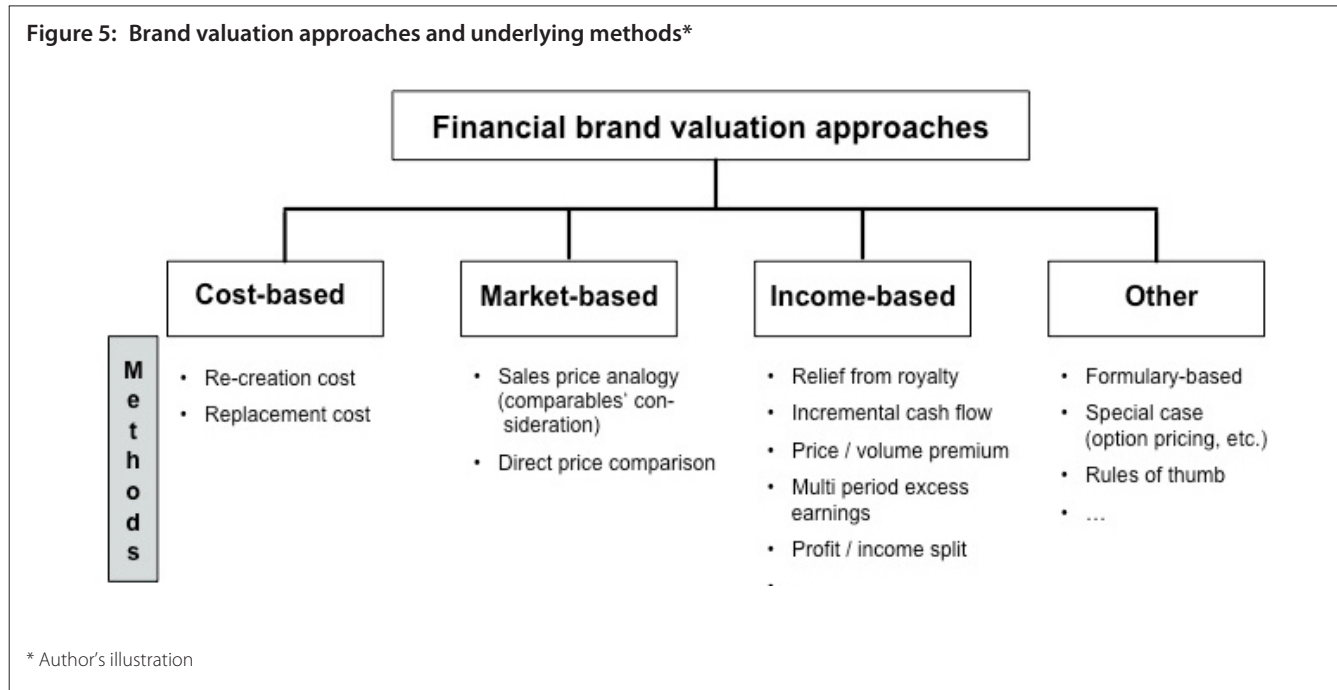
46. Compare N. Drees, *Markenbewertung und Markenberatung in Deutschland – Ergebnisse einer empirischen Studie und Begriff des Markenwertes und Modelle zur Markenwertermittlung*, Fachhochschule Erfurt (University of Applied Sciences), Erfurter Hefte zum angewandten Marketing, Heft 6 (1999); A. Schimansky, *Der Wert der Marke* (Vahlen 2004).

47. Compare for example, Y. Cheridito, *Markenbewertung: Umfassendes Konzept zur Markenbewertung und empirische Studie bei Schweizer Publikumsgesellschaften* (Haupt Verlag, Doctoral thesis, University of Zürich 2003), at 99, 111, 147; M. Meister and C. Zimmermann, *Brand Valuation – Bestandesaufnahme und innovative Ansätze* (VDM 2008).

48. According to several authors, "brand equity" is a broad term, comprising "brand value (the figure on the balance sheet), brand strength (customer attitudes and behaviour) and brand descriptions and associations". See S. Foreman, *Broadening the Scope of Branding*, Henley Management College, Manager Update Database, Marketing Section (Winter 2005, volume 17/2), as well as different stakeholder perspectives. See for example, R.D. Raggio and P.L. Leone, *The theoretical separation of brand equity and brand value: Managerial implications for strategic planning*, 14 J. of Brand Management 5 (May 2007), at 380-395.

49. Sattler, *supra* n. 36, at 670.

Figure 5: Brand valuation approaches and underlying methods*



Most authors, however, discuss three basic monetary brand valuation approaches,⁵⁰ namely a cost-based approach, a market-based approach and an income-based (economic use) approach.

The *cost-based approach* uses creation or re-establishment costs to determine the value of a brand. The *market-based approach* refers to an analysis of (directly or approximately) comparable brand acquisition or sales transactions for establishing the value. Finally, the *income-based (economic use) approach* is related to a determination of the economic value of income from a brand. An overview is provided in Figure 5.

In addition to the three main valuation approaches, other more singular valuation approaches may rely on certain formulae prescribed for valuation, option pricing models or capital market data (for example, share price developments) as a basis for valuation, or even rules of thumb, which may be based to some extent on empirical observations (for example, *Goldscheider's rule* or *Knoppe's formula*).⁵¹ Individual brand valuation methods are discussed below.

2.4.2. Brand valuation methods

Based on the range of available approaches outlined above, a given brand (or other intangible asset) may be valued using various methods. The resulting values will vary depending on the nature of the brand (corporate, umbrella or product brand), the valuation purpose,

assumptions considered in the valuation process, available data and input parameters selected, as well as the approach and corresponding method chosen.⁵²

Even if the brand and its intellectual property components can be clearly defined, their valuation remains a subjective exercise.⁵³ However, this is not necessarily a problem for either external or internal valuation purposes, if underlying assumptions are made transparent.⁵⁴ The main valuation issues remain with regard to a reliable identification, separation and prognosis of brand value drivers; brand-related cash flows; profits, costs, savings or future growth rates; respective discounting and risk quantification; and the useful life of the asset taken into consideration, as pointed out by several authors.⁵⁵ In this context, valuation standards provide valuable guidance (see section 2.5.).

The relief from the royalty (or royalty payment) method (falling under the category of income-based valuation approaches, despite the fact that it also refers to market-based royalty rates) seems to be widely used in brand valuation practice.⁵⁶ But it may also be used for the valuation of technology-related intangibles such as patents.⁵⁷ While Sattler and Salinas acknowledge the advantages of this method in terms of its simplicity and ease of application,

50. For example, Reilly and Schweih, *supra* n. 27, at 39; G. Bick and R. Abratt, *Valuing Brands and Brand Equity: Methods and Processes*, 8 J. of Applied Management and Entrepreneurship 1 (Jan. 2003), at 21-39; H. Sattler (2005), *Markenbewertung: State of the Art*, Zeitschrift für Betriebswirtschaft (Special Issue 2/2005), at 33-57; Salinas, *supra* n. 3, at 58.

51. See the analysis of available market data by R. Goldscheider, J. Jarosz, C. Mulhern) *Use of the 25 per cent rule in valuing IP*, Les Nouvelles, volume 37 (2002), at 123-133; Lagarden, *supra* n. 29, at 45-46.

52. Compare Reilly and Schweih, *supra* n. 27, at 49; Trommsdorff, *supra* n. 14, at 1856-1857; or Salinas, *supra* n. 3, at 109, 363.

53. See Barwise et al., *supra* n. 29, at 70, 76-78; IVSC (2010), *supra* n. 32, at 4.

54. Bick and Abratt, *supra* n. 50, at 36.

55. Like Barwise et al., *supra* n. 29, at 38, 57, 66; Sattler (1995), *supra* n. 36, at 670, 674-678 and (2005), *supra* n. 50, at 42, 52-54; Bick and Abratt, *supra* n. 50, at 34-36; IDW, *supra* n. 8, at 619; Beyer and Menninger, *supra* n. 23, at 120-121.

56. T. Harms, *Consumer products IFRS financial statements survey November 2010*, 3rd edition, Ernst & Young (2010), at 20, available at [www.ey.com/Publication/vwLUAssets/ifrs_cp_ifrs_financial_statements_survey_nov_2010/\\$FILE/cp%20ifrs%20financial%20statements%20survey%20nov%202010.pdf](http://www.ey.com/Publication/vwLUAssets/ifrs_cp_ifrs_financial_statements_survey_nov_2010/$FILE/cp%20ifrs%20financial%20statements%20survey%20nov%202010.pdf) (accessed 27 June 2012); Salinas, *supra* n. 3, at 56.

57. H. Wirtz, *Die monetäre Bewertung technologie-basierter immaterieller Vermögenswerte*, 54 Zeitschrift für Controlling und Management 4 (2010), at 224-228.

both authors also point out its deficiencies, such as limited comparable brand-related market data (royalty rates) and subjectivity in selecting a range of potentially applicable royalty rates in any given case.⁵⁸

Several authors favour valuation methods related to the income-based approach. These methods rely on the well established discounted cash flow calculation ((net) present value determination), and as such they are future oriented and provide a better approximation of the economic value of a brand. However, depending on the lifecycle stage of a given intangible (i.e. either more remote from, or closer to actual market introduction) or with regard to the question of valuing intangibles that are held for defence purposes only,⁵⁹ cost-based valuation methods should also be taken into consideration. As an extreme and surely controversially debatable position, it could be argued that an inactive brand, which is not (or has never been) advertised, bears only a certain cost value related to its internal set-up and administration within the company and its formal registration with domestic or international brand inventories, or even no value at all.

At least, market-based or cost-based approaches or methods are suggested for approximation or plausibility-check purposes in literature, to double check valuation results obtained employing an income-based valuation method.⁶⁰ Nevertheless, the choice will ultimately depend on the brand valuation purpose, taking into account the validity and reliability of potentially available methods, their fitness-for-purpose, the scope, availability, quality and verifiability of required valuation input parameters and, last but not least, the relative simplicity and transparency of the method, its cost-benefit relation and the speed of the valuation process.⁶¹

These considerations lead to a closer look at standardization efforts in brand valuation.

2.5. Standardization of brand valuation

More than twenty years ago, Barwise et al. already considered the possibility that a suitable brand valuation method could be established as a basis for a standard, despite the problems that a valuation of brands (or other intangibles) poses from an accounting perspective.⁶² Later in 2004, Trommsdorff argued that a standardization of brand valuation methods “is desirable, but utopic”, due to the broad range and special valuation requirements of brand types, valuation stakeholders and different valuation situations.⁶³ Nevertheless, formulary-based brand valuation methods have been published as national standards in

Japan and Austria in recent years for example.⁶⁴ By contrast, the IDW in Germany published its standard S5 in 2007, which is explicitly based on management science-related brand valuation principles and became an established guideline for commercial valuation service providers, including major advisory companies in Germany. Meanwhile, the scope of IDW S5 has been expanded to cover the valuation of technology-related and customer-related intangibles⁶⁵ as well.

On an international level, the ISO published the draft standard ISO 10668 in 2010, providing a detailed framework of basic requirements for monetary brand valuation. The International Valuation Standards Council (IVSC) in London also published a modular valuation standard in 2011, related to general principles of valuation and, more specifically, to the valuation of intangibles, among other types of assets.⁶⁶ These initiatives reflect a clear trend regarding the future of brand valuation, which should be beneficial for commercial valuation providers in terms of enhanced credibility and more confidence on the side of brand valuation recipients as their clients.⁶⁷ However, a valuation standard does not give a detailed technical (nor calculatory) prescription for valuing brands or other intangibles. Rather, definitions, principles and framework conditions which constitute the basis for a valuation according to professional best practice are described. In other words, these standards are not designed to provide detailed cooking recipes, but rather an outline of the kitchen set-up that is needed to cook a good dinner.

Nevertheless, the basic goals of standardization are the same for financial standard setters and for the OECD in its current project on chapter VI (Transfer Pricing Aspects of Intangibles), namely trust building; greater transparency; establishment of uniform definitions and principles as best practice guidance; convergence of varying approaches to intangibles in transfer pricing; and information transfer as well as information asymmetry reduction between parties involved.

2.6. Prior empirical studies on brand valuation

From 1998 to 2005, six empirical studies on brand valuation, its perceived importance, purposes, and methods employed, stakeholders, reasons for (not) doing brand valuation and awareness of standardization efforts were conducted in Germany and Switzerland.⁶⁸ The main findings are briefly reviewed here, as they provide relevant background for the empirical research presented in this article, in terms of content and geographical scope.

58. H. Sattler (2005), *supra* n. 50, at 47-48; Salinas, *supra* n. 3, at 70-82.

59. In order to claim certain fields of application and to exclude competitors from these – from the perspective of the legal holder of such “defensive” or “passive” brands or other intangibles.

60. Sattler (2005), *supra* n. 50, at 52; IDW, *supra* n. 8, at 617; ISO, *supra* n. 8, at 6-7.

61. Trommsdorff, *supra* n. 14, at 1864; Sattler (2005), *supra* n. 50, at 37-38.

62. Barwise et al., *supra* n. 29, at 77.

63. Trommsdorff, *supra* n. 14, at 1856, 1866. See also Bentele et. al, *supra* n. 14, at 169-171; Salinas, *supra* n. 3, at 398.

64. Japan: See F. Beccacece, E. Borgonovo and F. Reggiani, *Risk Analysis in Brand Valuation*, revised version (Bocconi University, Milan, Italy, 28 October 2006), at 4-8, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=931023 (accessed 21 January 2010); Austria: ONR 16800; compare Salinas, *supra* n. 3, at 292.

65. See M. Lagarden and J. Menninger, *supra* n. 8.

66. Id.

67. See for example B. Liodice, *Ten reasons marketers should establish generally accepted brand-valuation standards*, 81 Advertising Age 25 (21 June 2010), at 26; Salinas, *supra* n. 3, at xxii-xxiii, 397.

68. Compare M. Lagarden, *supra* n. 29, at 49, 147-149.

The earlier studies found that most companies did not value their brands, even if this was considered an important topic by the majority of respondents. This is not surprising, as international accounting requirements to recognize acquired brands on the balance sheet separately from other goodwill were introduced only in 2004 (see IAS 38, IFRS 3). These studies also investigated the reasons why companies did not value their brands.⁶⁹ The main reasons given were the lack of an established, suitable or reliable valuation method, overly burdensome requirements with regard to costs and time, overly volatile brand values, little relevance of the topic for the respective responding company, or little knowledge or awareness of brand valuation methods.

With respect to valuation purposes, brand management (including budgeting); internal control and reporting; mergers and acquisitions; and licensing were mentioned most often in all studies (see Figure 2). This is in alignment with major brand valuation purposes discussed in literature. The predominance of internal or management valuation purposes ahead of accounting purposes, however, may also be due to the fact that the studies – except for Cheridito's – primarily addressed *marketing professionals* as respondents, who will not normally be much concerned with monetary valuations for accounting, external reporting, tax or litigation purposes.

Brand valuation is done mainly by internal employees supported by third parties.⁷⁰ While Günther and Kriegbaum-Kling, as well as PricewaterhouseCoopers et al. reported that even among companies employing brand

valuation, *non-monetary* valuation was more widespread than monetary valuation, Cheridito mentioned in his Swiss study published in 2003 that in most cases brand valuation resulted in a quantitative (monetary) value. According to his findings with regard to the three basic approaches to brand valuation, monetary brand valuation is mainly done by referring to an income approach and applying a discounted cash flow method.

PricewaterhouseCoopers et al. also investigated the knowledge of managers regarding institutions working on brand valuation standards in Germany in 2005.⁷¹ The majority of respondents were aware of at least one of several institutions. Moreover, there was a high level of agreement among respondents that standardization of monetary brand valuation is (very) important, as well as generally accepted monetary brand valuation methods. This finding is also backed by the fact that the “lack of suitable brand valuation methods” as prime reason for not performing brand valuation in 1998 has changed position with “brand valuation is too costly and time consuming” in 2005.⁷² The PricewaterhouseCoopers study was recently repeated in Germany.⁷³

The results of these empirical studies and literature findings provided a starting point and framework for orientation with regard to the author's research plan and empirical study which will be presented in the following sections, in the next issue of the *International Transfer Pricing Journal*. Indeed, the second part of this article will focus on research design; study findings, analysis, and discussion; and the author's recommendations.

69. T. Günther and C. Kriegbaum-Kling, *Brand Valuation and Control: An Empirical Study*, 53 Schmalenbach Business Review 4, ZFBF (Zeitschrift für Betriebswirtschaftliche Forschung), (Oct. 2001), at 263-294; PricewaterhouseCoopers and H. Sattler, *Praxis von Markenbewertung und Markenmanagement in Deutschen Unternehmen*, 2. Auflage (Fachverlag Moderne Wirtschaft, 2001); PricewaterhouseCoopers, et al. (2006), *supra* n. 35; Cheridito, *supra* n. 47; Schimansky, *supra* n. 46.

70. Compare Günther and Kriegbaum-Kling, *supra* n. 69.

71. PricewaterhouseCoopers et al. (2006), *supra* n. 35.

72. Id.

73. PricewaterhouseCoopers, *Markenstudie 2012*, (J. Menninger, N. Reiter, H. Sattler, S. Högl and D. Klepper eds., PricewaterhouseCoopers AG Wirtschaftsprüfungsgesellschaft 2012).