

The Intangible Economy: US Policies and Proposals

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Exploring the promises and pitfalls of the global information economy

www.athenaalliance.org

Financing economic development through Intellectual Property assets

IP Finance Institute

Politecnico di Torino

May 28, 2009

Intangibles Are More Than IP

FASB list of intangibles

A. Marketing-related intangible assets

- (1) Trademarks, tradenames
- (2) Service marks, collective marks, certification marks
- (3) Trade dress (unique color, shape, or package design)
- (4) Newspaper mastheads
- (5) Internet domain names
- (6) Noncompetition agreements

B. Customer-related intangible assets

- (1) Customer lists
- (2) Order or production backlog
- (3) Customer contracts and related customer relationships
- (4) Noncontractual customer relationships

C. Artistic-related intangible assets

- (1) Plays, operas, ballets
- (2) Books, magazines, newspapers, other literary works
- (3) Musical works such as compositions, song lyrics, advertising jingles
- (4) Pictures, photographs
- (5) Video and audiovisual material, including motion pictures, music videos, television programs

D. Contract-based intangible assets

- (1) Licensing, royalty, standstill agreements
- (2) Advertising, construction, management, service, or supply contracts
- (3) Lease agreements
- (4) Construction permits
- (5) Franchise agreements
- (6) Operating and broadcast rights
- (7) Use rights, such as drilling, water, air, mineral, timber cutting, and route authorities
- (8) Servicing contracts, such as mortgage servicing contracts
- (9) Employment contracts

E. Technology-based intangible assets

- (1) **Patented technology**
- (2) Computer software and mask works
- (3) Unpatented technology
- (4) Databases, including title plants
- (5) Trade secrets, such as secret formulas, processes, and recipes.

Intellectual Capital Framework

❖ Human Capital

❖ Structural Capital

❖ Relationship Capital

Corrado, Hulten, and Sichel

Computerized information

1. Computer software: own use, purchased, and custom software.
2. Computerized databases

Scientific and creative property

3. Science and engineering research and development (costs of new products and new production processes, usually leading to a patent or license):
4. Mineral exploration (spending for the acquisition of new reserves)
5. Copyright and license costs (spending for the development of entertainment and artistic originals, usually leading to a copyright or license): Development costs in the motion picture industry, development costs in the radio and television, sound recording, and book publishing industries.
6. Other product development, design, and research expenses (not necessarily leading to a patent or copyright): New product development costs , new architectural and engineering designs, R&D in social sciences and humanities

Economic competencies

7. Brand equity (advertising expenditures and market research for the development of brands and trademarks)
8. Firm-specific human capital (costs of developing workforce skills, i.e., on-the-job training and tuition payments for job-related education)
9. Organizational structure (costs of organizational change and development; company formation expenses)

See Carol A. Corrado, Charles R. Hulten, and Daniel E. Sichel, “Measuring Capital and Technology: An Expanded Framework,” Federal Reserve Board, August 2004, and
... “Intangible Capital and Economic Growth” NBER Working Paper No. 11948 January 2006

What is Happening with Intangibles?

Measurement and Management



“Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist.”

—John Maynard Keynes

Measurement

“Investments in innovation, or knowledge-based activities, are thought to be important engines of economic growth. Yet very little is understood about their role in the economy. Much of the growth that the U.S. economy has experienced in the last 10 years is not captured by traditional economic measures—many economists believe that as much as 40 percent of that unexplained growth can be accounted for by knowledge-based activities.



Understanding the role of these activities in the economy is critical to accurately measuring and encouraging a strong U.S. economy.”

—Bureau of Economic Statistics

Size of Investments

Leonard Nakamura, Philadelphia Fed: the value of US gross investments in intangibles is over **\$1 trillion annually**

Corrado, Hulten, and Sichel: **\$3 trillion missing from our accounting of capital stock**

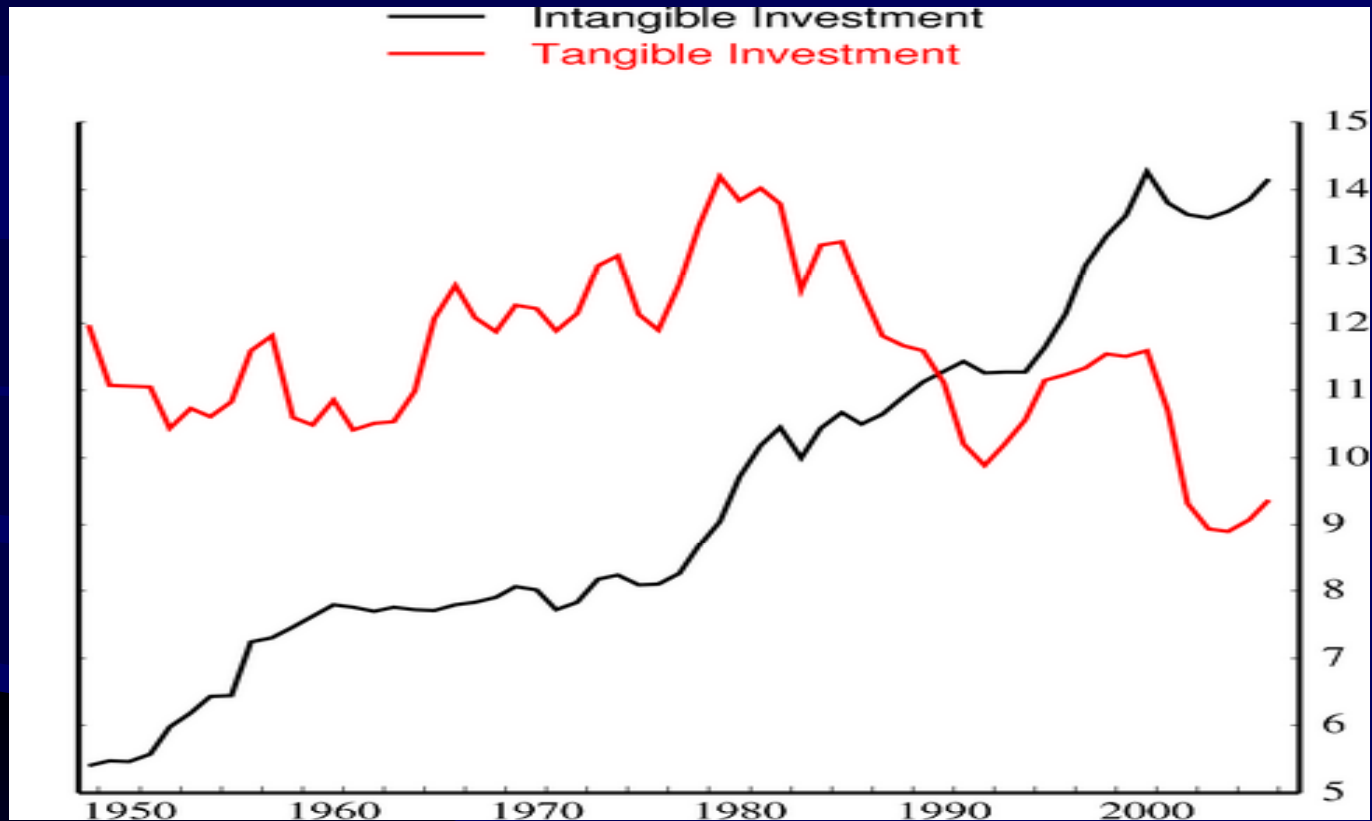
Leonard Nakamura, "A Trillion Dollars a Year in Intangible Investment and the New Economy," in John Hand and Baruch Lev, editors. *Intangible Assets: Values, Measures and Risks*, Oxford University Press, 2003.

Carol A. Corrado, Charles R. Hulten, and Daniel E. Sichel, "Measuring Capital and Technology: An Expanded Framework," Federal Reserve Board, August 2004, and

... "Intangible Capital and Economic Growth" NBER Working Paper No. 11948 January 2006

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Business investment in the US, tangible and intangible investment (% business output)



From OECD, *Intellectual Assets and Value Creation*, March 23, 2008

Based on Carol A. Corrado, Charles R. Hulten, and Daniel E. Sichel, "Measuring Capital and Technology: An Expanded Framework," Federal Reserve Board, August 2004, and

... "Intangible Capital and Economic Growth" NBER Working Paper No. 11948 January 2006

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Intangibles in GDP - BEA's Work

- ❖ Include R&D as an asset (rather than an expense) in GDP by 2013
- ❖ Include investments in motion pictures and sound recordings in GDP by 2013
- ❖ Research on framework for other intangibles
- ❖ Research on innovation metrics

Federal Investment in Intangibles

\$261 billion in FY 2006

\$250 billion in FY 2008

26% of discretionary spending in FY2006

44% of nondefense spending in FY2006

21% of discretionary spending in FY2008

35% of nondefense spending in FY2008

Federal Investment in Intangibles

Outlays in Billions(rough estimates)

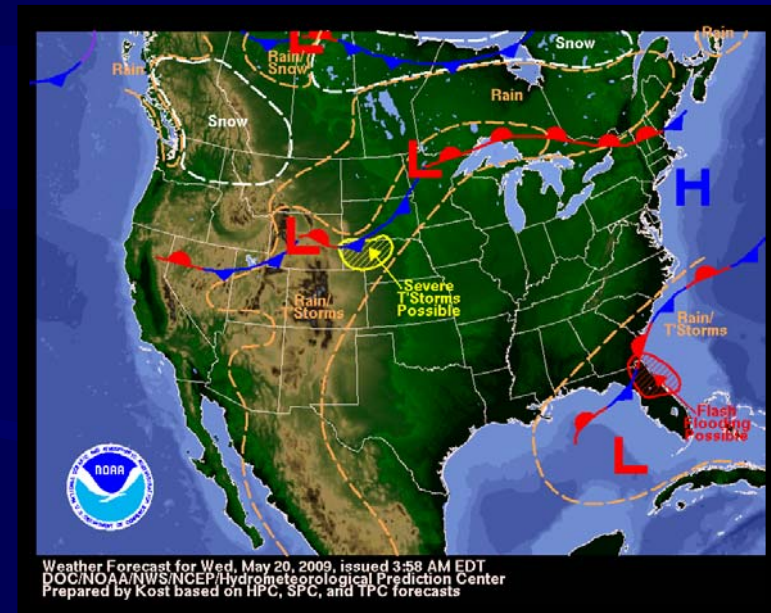
	FY2006	FY2008
Information and intellectual property		
R&D funding (does not include facilities and equipment)		
Defense	\$73.0	\$79.6
Nondefense	\$49.8	\$55.3
Arts & humanities/museum funding (including Smithsonian)	\$1.0	\$0.7
Government information creation		
Statistical agencies	\$2.2	\$2.9
Weather service	\$0.7	\$0.8
Library of Congress/CBO/GAO	\$1.0	\$1.0
PTO	\$1.6	\$1.9
Individual Human Capital (know-how)		
Education and training		
Grants to state and local governments	\$56.2	\$54.6
Direct Federal outlays	\$61.0	\$36.4
Training of government personnel (military)	\$9.0	\$10.7
Social Capital (Alliances & Networks) Organizational capacity building & technical assistance		
Community (HUD, EDA, HHS, USDA extension service)	\$0.5	\$0.5
Company (MEP, SBA)	\$0.5	\$0.5
Brands and marketing - reputation		
Export promotion	\$1.5	\$1.3
Product safety, food safety, drug safety (investments in product reputation)	\$3.0	\$3.3
Total	\$261.0 billion	\$249.5 billion

Does not include tax expenditures or value of landing slots, grazing rights, water rights, mining rights, spectrum and broadcast licenses, etc.

Management of Intangibles in the US

Who Owns Public Information?

- ❖ Weather data
- ❖ SEC data



Intellectual Property from Government-Funded Research

- ❖ Bayh Dole -- should it be rewritten?
- ❖ NASA OceanTomo auctions -- alternative commercialisation





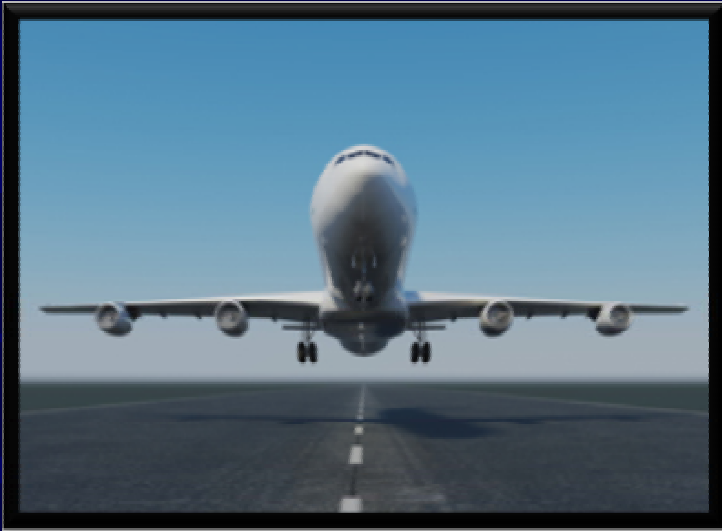
Government Brands and Trademarks

- ❖ Smoky the Bear & Woody Owl
- ❖ Presidential Seal
- ❖ FBI



18 USC CHAPTER 33

Airport Landing Rights



❖ GAO opinion on airport landing rights - not “property”

Back door funding mechanism

Cap and Trade System

❖ A new intangible literally from thin air



❖ Is the trading oversight system ready? -- Federal Energy Regulatory Commission & Commodity Futures Exchange Commission.

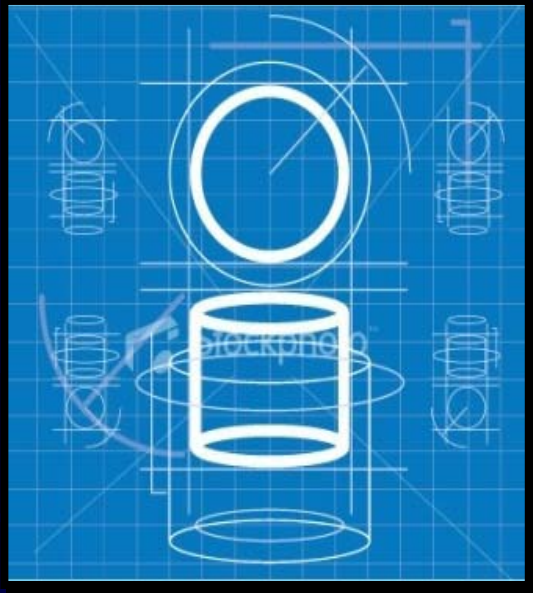
❖ FASB & IASB still working on accounting rules for emission rights trading.



Transfer Tax Proposals

- ❖ Workforce in place, goodwill, going concern
- ❖ Market valuation and aggregate worth

Patent Reform



- ❖ Courts -- actions on non-obviousness; automatic injunctions
- ❖ Congress -- still stalled on apportionment of damages; IT v. Pharma/biotech

New issues continue to arise (gene patent; business process; tax strategies)

Financing Innovation

❖ Techniques through intangible monetization

⌘ Intangible Asset-Backed Lending (IABL)

⌘ IA-Focused Equity Investment



Proposals and Policies on Intangibles

- ❖ Encourage understanding of intangibles
- ❖ Encourage financial investments in intangibles
- ❖ Foster utilization of intangibles



Policies to encourage understanding of intangibles

Increase corporate disclosure of intangibles:

- ❖ Reinstate the joint FASB and IASB research project on expanded disclosure guidelines for intangibles.
- ❖ Clearly designate nonfinancial measures for evaluating intangibles in MD&A portion of financial statements.
- ❖ Create a safe harbor in financial statements for reporting of intangible assets.
- ❖ Modify Sarbanes–Oxley so that there is a clear directive for assessments of the “material” intangible assets.
- ❖ Utilize the stock exchanges as initial testing grounds for increased intangible disclosure by requiring listed members to make additional disclosures that capture intangible metrics.

Policies to encourage understanding of intangibles

con't

- ❖ Explore the possibility of creating a “best practices” guidelines for intangible asset management.
- ❖ Include innovation and intangibles as part of the Baldrige Award.
- ❖ Create a crosscutting special analysis of the Federal budget.
- ❖ Include intangibles in the GDP accounts.

Policies to encourage financial investments in intangibles

- ❖ Convene a special FASB/SEC task force on valuation methodologies and support and encourage increased research on valuation standards (including efforts of International Valuation Standards Council)
- ❖ Explore the creation of an Intangibles Mortgage Corporation (Ida Mae) to regularize the intangibles-backed securities market.
- ❖ Undertake a review of the Basel II Accords to better understand their implications for intangible-backed lending.
- ❖ Coordinate with ongoing efforts at market reform to ensure that intangible-backed assets are properly included.

Policies to foster utilization of intangibles

- ❖ Expand/reorient the MEP program to include intangible asset management.
- ❖ Review federal and state insurance laws and regulations to promote the development of financial sound insurance coverage of intangibles.
- ❖ Create a permanent knowledge tax credit that would increase investments in intangibles.
- ❖ Explore lowering the tax rate on intangible asset royalties, in conjunction with stricter regulations on international transfer pricing mechanisms and cost-sharing arrangements and on passive investment companies. (Levin “Stop Tax Havens Act”)

Policies to foster utilization of intangibles

con't

- ❖ Enact patent reform legislation and include a review of patent litigation and patent liability insurance and a review of federal and state technology policies to encourage promotion of patent pools.
- ❖ Review how the federal technology transfer system, including Bayh–Dole, does or does not facilitate the creation of intangible assets.
- ❖ Review federal government business loan programs, especially in the small business arena, to ensure that intangible assets can be used as collateral, including requiring SBA to work with its commercial lenders to develop standards for the use of intangible assets as collateral, similar to existing SBA underwriting standards.

For Further Information

Intangible Asset Monetization: The Promise and the Reality; Working Paper #03, Athena Alliance, April 2008

Measuring Intangibles: A Summary of Recent Activity; Working Paper #02, Athena Alliance, June 2007

Reporting Intangibles: A Hard Look at Improving Business Information in the U.S., Working Paper #01, Athena Alliance, April 2005

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