KPMG

Realizing value from the intangible

How to manage IP as a business asset

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Executive summary

It's time for a paradigm shift in how intellectual property (IP) is managed.

If yours is like most companies, your IP is worth more than you know. In today's knowledge-based economy, IP is at the core of enterprise value creation. Recent studies attribute 80 percent of the market value of companies in the S&P to intangible assets.[1]

However, the activities around IP rarely reflect its high value. In most organizations, IP isn't managed as thoughtfully or strategically as other revenue generating activities and assets.

- **Most companies manage their financial and tangible assets well**—capital investments like manufacturing plants, office buildings, and vehicle fleets. They know how many they have, what they cost, what they're worth, how they contribute to revenue generation, what to expect from their lifecycle, and how to make the most of them. They have a rich framework and approach to portfolio management—directly informed by the enterprise strategy—which guides how the portfolio should be resized or adjusted based on changes in the business and market.
- **By contrast, IP is typically is managed with less rigor.** While companies may apply certain key principles of portfolio management to their IP, most lack a unified approach. The vast majority of IP departments lack organic connectivity with business decision makers. They treat IP purely as a legal function, where the goal is to obtain IP and use it if and when it is deemed necessary. Risks and returns are considered separately. They are unable to link specific IP assets to how the firm generates revenue and cannot continually optimize the IP portfolio. Based on our conversations with numerous clients, we have found that it is truly a rare company—maybe 1 in 50—that directly ties its IP strategy to corporate goals.

To view IP as primarily a legal right is to miss the fundamental role of IP—as an asset that generates enterprise value. Recognizing IP as an asset opens up a universe of sophisticated portfolio management techniques that allow companies to make better decisions about IP, extract value from IP, minimize risk, and position the IP department as a strategic partner to the firm, not just a cost center.

This report explains how to treat IP like the business asset it really is.

Based on what we know to be the core functions of the IP department, we diagnose the major problems holding IP teams from delivering full value. We also outline a business-centric approach to IP management built on four key principles. Finally, we describe seven capabilities of an enterprise IP model which improve how IP departments preserve, protect, and ultimately drive value.

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1 Ponczek, Sara, "Epic S&P 500 Rally is Powered by Assets You Can't See or Touch," Bloomberg (October 2020).

IP is your most valuable business asset. Why are you treating it as a legal right?

IP issues are often relegated to the legal world, excluded from strategy discussions, and underfunded. However, the primary functions of an effective IP department go beyond the legal realm. IP departments should:

Ensure existing intangible assets are protected: Recognize, identify, track and manage all valuable intangible assets—in any form and anywhere in the business. Know the right form of protection and deliver the additional level of care necessary to protect registered and unregistered IP.

Optimize the IP portfolio to generate the highest return for a targeted level of risk: Consider risk (e.g., likelihood of a patent being invalidated) and return (e.g., the revenue protected by an IP asset) together to make proportionate, cost-effective IP decisions.

Align the IP portfolio with current and future business needs: Protect assets in accordance with what is happening in the business (e.g., where and how revenue is being driven or where competitive activity is highest) and adjust with strategic changes.

Methodology

The insights in this report derive from our cross-functional KPMG IP Consulting team, which integrates diverse backgrounds in economics, intellectual property, law, valuation, operational transformation, data analytics, technical and engineering domains, tax, and accounting. Our approaches to client issues are also informed by our experiences supporting the world's highest performing organizations.

IP management: What's at stake?

IP is the primary asset of most companies. When companies don't take a business-centric approach to IP, they put the company and its value at risk.

STRATEGIC RISK: Critical IP that drives business value is unprotected and in danger of being lost or shared with competitors.

LOST VALUE: Valuable intellectual assets with significant revenue potential go unrecognized, unprotected, and uncommercialized.

WASTED RESOURCES: IP is expensive to obtain and maintain. Return on IP assets plummets when the scope and cost of protection is mismatched with actual commercial activity.

Today's IP management: What's not working?

Knowing your true IP inventory is hard enough.
Even if you have this knowledge, there are still challenges.

Many companies think about IP in a narrow way—get a patent, call it a day. As such, other key intangibles take a back seat in terms of identification and protection. Unregistered assets that fall outside of the patent, trademark, and copyright portfolios may go uncounted. Even when they are recognized, many companies don't end up taking the extra steps required to protect them.

More problematic, there's often little thought to the strategic relevance of IP as the product portfolio or corporate strategy evolves. This causes the IP portfolio to become misaligned with corporate priorities and companies to pay expensive maintenance fees for patents they may no longer need.

Failing to treat critical IP as assets not only misses opportunities to create enterprise value but also puts the firm at significant risk. Let's explore several root causes of IP mismanagement.

Root cause #1: The IP lifecycle is complex

The nature of IP creates unique management challenges.

IP assets do not come into existence the way traditional assets do. In fact, their path to creation is more complex and nuanced—and less understood.

The value you can't see

If you don't know what IP assets you have, you can't effectively manage your IP portfolio. But most companies are not aware of the full spectrum of intangible assets in their businesses. KPMG research suggests that as much as 75 percent of companies do not have a full inventory of their IP.

Unlike tangible assets, intangible assets are not always readily visible to IP, legal, or business leaders. "Soft IP," such as know-how, methodologies, frameworks, formulas, techniques and data, commonly reside throughout the company. While patentable inventions may be recognized in high stakes R&D efforts, firm-critical IP that can't be patented (e.g., unregistered assets) is created every day, much of it remaining unacknowledged. This IP may be a critical driver of firm value and a key source of competitive advantage.

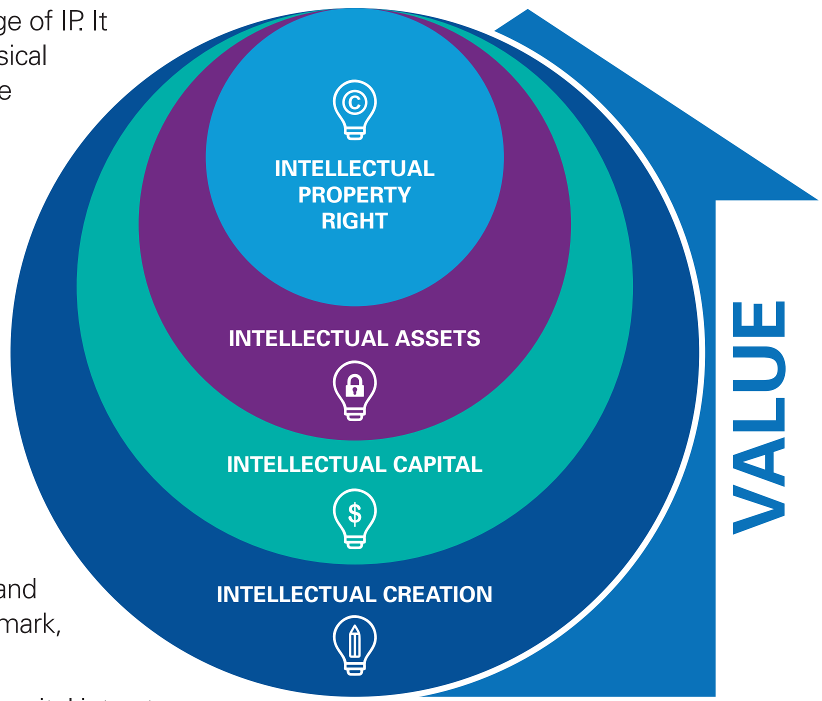
Tangible assets	Intangible assets
Identified and catalogued	Not identified or catalogued comprehensively
Asset utilization and performance tracked	Risk to business from not knowing assets
ROI evaluated and maximized	Missed opportunities to realize value
Relevance assessed	

Tangible assets, like land, equipment and inventory, are easily recognized as assets. They can be seen. There is usually a clear cost associated with their creation or acquisition. And firms know how to manage them.

In contrast, intangible assets start off as ideas in employees' heads, invisible to the wider business. They may have monetary value and represent potential revenue, but they do not physically exist. Rather, they need to be drawn through a deliberate process of documentation, management and governance in order to be converted into recognized IP assets and obtain ownership and protection rights.

The IP lifecycle looks like this:

- **Intellectual creation:** The idea is the initial stage of IP. It resides in people's heads or sometimes in physical form, such as a sketch of an invention, software code, or know-how. The idea exists but is not documented and recognized by the firm.
- **Intellectual capital:** An intellectual creation becomes intellectual capital when the company invests funding for further development—e.g., when the firm formally recognizes the idea and agrees to invest resources into its development.
- **Intellectual asset:** Intellectual capital is converted into an intellectual asset by documenting it and establishing an asset management and governance plan.
- **IP right:** An intellectual asset that qualifies for and has been protected by patent, copyright, trademark, or trade secret is an IP right.



Companies should aim to convert all intellectual capital into at least intellectual assets. This allows them to secure the value of their intellectual creations. However, many companies don't have a good handle on the process of converting an idea into an intellectual asset. This puts the business at risk from not knowing its assets, assets being lost to the competition, and missing out on opportunities to realize value.

Root cause #2: Treating all IP the same

Since not all IP is the same, it should not be managed in the same way. Each IP asset class requires a different approach to claim protection.

Some forms of IP, like patents, copyrights and trademarks, are registered assets that can be protected through specific legal processes. Others, like trade secrets, are non-registered assets that require a separate set of processes—including documentation, controls, and governance—to secure protection. Further, there are many other "soft" intellectual creations that may not qualify for IP rights yet generate value for the company. They require the company to convert those creations into assets.

The emphasis of most IP strategies and approaches is on registered IP such as patents, copyrights, and trademarks. That narrow approach represents a disconnect with the world in which businesses compete today.

In today's knowledge-based businesses, non-registered assets can be just as important as patents. Consider, for example, the value that Google's search algorithm—a famous trade secret—generates.

In today's knowledge-based businesses, non-registered assets can be just as important as patents.

IP leaders—and even business executives—are accustomed to thinking about patents. Where many struggle is protecting things that aren't patentable, yet account for a large portion of the company's value.

Root cause #3: It is challenging to operationalize IP management and link IP decisions to business objectives

We have already discussed how many intellectual creations go unrecognized or underappreciated. But that's only part of the problem. Even when IP is recognized, it is not necessarily managed strategically.

Because IP departments and decisions are not often integrated with the business, patents—and other IP rights—are often obtained in a reactionary way. Invention happens in one vacuum and patenting happens in a separate vacuum. In the meantime, the business world churns on: markets shift, inventions morph into commercialized innovations, competitors emerge, and business strategies change—each impacting how IP correlates with commercial activities.

This model tends to lead to large and expensive IP portfolios with unclear relevance. A company might build up a substantial IP portfolio but have little or no understanding of the nexus between its IP, its products, and its revenue. Consider that even among registered patent assets, only a small fraction—approximately 5 to 10 percent—are in use.[2] Odds are you are paying for a large number of IP assets that you no longer need.

Another important outcome is that the IP portfolio may not actually protect current revenue-generating activities and products. As corporate strategy and products evolve, a static IP portfolio can leave key assets unprotected and vulnerable to competitive exploitation.

2 Based on discussions with KPMG clients across a broad spectrum of industries

Building the infrastructure for a strategic IP program

How do companies create a new and better model for IP management—one that embraces the critical role of IP as a business asset and recognizes and protects its true value? We recommend several key principles for IP management transformation.

Connect corporate and IP strategies

A crucial piece of the transformation journey is to focus IP activities on business objectives. IP should not be a reactionary function, but a dynamic and proactive function—both responsive to and informing corporate strategy and engaged with the earliest stages of innovation.

Many IP managers tell us they have a "communications problem"—that the business just doesn't "get" IP. We think they have a strategy problem. It will be easier to win the hearts and minds of business leadership if the IP team speaks the same language as leadership and clearly shows how IP creates value.

No IP for IP's sake

To properly manage intellectual creations from a competitive perspective, all IP decisions—at the product/service level and at the enterprise level—must revolve around business objectives, tied to how IP helps support and protect corporate goals. Consider:

- Is the company entering a new market? How might IP help that effort succeed?
- Is the company launching a new product? How might IP protect the product's anticipated revenue stream?
- Where does the company want to be in five years? What IP does it need to create to close gaps and support the future vision?
- Has the company changed strategy? How should the existing IP portfolio change as a result?

There are several valid reasons to secure IP—to enjoy exclusivity, protect competitive advantage, defend against claims, bolster brand, and engage and retain talent, to name a few. However, revenue protection should be a core role. When IP is connected to revenue objectives, far better decisions can be made around which IP to obtain, how much IP is needed, and which IP can be monetized or otherwise disposed.

With this key principle in mind, an important early step on the road to strategic IP management is integrating IP into the wider business. While the optimal organizational model will vary based on each company's unique circumstances, the goal is to manage IP with direct input from business units and full C-suite support. For some that might involve giving IP leaders a seat at the table during major company planning and decisions. For others it might involve establishing IP departments outside of legal, attached to or under other business functions, such as finance or technology—a trend we are seeing in leading innovative companies.

Greater connectivity allows the IP strategy, decisions, and investments to derive from the corporate strategy and adjust as business goals change. Business leaders can share key insights on strategic efforts and revenue-generating activities with the IP team—e.g., where the firm will invest its resources, how it expects to generate revenue, and where the firm is no longer active. This allows the IP department to set its own priorities, budgets, and plans in alignment with corporate financial projections, accounting for issues such as: How much revenue is anticipated from a given product? In what jurisdictions? How might our competitors react? How confident are our financial projections? It also enables business leaders to think about the tax implications of their IP and engage in sophisticated tax planning that could drive significant value, such as by transferring IP to a jurisdiction with favorable tax treatment.

The power of corporate and IP linkages

Agility: Taking a business-first approach to IP management helps companies avoid product-IP mismatches by evolving along with the business and market. Change is constant in today's business environment, and even seemingly unrelated changes can trickle down to the IP level. A company could adjust its business model, creating revenue in new ways, which could impact the size of the IP portfolio. The level of competition in the market could shift, making certain IP rights more or less vital. When integrated with corporate strategy teams, IP teams can revaluate and adapt their own strategies as the business changes, ensuring the company's IP is relevant and generates returns.

Cost reduction: Getting rid of non-core assets that are no longer valuable can result in significant savings. A corporate-driven IP strategy delivers investments that are proportionate to the revenue expectations associated with new ideas and inventions. It enables companies to map the right IP streams to products and avoid the expensive trap of creating IP for IP's sake.

Client story: Delivering savings through a more strategic patent portfolio

Recent KPMG experience working with a client to better connect its patent portfolio to its strategic goals illustrates the power of linking corporate and IP strategies. Our client had amassed a large portfolio of tens of thousands of patents yet used only a portion of that portfolio and was incurring significant costs to keep their unused patents alive. Using our proprietary framework and supporting technologies, our professionals evaluated the market relevance and revenue potential of each patent in the portfolio, identifying IP assets that could be sold, licensed or abandoned to meet revenue goals. We also identified patents that have potential value for third parties but are no longer relevant to the client, since these were likely excellent monetization—new revenue—opportunities.

Manage across the IP lifecycle

For IP to satisfy its objective—to protect revenue—it must be converted into and managed as an asset. Unlike tangible assets, IP requires disciplined steps to convert into an asset. Without that action, no asset exists, no value has been created, and major loss can occur.

Organizations need robust identification, evaluation, and management processes to ensure valuable intellectual creations are both discovered and protected. This includes technology and methods to detect valuable IP as well as frameworks for making informed decisions about which IP rights to pursue (e.g., patents vs. trade secrets) and how to stimulate disclosure and protection activities.

Since intangibles aren't assets upon conception, it is critical to focus on the very first steps of the creation process. Many companies have a great deal of IP sitting in the initial intellectual creation phase, where it can easily evaporate when the idea owner moves on to another project, team, or company. Recognizing the existence and value of these ideas early on enables companies to take strategic action to convert creations into assets—the most critical yet most overlooked step of the IP lifecycle.

Finally, managing IP across the lifecycle helps maintain protection as ideas develop and change. IP is often initiated at the "invention" stage when an idea is still rough. When an invention becomes an innovation that can be sold—i.e., it undergoes design changes to make it more feasible to produce or meet consumer needs—IP teams must reassess whether the product is still protected through its underlying IP.

Trade secrets: An underappreciated yet highly valuable asset class

Managing trade secrets requires companies to take a new approach to IP management.

Many companies heavily favor patents but should also carefully consider the role of trade secrets too, especially given existing challenges with patent litigation.

Trade secrets are becoming increasingly important and sometimes are a company's most valuable IP. However, trade secrets are not obtained like other forms of IP. There is no government grant of a right. Instead, trade secrets can only qualify for protection if they are secret, have value, and the company takes "reasonable measures" to keep them secret.

Since creations requiring trade secret protection typically live in the business, not the legal department, it is the business that must take responsibility for managing the asset. As such, companies must implement controls to satisfy the "reasonable measures" requirement and keep the information secret.

For example, at KPMG business knowledge—which can often only be protected via trade secret—is at the heart of everything we do. As such, KPMG IP Consulting is actively involved in helping the firm's own IP department redesign and operationalize a trade secret program consisting of policies, processes, education, and technologies to protect and manage trade secrets through the full IP lifecycle in a way that can withstand challenge and scrutiny.

Think like a risk manager

In addition to managing IP in line with overall enterprise strategy and the IP lifecycle, it is crucial to take risk into account. IP leaders must weigh how much volatility they are willing to tolerate against the value of the intellectual assets and the cost of the protection.

In this way, IP protection is analogous to homeowner's insurance.

Keep in mind that as the business changes, so does the company's risk exposure: magnitudes, tolerances, and probabilities.

Consider the following example: Your home is at risk of loss due to, let's say, a fire. You take a deliberate step—buy a home insurance policy—to protect the value of your home. Should a fire occur, your insurance will make you whole, returning to you the value of your home. In buying an insurance policy, you weigh the cost of the policy against multiple risk-driven factors: the magnitude of the risk (your home value), the probability of the risk (the likelihood of your home being destroyed by fire); and your willingness to assume risk (your deductible size).

IP investments should be similarly evaluated, with risk-management thinking embedded into decision-making. Companies should develop a risk-based IP management framework to ensure the company obtains a portfolio of IP that is proportionate to the risk. This requires the firm to understand what is at risk—for example, the revenue associated with a given product due to competitive threat—and also the magnitude and probability of the risk. Viewing the IP portfolio through a risk lens allows IP leaders to assemble optimized portfolios. They can assess the expected return, risk, and cost tradeoffs of individual assets as well interdependencies between assets and the degree of correlation with key business drivers and between each other.

For example, imagine your company sells Product A, which is the result of know-how held by a few key employees. If left at the intellectual creation stage, that know-how is at risk of being lost or shared with a competitor. The magnitude of risk to your company is the revenue associated with Product A. The probability of the risk is the likelihood that the know-how will leave your company. Based on these factors, you can make better decisions around which forms of IP to acquire and how much IP to acquire.

Keep in mind that as the business changes, so does the company's risk exposure: magnitudes, tolerances, and probabilities. Consider that Product A's revenue potential could change at any time and for any reason. For example, it could increase if the company begins to sell in a new market, changing the magnitude of the risk (the value of the intellectual asset) and the probability of the risk (competitors would be more likely to target a more valuable asset).

As such, the IP management program must be tuned in to what is happening at the strategic level and be nimble enough to adapt accordingly. Organizations should have dynamic monitoring and assessment processes in place to align the IP portfolio with the underlying product value.

Ramp up data, analytics, and technology

Today, great data, advanced analytics and emerging technologies are key enablers of leading IP management.

Asset-mining tools are one example. IP teams need a complete and accurate inventory of "soft" IP to tap into significant value-generating opportunities. Leveraging KPMG proprietary asset-mining solutions, organizations can mine for intellectual creations that haven't been recognized or protected and help them quickly build a full inventory of key IP.

There are also technologies available to support IP portfolio management. The assessment of the expected return, risk, and cost tradeoffs to assemble an optimized portfolio requires significant analytical heavy lifting. In most instances, it isn't practical to review a portfolio manually. Technology solutions make it possible to quickly assess a large IP portfolio along a variety of measures.

Finally, technologies make gathering competitive intelligence a less resource-intensive process. Using data feeds, tracking tools and artificial intelligence, IP departments can obtain and organize external patent information related to competitors' R&D and innovation plans.

Of course, sound supporting processes around IP technologies are just as important as the tool itself. For example, IP functions can:

- Develop frameworks to stimulate disclosures and obtain protection when asset mining tools detect an unknown intellectual creation
- Implement techniques to map the IP portfolio to the business strategy, lowering the risk of mislabeling core assets or monetizing the wrong assets
- Leverage outside expertise to turn data coming in from valuation and competitive intelligence platforms into actionable insights.

The assessment of the expected return, risk, and cost tradeoffs to assemble an optimized portfolio requires significant analytical heavy lifting.

Seven capabilities of an enterprise IP model

Say you have convinced your C-suite leaders of IP's contribution and connection to enterprise value. You have evolved your strategic IP approach by aligning IP, enterprise strategy and commercial offerings; expanding the purview of IP management to include processes from creation to monetization; embedding risk-management thinking in IP processes; and investing in powerful analytical tools. What operational capabilities can you expect to unleash?

Here are seven capabilities of a strategic IP function that approaches IP as a business asset.

1

IP strategy: In an enterprise IP approach, the contribution of IP to business value is clear, leadership views the IP department a strategic partner rather than a cost center, and there is strong connectivity between IP, corporate strategy and commercial offerings. Alignment on the core purpose of IP activities—protecting revenue—drives more profitable and risk-informed IP decisions.

2

IP portfolio management: Managing the IP portfolio is complex and expensive if it is not driven first and foremost by business goals. Mapping the IP portfolio to the corporate strategy brings clarity to the true value of IP assets and which IP to keep, abandon, or monetize to support current revenue activities and strategic plans.

3

Trade secret program planning: Managing trade secrets requires an enterprise model that involves collaboration between IP, legal, and the business. This connectivity allows for centralized oversight of the trade-secret portfolio, business-based protection of the assets, and comprehensive records of content and control activities.

4

IP monetization: Business-centric IP management helps ensure valuable assets into the portfolio aren't overlooked or mislabeled as "noncore." For one, it changes the perspective on the value of IP, helping attract more staff and resources to the IP team. Secondly, it ensures asset monetization decisions are tied to strategic goals, with revenue generation (or protection) always at the center.

5

IP asset mining and discovery: "Soft IP" can be critical, but when IP is managed primarily as a legal right, it often eludes detection. Elevating IP to business-asset status in how it is viewed and treated allow companies to recognize intellectual creations. Processes and technologies can be implemented to mine for, disclose, and protect valuable IP that was previously unknown.

6

Valuation: Knowing the value of an IP asset greatly improves decision-making about portfolio optimization, resource allocation, and corporate transactions. Approaching IP as a business asset helps companies focus valuation questions and metrics activities on what matters most—revenue generation.

7

Market and competitive intelligence: To be effective, intelligence on competitors' innovation and R&D must be timely and insightful. By elevating IP to a C-suite topic, IP teams are better able to attract investment in people, data and tools for filtering, categorizing and organizing rich patent information and quickly transform it into actionable insights.

How KPMG can help

The KPMG IP Consulting practice helps companies take a strategic approach to IP management, focusing on IP as a business asset instead of only a legal right. We advise companies on the infrastructure, processes and capabilities necessary to recognize, develop, secure and manage IP in a way that delivers organizational and strategic value.

Who we are:

Our multidisciplinary team specializes in economics, intellectual property, law, valuation, business modelling, tax and accounting, delivering an enterprise-level view to IP challenges and opportunities. We have over 100 years of experience helping clients manage assets and create value.

Our services:

Trade secret protection: Operational protection framework and supporting technology

IP transactions: Due diligence support, M&A planning and integration, valuation, restructuring, financing, and international tax strategies

Driving value through IP: Cross-functional approach to managing IP as a business asset and enhancing enterprise value

IP portfolio management: Portfolio cost/risk/return optimization, pruning, and large portfolio analysis at scale

Enterprise IP solutions: Solving unstructured, complex IP problems arising from or across corporate functions such as procurement, finance/tax, HR, and data-intensive activities

Learn more at: visit.kpmg.us/IPconsulting

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Justin Rerko: Justin is an attorney who thinks like a corporate strategist. As an IP Transformation Leader at KPMG LLP, he applies extensive strategic and legal experience to help organizations take full advantage of their IP. Justin formerly served as in-house IP counsel for KPMG, where he helped the firm embrace the strategic value of its IP. Under his direction, KPMG grew its patent portfolio by 500 percent, operationalized a global trade secret management program, and monetized intellectual assets to generate revenue. Justin has 20 years of experience in legal and business roles, specializing in complex strategic growth initiatives, including IP transformation. He earned his law degree from Case Western Reserve University, is admitted to the Ohio Bar Association, and has conducted graduate work in technology entrepreneurship.

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