MAKING MUSIC – MORE THAN A LEGACY OF SONG – A LESSON IN THE VALUATION OF THE INTELLECTUAL PROPERTY RIGHTS OF PRINCE AND OTHER ARTISTS

Evan Levine and **Nainesh Shah** provide members with commentary that examines the valuation of Prince and other artists.

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Here is their commentary:

EXECUTIVE SUMMARY:

What do music icons Michael Jackson, Aretha Franklin, Sonny Bono, Kurt Cobain, John Denver, Bob Marley, and Prince have in common? Each artist left us with a legacy of music that will last for an eternity. Sadly, each artist also died intestate with no estate plan for the protection, management, and distribution of their most valuable asset – the value of the vast array of their creative intellectual property rights. The intellectual property of a musician includes copyrights of published and unpublished songs, ownership interests in a music label, their name and likeness, and more.

Valuing business assets of any type can be challenging, but even more so for evaluating a musician's intellectual property rights. Although the estate tax valuation of a decedent's assets is the fair market value as of the date of death or the alternate date (six months after death), a well-conceived estate plan includes tax savings techniques. Unfortunately, this was not in place for those named musicians who died intestate. In such a plan, potential estate tax saving valuation methods of the artist's intellectual property would have been considered in advance. This would have provided the executor/administrator with a leg up should a dispute with the IRS arise.

COMMENT:

For example, Prince (Prince Rogers Nelson), who died intestate in 2016 at the age of 57 from an accidental overdose of painkillers, left behind a music treasure trove of ownership rights to released and unreleased music and video recordings. During his lifetime, Prince had achieved intellectual property independence, as he, rather than recording and publishing companies, owned the rights to his compositions and recordings of published and unpublished music and videos.

Following Prince's death, his estate became embroiled in a valuation dispute with the IRS in Tax Court. Predictably, the central issue was the value of Prince's most valuable asset - his intellectual property rights. The IRS asserted the value of $163.2 million was approximately $80 more than the amount reported on Prince's estate tax return. An IRS victory in Tax Court would cost the estate $38.8 million of additional tax as well as interest and penalties.

The chart below illustrates the estate and IRS valuation discrepancies in intellectual property and music assets.[i]

Asset	Details	Estate's Valuation	IRS Valuation
NPG Music Publishing	A collection of songwriting copyrights	$21.0 million	$36.9 million
Music composition	Writer's Share	$11.0 million	$22.0 million
NPG records	Ownership	$19.5 million	$46.5 million
Name & Likeness	Publicity, name, image, and likeness	$3.2 million	$6.2 million

The high-profile – high stakes valuation dispute between Prince's estate and the IRS reinforces the significance of a well-conceived valuation of intellectual property.

Although an intangibles' valuation is both art and science, the analyst should employ assumptions particular to the different types of intellectual property rights a musician owns to ascertain a credible valuation. Generally, an analysis involves three types of approaches - income, market, and asset. All approaches can be relevant and should be weighed according to the peculiarities of valuing such unique rights.

For example, in valuing various types of music and video ownership rights, industry analysis is critical. Due to rapid advances in technology, industry models mainly related to marketing and selling are in a constant change of flux. Now more than ever, music and video are being sold on multiple platforms. Not only can music and videos be individually purchased on Itunes, the packaging of multiple music and video are also available through subscription services such as Spotify and Pandora. Streaming music and videos from anywhere on the planet has exponentially boosted and expanded the market, and, hence, the value of an artist's creative output.

The valuation of Prince's estate is even more problematic because, in addition to Prince's recorded songs and videos, his estate also included a vast number of unpublished songs and videos (a music "vault" of sorts). Consequently, the appraiser's task includes predicting future royalties from sales of Prince's well-known published music and videos as well as estimating royalties from his unpublished works.

Finally, a separate valuation of the rights to Prince's name and likeness must also be factored into the valuation. A case in point is the Estate of Andrews [ii] illustrating the difficulty in valuing the monetary rights of the commercial exploitation of an artist's name and likeness for estate tax purposes. Significantly, despite disagreeing with the IRS's approach to valuation, the court agreed with the IRS that an artist's (in this case an author) "name and likeness" was an asset to be included in the artist's gross estate.

CONCLUSION:

In conclusion, since the highest valued asset of a celebrated musician’s estate is likely to be an array of the intellectual property rights, date of death (or alternate date) intangibles' valuation is necessary. Essentially, the valuation is an estimate of the value of future income streams from all means of marketing and selling a vast array of the musician’s creative treasure trove. However, there is the risk of overvaluation because a musician’s sustaining popularity is hard to measure definitively. Thus, an overstated value could be economically devastating for the musician's beneficiaries/heirs as there are no after-the-fact estate tax refunds for an overestimation of value. Conversely, an understated value of a high-profile musician's intellectual property rights (such as Prince) is more likely to be challenged by the IRS. In that instance, the estate would likely incur substantial litigation costs, additional estate tax, and the potential imposition of undervaluation penalties should the IRS prevail.

Ultimately, significant differences in the valuation of a musician's intellectual property, such as in the estate of Prince/IRS dispute, are likely the consequence of ever-increasing selling venues in which music and videos can be commercially exploited. Equally important is the extent and duration of the marketability of Prince’s creations. The outcome of the dispute between the estate of Prince and the IRS should turn on whether the valuation is supported with sound assumptions and analysis. If not, the IRS will likely prevail. Either way, the result will be informative to appraisers of the type of factors that can potentially result in bloated or understated valuations. In any event, the Prince dispute is a teaching moment regarding the importance of estate planning for high-profile musicians and other artists that includes a credible intangibles valuation method.

[i] United States Tax Court, Estate of Prince R. Nelson Deceased, Comerica Bank and Trust, N.A., Executor v. Commissioner of Internal Revenue; Docket No. 11442-20.
[ii] Estate of Andrews v. the United States, 850 F. Supp. 1279 (E.D. Va. 1994).