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Preparing Proactively for Future Licensing or Sale

By: Julia Elvidge, President, Chipworks

More companies are concluding that patents can be a revenue generator rather than a cost centre and are making their IP groups responsible for driving revenue. CEOs are asking senior IP staff, "What is the value of the company's patents?" Should the answer simply be a dollar value or should it explain the many ways that a patent portfolio supports an IP strategy that drives value for the business? Regardless, shareholder activists, directors and corporate senior management are beginning to see the value and potential uses of IP, in general, and of patents in particular.

As a result, high profile transactions of large portfolios for tens or hundreds of millions of dollars are being widely reported such as Kodak selling patents to Apple and Google or HP sale of patents to Qualcomm. Many other smaller transactions are also taking place. Companies with a good catalogue of their own portfolio know what patents should be retained to execute their IP strategy, which are ideal for licensing, and which can be sold as surplus.

Unfortunately, as patents are leveraged to support business strategies in innovative and varied ways, many sales and licensing deals – especially for technology patents – are not announced or publicized. This makes it difficult to understand best practices and prepare successful strategies for future licensing or sales. Even so, there are specific actions that companies can take to help maximize the value of their patents.

To maximize the ROI from a patent portfolio, patent owners must first determine whether sales or licensing is more lucrative. For the most part, patent licensing promises the highest total return on monetizing an IP portfolio. The calculation is simple: the IP owner can license the same asset (i.e., the IP portfolio) to a number of different licensees, which may generate higher revenues than selling the asset once to one purchaser. Licensing takes longer (3 – 5 years) to generate revenue and comes with many risks such as litigation, invalidity arguments, and more. A licensing program can be run internally with the advantage of retaining ownership and control of the patents and strategy and leveraging internal knowledge of the portfolio. Licensing programs can also be run externally through a contract licensing organization. While it may appear to be more costly, this option can be done in combination with an internal program to more quickly ramp up royalty streams. Patents are a decaying asset and generally expire 20 years after first filing.

When it comes to patent licensing and sales there is an ongoing debate over patent quantity versus quality. These terms often get used almost interchangeably yet they are in fact separate concepts. Quality, generally, refers to the legal aspects of a patent and high quality patents meet or exceed the statutory requirements for patentability. Patent value alludes to the business aspects of a patent, the market value of the technology as incorporated into products and services being sold on the market. While the overall trend today is to focus on quality, for technology companies having both sufficient quantity and quality in a portfolio is the best strategy. There must be enough valuable patents, supported by enough additional patents to assure potential licensees or buyers that it is impractical to consider invalidating an entire portfolio.

To be effective in today's more patent skeptical market patent owners must be prepared to demonstrate the tangible value of their patent portfolios before entering into sales or licensing discussions. Only a small number of a company's patents are valuable, meaning that they are legally valid, technically important, and actually in use in high revenue products. A general rule of thumb is that 3% - 5% of patents in a large portfolio meet this definition of valuable. In most portfolios a few key patents are the deal drivers. Knowledgeable buyers are insisting on evidence of use and often demand financial models illustrating potential value supporting the asking price. Tactically this means that to maximize value a company needs to prepare a case as rigorously as a pre-litigation case. Valuable patents are selling, usually with a supporting portfolio wrapped around them. It is always a few key patents with supporting documentation that drive high value deals. Many companies have experienced negotiations where a licensee or buyer will admit, after the agreement has been signed, to being really interested in a particular patent that is not on their list of key patents driving the deal.

Successful sales and licensing transactions require extensive preparation before contacting a future licensing partner or buyer. Patent owners must demonstrate the clear value of the patents by showing their use in competitive products and linking that use to a competitor's revenue. They must vigorously prepare, essentially preparing litigation without the benefit of discovery, including building claim charts, anticipating validity arguments and doing economic damages modeling. Clear and convincing evidence that leads to a conclusion that a license or purchase is both required and inevitable will help convince a partner or buyer to spend a large portion of a shrinking or non-existent budget on the patent owner's portfolio.

With a practical definition of patent portfolio value, it is possible to apply methods for measuring the performance of the patent portfolio. To generate business value from patents, the metrics established for evaluating the performance of a portfolio must link back to the business strategy. The traditional measurement for IP groups is the number of applications filed and/or the number of patents issued per year. These are simple to measure, yet they make no attempt to include any consideration of value or contribution to the business. Measuring the number and not the value of patents is a dangerous path.

A better quantitative measurement might be the number of new proud patents (or star patents or any number of other terms) created each year. Proud patents are the subset of the 3% - 5% of a company's patents that can be documented to show use in products available on the open market. Any patent with demonstrated value is a useful tool to help achieve numerous patent objectives. Unfortunately this measure both adds a few more years to the timeline between invention and achievement and must attempt to span the chasm between prosecution teams and licensing teams.

In preparing to license or sell patents, a Patent Catalogue is an invaluable tool that identifies the most strategic patents and measures the value of patents. While starting as an inventory of your patent resources, it becomes an essential asset that includes the data needed to confidently develop successful monetization strategies. There is no real off-the-shelf solution for a Patent Catalogue. Many organizations have ad hoc systems that attempt to track their valuable patents. In some cases this consists of asking inventors what patents they think are most useful, collecting the claim charts and assertions that have been used in previous licensing campaigns and litigations, or collecting data on spreadsheets.

The task of developing and maintaining a well researched, organized and documented Patent Catalogue is not trivial, especially for an organization that owns hundreds, if not thousands, of patents. It is, nonetheless essential for reaping the benefits of a patent through sales or licensing.

The Patent Catalogue provides a framework for making decisions on what to do with an existing portfolio while a Patent Market Matrix (PMM) plots patent families against the markets and identifies potential licensing partners. Once a potential licensee is identified, a Patent Product Matrix (PPM) is developed through technical and legal due diligence and determines the strength of a portfolio when an assertion campaign is being considered. It is also prudent to do some sort of PPM in reverse to determine which patents a licensing partner owns that could be asserted against the company's products. Once complete, the Patent Market and Patent Product Matrices help guide decisions about initiating a licensing program or seeking a cross license.

Thorough technical due diligence provides the proof based on a PPM recommendation and ensure that a patent has value in the industry. Technical due diligence can range from a basic and quick patent review through online literature reviews to full infringement analysis that helps identify and map claim elements to applicable products/devices. In all cases, if a true market value is being sought for patents the potential buyer/licensee will require that the value of the patents to their own company be demonstrated. More evidence and more patents equal more coverage and higher value. A license or sale value will be related to the size of the market (damages in legal parlance) that the technology covers and the breadth and significance of the technology offered. Technical due diligence can be performed by in-house experts working with external specialists like Chipworks who provide specific market knowledge and / or technical expertise a company may not have internally.

Traditionally there has been minimal need for due diligence on the sell side, but the economic climate has changed creating a buyer's market. The supply of patents exceeds demand, but demonstrated valuable patents are still in short supply. To separate the 3 -5% of valuable patents from the rest, buyers ask sellers to provide evidence of a patent's value with expectations rising in lockstep with price.

Intellectual property strategy has emerged as a key component driving business strategies in an increasing number of companies. The proliferation of patents and of patent owners who are interested in leveraging their patents have been a catalyst generating a more competitive and difficult sales and licensing environment. Despite these pressures, with the right preparation patent portfolios can be successfully sold or licensed.

Author Bio

Julia Elvidge is president of Chipworks, a trusted patent and technology partner to the world's largest and most successful companies. She joined Chipworks in 1994, and held increasingly senior management positions prior to being named President in 2003. Under her leadership business leaders have come to rely on Chipworks to help them identify and fully leverage their most valuable patents and provide crucial analysis of high-revenue products in the most competitive, fastest changing technology markets.