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Monetization of patent Rights

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From their traditional role of building value and forming an entry barrier to competitors, patents are rapidly becoming an asset by their own right. Patent rights can be licensed, sold or subjected to a variety of other types of transactions and become an independent source of revenues. The patent arena is, accordingly, changing rapidly and becoming a sophisticated marketplace that requires skill and expertise in order to realize the multitude of options that become available to patent owners.

Over the last two decades, there has been a dramatic rise in the number of patent litigations and in the extent of damages awarded to patentees in patent infringement cases. There is consequently a growing awareness of the immense importance of patents in preserving competitive advantages, on the one hand, and of the risk that third party patents may pose, on the other hand. This growing awareness, led to a dramatic increase in the volume of trade in patent rights through licensing or acquisition of patents. Thus, from being a mere legal right on the sidelines and intended to support mainstream business activity, patents have transitioned onto the center stage of the modern business world. Against this background, the May 25, 2010 announcement by Kodak's CEO of his intention to make patent out-licensing a key component of his company's business practice, with a projected annual income of more than \$250 million, came at no surprise¹. It has, indeed, become commonplace for executives to consider patents and implement patent-linked business practices as one of the pillars of a company's business plan.

Well-known players in the patent arena, such as IBM, Philips, Infineon, and many others who spend significant funds in building their patent portfolio and in its commercialization, were joined in recent years by entities, with a variety of business models, that specialize in the acquisition of patents solely for the purpose of licensing or enforcement, often referred to by the term "patent trolls".

Intellectual property developers and technology-based emerging companies have also come to realize that patents, in addition to their traditional role in building value and blocking competitors, may be an independent source of income, and in some cases have driven companies to even completely adjust their existing business model. Qualcomm is a classic example of such companies². Thus, patents are rapidly becoming a new asset class by themselves and the trade in patent rights through licensing, sale, litigation, lending, financing, or other creative structure, has become a very lucrative marketplace.

Many corporations, who have routinely used patents defensively or offensively, are now using patents, in a variety of sophisticated ways, as an independent source of revenue, often entirely divorced from its key business of selling products or providing services³. As many have realized, a well crafted and prosecuted patent portfolio may be a means to reap financial benefits even in the face a failure of the R&D to culminate in a marketable product. Also, even successful companies may have programs that are not implemented commercially but nonetheless give rise to valuable patents, which may become a source of income in their own right and supplement other lines of activities of the corporation.

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Thus, for example, CadTrack, a small corporation that was established in the early 1980's, managed to reap a total of about US\$50 million in 300 licensing deals on its patent after failing in research and development⁴; and Honeywell, that sued the camera manufacturer Minolta for infringement of patents relating to a shelved project and was awarded US\$ 120 million by the court and thereafter reaped the further staggering sum of US\$ 700 million (!) in settlements with all other camera manufacturers⁵.

The trade in patent assets is estimated to have an annual volume of many billions of US dollars, which is expected to rise to even larger scales over the coming years. There is also a new trend (of which Marshall Phelps⁶, who was the head of IP in IBM and later the head of IP in Microsoft, is one of its leaders) to use patents as a tool to foster cooperation and controlled exchange of information (e.g., through licensing or cross-licensing).

Patent transactions may take on a variety of different forms. They include, but are not limited to, such forms as an outright sale or assignment, exclusive or non-exclusive license, exclusive field of use license, sale with a retained license, right to enforce with or without upfront payment, options to purchase, and many others. This is a dynamic market that will no doubt continue to increase in sophistication in the years to come. Deep understanding of such deal structures and their significance, of the manner the market evolves and an acquaintance with the relevant players is often critical for the success of a deal and for realizing the value.

The realization that patents are a new class of assets is becoming more widely accepted in Israel as well. Some patent-based deals have been reported⁷ but the majority of transactions remain hidden from public view. Consistent with the existing entrepreneurial approach and attitude, Israeli companies, and more particularly the venture investors, have been quick to embrace the flurry of these IP transaction and financing alternatives⁸.

A solid market understanding coupled with meaningful legal and patent transaction understanding and experience is a clear prerequisite for the successful execution of these various options. As distinct from the trade in tangible assets, such as automobiles or real estate, for which objective valuation metrics exist, the patent commercialization realm is not yet a well developed market, and a complex and varied set of skills is required for the creation of value in a patent portfolio and its realization.

Through the creation of opportunities to monetize patent rights, entrepreneurs and innovators may gain access to new revenue opportunities, particularly (although not only) in those cases where the R&D efforts did not yield the desired fruits. Patent owners are thus advised to seek professional advice on such opportunities.

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Marqera is a US/Israeli IP Investment Bank with world-class expertise in the trade in patent assets.

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- ¹ Kodak is also actively enforcing its patents. In 2009 the company settled two patent infringement suits, one against Samsung and the other against LG, receiving \$550 million and \$400 million from these two companies, respectively. Earlier this year Kodak has also filed patent infringement suit against Research In Motion (RIM; the company behind Blackberry) and Apple.
- ² Originally a manufacturer of cellular communication hardware, Qualcomm has become in the year 2000 an intellectual property-oriented business, making licensing and enforcement of its patent rights one of the pillars of the company's business, supported by a portfolio of over 13,000 US patents. See also The Washington Post, Qualcomm's Business Model Attacked, Elliot Spagat, January 26, 2007.
<http://www.washingtonpost.com/wp-dyn/content/article/2007/01/26/AR2007012600826.html>
- ³ IBM, for example, developed an IP licensing strategy yielding at its peak annual licensing revenues close to US\$ 2 Billion.
- ⁴ CadTrack Corporation was established in the early 1980's and developed graphic stations. After the company's R&D did not culminate in a marketable product it was realized that the then new color displays of IBM and all other companies in fact infringe the single patent the company had. Throughout the life of that patent CadTrack corporation executed about 300 patent licenses reaping a total of more than US\$ 50 million.
- ⁵ Honeywell developed an optically-based range-finding system. The development was intended for military use. In the 1980's Minolta launched the first camera that made use of an optically-based automatic focusing mechanism that was within the scope of Honeywell's patent. After a period of time all camera manufacturers launched cameras with such a focusing mechanism. Having failed to license those patents, Honeywell filed a patent infringement suit against Minolta and eventually received a damage award of about US\$ 120 million. The company thereafter reached licensing deals with all other camera companies reaping a total of more than US\$ 700 in licensing fees.
- ⁶ Marshall Phelps headed IP at IBM in the 1990s, and is the one who devised and executed the IP strategy of the company that is continued to these days. At the core of this strategy is the utilization of IBM's portfolio of patents and other IP rights to create profit center through licensing rights, under this portfolio, to third parties. In 2002 he was appointed to head IP affairs for Microsoft and totally changed the manner in which Microsoft used patents in its business, such that licensing out patents and collaborative, patent-based agreements became a central component in Microsoft's business practice.
- ⁷ Recent examples are: Vocaltech selling its patent portfolio for a reported sum of US\$17 M; and the Israeli company SercoNet selling its patent portfolio for an unreported sum plus future royalties, to the Canadian company MOSAID.
- ⁸ See http://www.infinity-equity.com/press_portfolio_item.asp?ID=22. In this instance, an Israeli based Israel/China focused investment fund sold off the IP assets to a U.S. company, while transferring the manufacturing and product side of the business into a newly created China based entity.
- ⁹ Dr. Ilan Cohn and Mr. Ehud Hausman, in addition to their other roles in the Reinhold Cohn Group, also spearhead the patent commercialization line of service of the firm.