



Meet the dealmakers

IPOfferings' **Richard Ehrlickman** explains how a patent broker can help revitalise and monetise IP assets

For the first 100 years of US patents, inventors kept their patents and practised them. Samuel Hopkins received the first US patent for an improvement "in the making of pot ash and pearl ash by a new apparatus and process!". Eli Whitney manufactured cotton engines. Elias Howe patented the first US made sewing machine. The Wright Brothers manufactured airplanes – or "aeroplanes" as they were called then. Buying and selling patents is a relatively new phenomenon that has gained momentum in just the last few years.

And yet patents are property just like any other type of property. Patentees have the right to sell, assign, license or donate the patent² as they see fit, or to buy more patents to complement their portfolio.

We have seen a serious increase in the number, size and dollar amount of patent sales and auctions lately. That is because patents serve as both ammunition in the patent wars and armour to use when opponents attack. Patents can provide significant financial returns, and they are now more valuable than ever.

However, patents – unlike virtually any other asset a business can purchase – cannot be modified. For example, a business can spend millions on buying a factory, then remove all the equipment and make it a warehouse, or add windows and doors and make it a retail store.

Or they could buy it just for the land, tear down the original building, and put up a new structure or structures. Obviously, you cannot do that with a patent. It might have applications for another field of technology than the one the inventor intended, but even in that scenario, the patent itself cannot and will not change – just the mode of practising it. Remember that a patent does not give the owner permission to practise an invention, but provides the owner with the right to exclude others from "making, using, selling or offering for sale" any product or service that includes the patented invention.

Many patent owners do not know where to begin when they decide to sell or buy patents, because selling or buying patents is so different from other types of property transactions. To save themselves a great deal of valuable time, and to make sure they get the right price for their patent (if selling), and the right patent for their purposes (if buying), many businesses turn to a patent brokerage firm to enable a successful transaction.

On the seller's side

Finding a buyer for a patent is the ultimate needle-in-a-haystack search. The buyer has to need exactly what is covered by the patent

because each patent covers a specific invention. Perhaps it is precisely the invention that another company needs – but how do you find that company (or the one with just the patents you need), much less negotiate a fair price for both parties?

That is where a patent brokerage firm comes in. Like a real estate broker, a patent broker knows how to find the needle that is buried in one of several dozen or even a few hundred haystacks.

A patent broker is also knowledgeable about how to price a patent. Going back to the real estate analogy, a real estate appraiser can come up with a fair market value for a house by looking at comparables – what similar houses in the neighbourhood sold for. That can be done with some patents if the broker can find patents with similar technology, but many patents are totally unique, so there are no comparables.

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Pricing the patent for sale is critical because if you price it too high, you scare off a potential buyer, but if you price it too low, you could end up leaving money on the table. A patent broker – whose business is the buying and selling of patents – has the expertise to come up with an asking price that will solicit interest while not giving away potential dollars. Sometimes, a patent broker may bring in a patent valuation expert for a second opinion.

The broker begins by analysing the market potential of a patent (or patent portfolio), examines monetisation strategies that have been tried (and failed or succeeded) in the past, and recommends the best monetisation vehicle for that patent (or portfolio) — whether it is licensing, enforcement or sale.

With extensive contacts in many industries, the broker can act as a “matchmaker” between patent sellers and patent buyers. The broker helps determine a dollar value for the patent portfolio, and then assembles a package that includes all relevant information (such as evidence of use charts, file histories, market research and competitive landscape, uses of the patent, and encumbrances, if any), showcases the patent(s) for sale, and presents a comprehensive package to buyers. A buyer’s due diligence process may take a few months and include a prior art search, so presenting prospects with plenty of useful information helps both parties.

When it comes to licensing, a patent broker can help develop a campaign that typically includes evaluation, assessing revenue markets, identifying target products, matching patent claims to infringers or new product opportunities, preparing presentations for targets, and leading negotiations.

Patent brokers, like real estate brokers, work on a commission that is paid upon completion of the sale. To license a patent, they will likely ask for a monthly retainer and a success fee. And to acquire a patent, a broker will charge a consulting fee with a success completion bonus.

Patent brokers and in-house counsel

What is the role of in-house counsel when a patent broker gets involved? It is a big role, as it turns out. Naturally, the in-house counsel

are very familiar with the patent portfolio, what is going on in R&D and product strategy and understands how the company’s patents relate to its products.

The in-house patent attorney(s) often also perform, at some level, sorting of the portfolio. Roughly less than 1% of patents in a typical portfolio represent seminal scientific discoveries. The next cluster at the top of the list are “core” patents (20%) that are central to the company’s business. The patents descend in order of importance from there: the bulk (about 45%), are minor improvements on existing patents and a little over a third of them are decidedly routine and non-core patents.

In the middle of the list, (45%) are patents that could possibly be better monetised. Some of them may be infringed and should be enforced. Others may be useful in a non-competing industry through a licensing programme or patent sale, where a grant back licence³ ensures the licensee can continue to practice the patent if required.

At the bottom of the patent portfolio list (the non-core, unutilised group) are patents that the company will probably drop when the maintenance fees are due. (If patents are not worth monetising through licensing or selling, then monetising them through saving money on their maintenance fee is about as good as it gets.)

Needless to say, an in-house attorney who is intimately familiar with the company’s patents, products and plans, can be a tremendous asset when a patent broker comes into the picture.

Do’s and don’ts of patent monetisation

If you are contemplating a monetisation strategy, you might need to bring in a patent broker to help value and market some of your patents. Here are some do’s and don’ts that are helpful to remember:

- Don’t automatically drop seemingly worthless patents at annual maintenance fee time.
- Do put a process in place to evaluate your patents, if you do not have such a process already. For those “problem” patents that are next on the drop list, perform that evaluation a year before their maintenance fee is due. If a patent looks likely to be dropped, give it to a broker while there is still a full year left to explore means of monetisation.
- Do bring in a patent broker to help with the evaluation process, as well as the selling or buying patents. A broker can give an unbiased, first-pass valuation and report of market potential. Once you have identified which patents are to be sold, the patent broker will provide an active campaign utilising their connections throughout industry and the IP community, as well as other entities that frequently buy patents such as patent aggregators, to make the right match between seller and buyer.
- Do be open to changing your initial plans. For example, perhaps you only meant to sell one patent, but the broker finds that more than one patent should be sold – or that more than one weak (for your purposes, anyway) patent should be offered together to make a stronger offering. A patent broker’s evaluation can actually help you in terms of your overall strategy for your patent portfolio – whether that strategy is protective, defensive or offensive – and can also implement a licensing programme or provide support for an existing one.

Should you put your patents up in a public auction? There have been some high-profile patent auction success stories⁴ in the past few years, but there have also been failures. One distinct disadvantage of a publicly-known patent auction is that if a patent or portfolio does not sell for the asking price, it is likely to be perceived as “shop worn”, and having the value of its bid revealed at auction, at a much lower value than the patentee would like, the patent’s worth is revealed to the buyer.

Also, success at patent auctions is very much a matter of whether the right person shows up. Some patent auction houses are very

particular about which patents they accept for auction, their reputation is also on the line. So a patent auction is a valid vehicle for selling patents and the success fee is similar to that charged by a patent broker, but the public nature of a patent auction makes it a venue where patent owners should proceed with caution.

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Have your cake and eat it too

If you are practising a patent, but your broker finds it an attractive patent they believe they can sell, you can sell it and license (commonly called a grant back³) it back from the new owner — just as companies going through restructuring will sometimes sell an office building, warehouse or factory for the benefit of the immediate cash, and then lease it back. If you previously licensed a patent (referred to as an encumbrance), you can still sell it as long as the new owner agrees to honour the terms of the licensing agreement.

On the buyer's side

When a patent broker is contacted about finding a patent or portfolio for a buyer, the advantage to the buyer is that the broker can find as many as 250-500 patents in the right technology field, narrow them down to those that the patentees are willing to sell, and narrow that list even further to a prioritised list of the 10 or 12 most eligible patents. That would clearly be a time-consuming proposition if one were to attempt doing it in-house.

Once the right patent or patents have been identified, the patent broker commences negotiations and seals the deal. And working through a broker means the buyer can remain anonymous, generally lowering the purchase price and often limiting public knowledge, and thus provide competitors with strategic intelligence on the buyer's company.

New trends in patent transactions

In April, headlines were made when Microsoft sold hundreds of patents it had purchased from AOL. It was a brilliant piece of deal making. Microsoft purchased a 925 patent-strong portfolio from AOL for \$1bn (an amount which was greater than AOL's market value). Microsoft kept the patents it needed, then sold 650 patents it did not need to own (but, received a grant back licence to use) to Facebook for \$550m.

Brad Smith, executive vice president and general counsel of Microsoft, said the agreement with Facebook “enables us to recoup over half of our costs while achieving our goals from the AOL auction”.

As patents on solid, basic technologies become essential to staying competitive and winning (or warding off) lawsuits, it is likely we will see more of this kind of “patent flipping”.

Such high-publicity and high-stake deals aside, there are vast amounts of unused or underutilised IP assets out there, just looking for a market. And there are potential buyers who wish to buy patents on specific technologies but do not know where to find sellers, and sellers that do not know how to begin the negotiation process or set a price on a patent in the first place. (There is no Kelley Blue Book⁵ for patents, after all.) An experienced, reputable patent broker has the experience, connections and skills to bring buyers and sellers (or licensors and licensees) together.

The haves and have-nots

There will be increased demand for patents in the coming years as companies' play IP catch up. The older technology businesses that invested in R&D, filed for patents for their inventions and now have a considerable inventory of IP assets are the 'haves'. The newer technology companies – primarily web-based businesses like Google and Facebook – are the new 'have nots', so they have been buying, and will continue to buy, patents.

Unrecorded assets

Because of the way patents are created, they often do not appear on a business's balance sheet, even though they are sometimes incredibly valuable assets. When a company buys inventory, the value of that inventory is added to the company's balance sheet. When an invoice is issued, accounts receivable – an asset – is added to the company's balance sheet. But when a company invests in R&D, invents something, files for and receives a patent, no accounting transaction occurs to add the value of that patent to the balance sheet.

The result is that many businesses that decide to sell their intellectual property assets discover incredibly valuable, but unrecorded, assets. A patent broker can help in uncovering the true value in under-valued or unrecorded intellectual property.

Footnotes

1. In 1790, Samuel Hopkins became the first person in the US to file and to be granted a patent for a process of making pot ash (potassium), an ingredient used in fertiliser. Pearl ash was used to make soap and glass.
2. Sometimes a company will donate a patent if it no longer feels it is worth maintaining and donate it to a qualifying charitable organisation. Patent donation also helps to promote business relationships.
3. In US patent law, a grant back licence is a licence under which a party grants another the right to use a patent under the condition that the licensee agrees to grant the licensor a licence with respect to any improvements to that patent made by the licensee.
4. When the Canadian telecom giant, Nortel Networks, went into bankruptcy, its “hard” assets were sold off for \$3.2bn. When Nortel's patents were sold, they fetched \$4.5bn! It turned out that Nortel's intellectual assets were worth over a billion dollars more than the rest of the business.
5. The US' largest automotive vehicle valuation company.

Author



Richard Ehrlickman is founder and president of IPOfferings LLC, a provider of intellectual property transaction and consulting services that help clients identify IP asset value, and leverage and monetise those assets to increase shareholder value. He previously served as vice president of intellectual property and licensing at IBM where he was responsible for patent and technology IP licensing, alliances, acquisitions, and divestiture of assets.