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Patent wins are overlooked and under-reported

Defining a patent "win" is not as simple as it may appear. It defies easy explanation and differs by industry, company and audience

Most people regard patent out-licensing as a clear indication of success. Strategic patents, however, typically associated with freedom to sell products, are rarely seen as a win. The double standard is particularly confusing when it comes to operating companies whose primary concern is to maintain market share and profit margins. Businesses that are unable to relate the role that their rights play in performance can expect to pay a price. The inability to articulate patent performance (under-reporting) affects market value and access to capital, as well as reputation for innovation. Many strategic holders whose patents are performing well often fail to explain their relevance because management has not clarified what good IP performance means. Patent wins - all of them - need to be defined and reported before regulators require it.

Outside of royalty income and enforcement damages, successful patent performance is still a mystery. That is why I believe most companies do an awful job of discussing it, even when it is in their interest to do so. Explaining return on IP (ROIP) can be equal parts frustrating and embarrassing. Just ask most chief IP officers (CIPOs).

ROIP can mean many things to different businesses and audiences. The onus is on the CIPO or equivalent to provide a context to define success and manage expectations. Lest we forget, it is not always obvious why companies conduct research and file for and maintain patents. Audiences want to know that patents are necessary; that they are being used effectively; and that they are providing an adequate return.

ROIP typically represents the net of the costs paid by companies to obtain legal rights (eg, patent filings, continuations, maintenance and legal fees), and the R&D underlying an invention. In some cases it also may reflect the cost to acquire rights to practise an invention. ROIP for purposes of this discussion is the costs associated with identifying and nurturing an invention, and obtaining and managing the patents that cover it (additional outlays are usually necessary to defend or enforce them).

Out-licensing is the type of IP performance that is readily understood on Wall Street and by senior management. Unfortunately, patent out-licensing is in most cases a fractional revenue generator for operating companies and is often inappropriate because of the pain associated with litigation. It also is only one of several ways - albeit an important one - that patents can generate return. Others include in-licensing and cross-licensing, mergers and acquisitions, patent sales, securing customer and vendor relationships, shareholder value, enhancing reputation and brand equity, and cost of capital.

Interpreting return on defensive intellectual property is much more difficult to calculate than identifying licensing income. Despite this, strategic intellectual property can be more valuable to some businesses than rights that generate direct, high-margin income. It really depends on the particular industry and business model, and on timing. Licensing is readily understood, while strategic patents are typically recognised as useful and abstractly contributing to the bottom line. Operating companies that can step up and explain subtle patent wins reveal not only performance, but also depth and determination.

For example, patents that can help to make an LCD display sellable with, say, 35% market share with 25% margins are pretty valuable. Which patents are they and how do they play a role in product revenue and overall profitability? How much in the way of R&D, filing fees and legal costs was invested in securing the patents? What is the estimated return to the company over how many years?

IP holders are under increasing pressure to prove the value of their portfolio. As R&D costs rise and the cost of borrowing remains low, buying necessary patents at market prices may be a safer and more efficient strategy for some. Companies that develop patents internally need to justify build-versus-buy decisions, as they do with other assets.

Business executives and boards of directors - many of them graduates of elite business programmes and experienced in running public companies - have been weaned on managing human, financial and physical resources, plants and equipment, people, capital and strategy; not on deploying intangible assets. Intangibles need to be managed aggressively and reported regularly. Companies that are timid about occasionally selling under-utilised assets in a carefully structured transaction that facilitates shareholder value without compromising safety may also be underestimating their assets.

A business that conducts little or no out-licensing need not be embarrassed if doing so makes sense, given its industry and business model. Conversely, if it has a valuable portfolio of rights that can be monetised, it may want to consider deploying those assets. Increasingly, transactions are being structured that allow sellers to retain maximum protection, as well as counter-assertion resources and some back-end returns, without direct patent ownership.

It is a reporting challenge to quantify the role that patents play in various with performance. There are many impediments to doing so and precision is certainly one of them. But the attempt still must be made. Businesses that rise to the challenge can free themselves from reliance on the "trust me" approach to IP management that satisfies few and undermines credibility. Good IP rights deserve better treatment; so do investors.

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