The intangible investor

Written by
Bruce Berman

Build, license, buy or steal

The decision to create, rent or acquire patents is becoming less confusing for some cash-rich companies. A new role for C-level executives and investors may be emerging

Companies that can gain access to the right patents at the right time, regardless of the cost, may be in the best position to win in the competitive consumer market for smart phones, cloud computing and social networking.

This may be a zero-sum game for most, but for the right operating business the high cost of securing valuable rights at the right time is crucial not only for the freedom to sell products, but also to prevent competitors from waltzing unfettered towards dominant market share. It is a game many significant tech giants have sufficient resources to play and, in most cases, cannot afford to observe from the sidelines.

Recent portfolio transactions (Nortel, *et al*) have proved that some buyers are prepared to pay a hearty premium to keep some patents out of the hands of competitors. C-level executives, boards of directors and activist investors are all fascinated with these marquee IP transactions not only because of their cost, but also because of their potential for game-changing impact. Management's scrutiny may seem meddlesome, but it is forcing some businesses to re-examine their IP inventory and the effectiveness of their strategy.

Pride of inventorship

Patent holders sell and acquirers buy for many reasons – some of which have more to do with reported results than IP strategy. A company that may need revenue in a particular quarter to meet Wall Street estimates may choose suddenly to conclude a long licensing negotiation for cash, "If we can get it done this quarter". Other factors include a business's preference to make a one-time licence payment or consummate a patent purchase in a strong quarter, or hide it in a weak one.

Informed IP stakeholders can play a key supportive role in assuring that patent objectives are realised. It is not easy for a chief executive or activist investor to refrain from second guessing IP management about monetising patents when prices are at historic highs. With a little help, however, they can be welcomed as collaborators. Their ability to access capital and manage risk should not be underestimated.

Until recently, companies rarely acquired patents: engineering pride, the belief that costly R&D should be self-sustaining and fear that showing a weak hand may encourage disputes (and firings) forced many prominent IT businesses to go it alone. Why pay cash for innovation rights when R&D and legal departments could churn them out like parts on an assembly line? That is, until companies started taking an honest look at which of their patents actually read on their products and which of others do.

Pay the ticket

Much in the manner of large pharmaceutical companies, more IT companies have concluded that if they cannot successfully generate, in-license patents or buy patents, acquiring companies that own those they require is not a bad alternative (see Google's acquisition of Motorola Mobility). Businesses in the financial position to pay market prices for the innovation rights and know-how they need to practise, or to prevent others from doing so, will not let much stop them.

For cash-rich companies such as Microsoft (US$57.4 billion), Apple (US$81.6 billion) and Google (US$42.6 billion), the cost to settle litigation or acquire most patent portfolios is little more than a speeding ticket on the valuation highway. It is barely a blip on analysts' quarterly earnings radars. Premium buying beats having to do business in the shadow of ongoing disputes or spending billions to design around. The size and importance of some of these patent transactions have sucked stakeholders not normally associated with intellectual property into the vortex of the patent strategy process. A transaction such as Nortel-Rockstar Bidco gets done for many reasons, but rarely without the support of senior managements and boards of directors.

The patent transaction process is not without its ironies. Patents in a distressed sale can frequently command higher prices than those sold when the company is solvent – that is, the patents of some companies are worth more with the company fully dead than partially alive. A distressed IP sale will be orderly and take place according to bankruptcy court rules. The process is more transparent and inclusive, and at the end of the day there will be a new owner. It behoves affected parties (or their representatives) to participate. They can bid on the assets in the hope of acquiring them at an acceptable price or make it more costly for other parties to do so.

A roll of the dice

In solvent sales there is more mystery about who is interested in the assets and at what price. This makes acquiring patents somewhat riskier. It also makes it more difficult for most buyers to sell the deal to management and directors. In the case of a near-bankrupt company (eg, Kodak), there is also the risk of fraudulent conveyance – unauthorised sale of the assets pre-filing – which can unwind a deal faster than a buyer can say "Department of Justice".

For many businesses, abundant R&D and patent filings may be an effective means of innovating, but they are rarely productive enough to fill all of a company's IP needs, especially in patent-intensive industries. Executives are learning to be less sanguine about their IP resources. When it comes to patents, it is sometimes more efficient to secure what is needed rather than rolling the dice on what a business might be able to generate internally or get away with legally.

While necessity may be the mother of invention, pride of authorship may prove too costly even for the most innovative companies to endure.

Bruce Berman is chief executive of Brody Berman Associates, a strategic communications firm that works with IP owners, managers and service providers. www.brodyberman.com; blog: IP CloseUp.