

Patents: Realising and securing value

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Executive summary ¹

The context and challenges

The development of the knowledge-based economy and new technologies has brought a number of new players into the patent arena. Financial services companies like Swiss Re have become solid patent holders. They increasingly rely on patents to protect the outcome of their innovative efforts, to preserve their freedom to operate and to provide incentives to create and diffuse innovations.

The importance of patents as key assets is also validated by venture capitalists who strongly encourage entrepreneurs and new businesses to actively and offensively protect their intellectual assets, especially at early stages in their development, in order to maintain a sufficient level of flexibility in terms of business models and markets. Patent-backed companies have an easier access to capital markets and new financing solutions, witnessing the virtuous relationship between patents and risk capital.

The reliance of investors and financial markets on patents and the increasing risks incurred in product development activities due to new “abusive” patenting strategies (patent thickets, pools, etc.), raising uncertainty and the potential costs of bringing a product to the market, lift the need for reliable patent valuation methods. Well established methods are diverse in nature, including market-based, income-based, option pricing, and patentometric approaches. But patent valuation increasingly needs to be achieved in view of the entire value chain a company is active in. This can be achieved in three steps: at any stage in the value chain in particular, at the level of the entire value chain, or in the broader perspective of market and technology standards. Analysing patents into the perspective of an entire value chain provides a more in-depth insight into the strategic value of a patent portfolio.

The rise of technology market makers

The IP marketplace is nowadays in a probe and learn period where the number of intermediaries is rising. Several models are appearing, from partnerships or technology pools to special purpose investments vehicles, patent value funds and auctions. They may be analysed in terms of their connection to the inventive process and their offensiveness.

Patent value funds (PVF) aim at taking care of IP logistics issues (e.g. finding and negotiating with potential licensees) whilst filling in the financial gap needed to allow the necessary managerial efforts preceding the commercialization of new products. Patent value funds therefore identify, value, and then realize patents. The latter phase consists in identifying potential licensors, establishing contacts and negotiating with them up to the closing of a deal. Patent value funds, such as the ones recently launched by IP Bewertungs AG, make one step forward towards the development of a market for IP transfers.

Ocean Tomo’s IP auctions, taking place two to three times a year, also contribute to the maturation of the IP market, though copyrights seem more successful than patents so far. Another step in the direction of a clearer IP marketplace is Ocean Tomo’s 300 Patent Index, the first publicly traded IP index, consisting in a diversified portfolio of 300 companies owning quality patents (the value of these patents being assessed by Ocean Tomo’s Patent Ranking software).

¹ The following summarizes the comments made by most speakers during the conference proceedings. The programme and handouts will be available on the European Patent Academy’s website.

Toward a centralization and standardization of IP management?

IP rights are inherently inducing major risks: enforcement expenses, possible loss of value of the asset in case of nullity actions, cost of defence or possible damages in case of infringement, and risks associated with inventorship issues. These risks can be successfully managed through a better monitoring and centralization of the IP capture, development, diffusion and exploitation.

Accounting standards and practices (IFRS and IAS standards, the purchase price allocation method, etc.) may however provide starting points for monetizing IP assets, possibly after business combinations or impairment tests. Accounting focuses on current uses of IP rights, whereas monetization operations (i.e. conversion of IP assets into cash) are more focused on future or alternative uses, and mainly dictated by corporate and IP strategy decisions.

IP holding companies, by centralising the ownership of a group's IP assets, may provide a powerful optimization instrument. Such holdings, also driven by potential fiscal benefits, may be responsible for IP registration, drafting legal agreements, managing infringement issues, policing of IP use by the group, licensing to third parties, and oversight of R&D activities. A stable political environment appears as the most important criteria for companies to determine the choice of a location, while lawyers and consultants consider a flexible tax authority as the major parameter. Overall, there is no one obvious choice for an IP Holding's location. Such structures are in the end "to aspire and evolve to, but not to rush to."

Patent insurances

Owning and using IP rights creates exposure to potential important financial losses, especially for SME's, whose survival may be decided by a single ruling in court. Enforcement and defence of IP rights may indeed be complex and ruinous. IP insurances aim at providing a safety net against such risks. Moreover, they can be highly valuable since they allow to free capital (provisions) in the organisation against upfront payment of a premium.

There has already been several attempts to bring such insurance policies to the market, but they have been much more successful and promising in the UK and US than in continental Europe for instance, as confirmed by a recent report to the European Commission.

In the UK, patent litigation insurances have been around for a while and several products have been developed over the past two decades. Coverage is now available for enforcement costs, defence costs against invalidity or ownership challenges, and against infringement claims. It is also possible to cover damages, reasonable royalty or settlements in case of infringement, future revenue streams, R&D expenditures, financial investments, and loan arrangements, threatened by legal challenges or government actions leading to the nullity or unexploitability of a patent.

To succeed, especially from SME's point of view, patent litigation insurances need to be affordable and to cover all industries and countries, justifying the need for international cooperation in the field. Their mandatory nature might be desirable in terms of risk spreading, but would be very difficult and hazardous to implement in practice and might not be desired by SME's themselves. Nonetheless, companies are often not even alert of the IP-related risks they are exposed to and a great deal of effort is probably needed to raise their awareness.

Concluding remarks

Along with the knowledge based economy, IP and technology markets are developing nowadays. Many actions have been taken by governments and institutions, particularly focused on SME's in the UK and Germany, and on IP management methodologies in Japan, to foster and sustain their development and exploitation by companies. LESI (Licensing Executive Society International) further emphasizes the modest but promising emergence of IP markets and financial tools. But there is a general consensus that their development will only be made possible by high quality patent standards and processes.