Introduction

A slowly turning tide

By **Joff Wild**, Editor, *Intellectual Asset Management*

Investors are beginning to see that there is real potential in intellectual property. And although company boards of all sizes may still struggle to appreciate this fact, such a state of affairs cannot continue forever.

The letter sent by one of AOL's largest shareholders to the company's board in February 2012 could not have been clearer. AOL, wrote Starboard Value LP, has "a robust portfolio of extremely valuable and foundational intellectual property"; however, failures by the board mean that it "has gone unrecognized and underutilized". The letter continued:

> *"This portfolio of more than 800 patents broadly covers internet technologies with focus in areas such as secure data transit and e-commerce, travel navigation and turn-by-turn directions, search-related online advertising, real-time shopping, and shopping wish list, among many others.*
>
> *Since our initial public involvement in AOL, we have been approached by multiple parties specializing in intellectual property valuation and monetization, some of whom believe that (i) a significant number of large internet-related technology companies may be infringing on these patents, and (ii) AOL's patent portfolio could produce in excess of $1 billion of licensing income if appropriately harvested and monetized. Unfortunately, several of these parties have expressed severe frustration that AOL has been entirely unresponsive to their proposals regarding ways to take advantage of this underutilized asset. The Company's inaction is alarming given our understanding that many of the key patents have looming expiration dates over the next several years which could render them worthless if not immediately utilized."*

Starboard, which owns just over 5% of AOL's shares, went on to state that it is "increasingly uncomfortable with the direction of the Company and the leadership of the Board"; consequently, it had decided to nominate five "highly-qualified candidates" to stand for election to the AOL board. They possess, says Starboard, "a well-balanced mix of skill sets to ensure that the Company evaluates, with an open mind and a keen sense of urgency, all alternative strategies to determine the best path forward to maximize value for all shareholders". Among the five named was Ron Epstein, a well-known figure in the IP marketplace, who was previously chief executive officer of iPotential and who currently runs the Epicenter IP Group.

Just a few months later, the AOL board announced that it had sold a portfolio of 800 patents, plus the right to license 300 more, to Microsoft for more than $1 billion. Just weeks later, Microsoft stated that it was selling on 650 of those patents to Facebook for $550 million. Not a bad return for a couple of pages of A4!

Investors get smart

The Starboard letter was part of a trend that has developed since the Nortel auction of June 2011, when a consortium, including Apple, Microsoft, RIM and Ericsson, successfully bid $5 billion for a portfolio of 3,000 patents that was being auctioned as part of the Nortel bankruptcy process. Since then, investors have taken a much greater interest in intellectual property. Just after the Nortel auction, billionaire investor Carl Icahn suggested that

Motorola should be doing more to monetise its patent portfolio; weeks later, Google's purchase of the company was announced. Then, in Autumn 2011 a group of lenders wrote to the Kodak board reminding it of its "fiduciary duty to sell its patent portfolio for fair market value". There can be little doubt that many similar, less public conversations have taken place with respect to other companies.

That is because big money patent-based deals continue to be done. Aside from the AOL sale in 2012, when InterDigital raised $375 million by selling a patent portfolio to Intel, the company's share price jumped too. Lower down the scale in terms of company size, Aware Inc – an R&D-based business which develops and licenses software for the biometrics, telecommunications and healthcare industries, and which employs fewer than 100 staff –generated $91 million from two patent divestments in 2012: one to Intel for $75 million, and the other to TQ Delta LLC for $16 million. And just to show that it is not only US companies that are harvesting cash from their patents, in late September 2012 it was announced that Taiwan's Hon Hai Precision – better known to the world as Foxconn – had agreed to buy a portfolio of patents relating to flat-panel production from Japan's NEC Corporation. The amount to be paid was ¥9.5 billion (equivalent to $122 million).

Everywhere investors care to look there are clear indications of the value-creating potential that exists in intellectual property. Alongside the Nortel sale and the Motorola purchase, the smartphone wars have demonstrated the importance of having a well-thought-through IP strategy – with companies such as Microsoft now harvesting hundreds of millions of dollars a year from licensing activities in the sector.

Away from the smartphone sector, savvy investors cannot have missed the stellar performances of companies with IP-based business models. For example, just three-and-a-half years ago, Acacia's market capitalisation stood at $90 million – it is now worth well over $1 billion. Meanwhile, in the United Kingdom, in January 2012 mezzanine finance outfit ICG sold its stake in CPA Global to private equity firm Cinven in a deal that valued the IP management and software specialist at £950 million. Less than two years earlier, ICG had brought a 49% share in CPA in a transaction that equated to the company being worth £440 million.

Corporates slow on the uptake

While the investment community may be waking up to intellectual property slowly, there remains a huge knowledge gap in the corporate world – even in the United States, regarded by many as among the most sophisticated global IP markets.

A report published in February 2012 by the National Science Foundation (NSF) that examined attitudes among 40,000 US companies across a wide range of sectors revealed that the vast majority of them believe that IP rights are of no importance at all.

The NSF and the US Census Bureau co-sponsored the data collection in 2008 as part of the Business R&D and Innovation Survey, and the details were published in the February edition of the NSF's newsletter *InfoBrief.* They show overall results as follows:

- **Trade secrets** – 14% of respondents considered them either very or somewhat important; 85% believed they were not important.
- **Trademarks** – 15% said very or somewhat important; 84% said not important.
- **Utility patents** – 5% said very or somewhat important; 95% said not important.
- **Design patents** – 6% said very or somewhat important; 94% said not important.
- **Copyrights** – 12% said very or somewhat important; 88% said not important.
- **Mask works** – 3% said very or somewhat important; 97% said not important.

Given that the data is four years old, things may have changed since then – but it is unlikely that there will have been any spectacular leaps. If that is the case, the only conclusion can be that, akin to their counterparts in other countries, the vast majority of US-based businesses just do not believe that intellectual property offers them anything. Strikingly, this even applies to sectors where it might be expected that the opposite would (and certainly should) apply. So:

- With regard to trade secrets, 46% of

companies in the computer and electronic products (CEP) sector do not see them as important, while this figure is 50% for internet service providers.

- When it comes to utility patents, 63% of CEP companies dismiss them, while the figure is 64% for chemical companies. Even more noteworthy, 34% of CEP businesses that engage in R&D do not think patents are important, while the figure is 46% in chemicals.
- On the trademarks front, 50% of companies working in the beverages and tobacco sectors say they are not important; and 45% of publishing companies agree.
- For copyrights, 39% of publishing businesses dismiss them, as do 65% of internet service providers.

Opportunities knock

Of course, 2008 was before the Nortel auction, there had been few other big-ticket patent-based purchases, and no guns had yet been fired in the smartphone wars; so there is every reason to believe that interest in patents and other rights has increased since then. However, there is still a long way to go before intellectual property is part and parcel of the decision-making process in most US companies – even to the extent that it is considered and then dismissed.

It would be tempting to find this conclusion depressing; but the alternative view is that a relatively small number of IP-engaged companies are driving what is already a thriving market. They are not suddenly going to disengage; instead, the probability is that they will be joined by many others and the ecosystem will grow.

Considered in this way, it is difficult to conclude anything other than that opportunities abound for IP owners and their advisers. It is just a case of going out and making the most of them. *iam*