

# HOW FINANCIAL BUYERS ASSESS PATENT VALUE

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***MARKETS FOR PATENTS:  
Emerging Practices and  
Directions for Research***  
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# OVERVIEW

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- **What is a financial patent buyer (FPB)?**
- **What is the *standard* valuation model used by FPBs?**
- **What is the *best-case* ROI scenario?**
- **What are the applicable risk-discount factors?**
- **What are the economics and deal structure options?**

# Types of Financial Patent Buyers

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## *Top-Line (Offensive) FPBs*

Primary objective is revenue generation via --

- » sale,
- » license or
- » litigation (settlement/award)

## *Defensive FPBs*

Primary objective is litigation risk/cost reduction

# Types of Financial Patent Buyers (cont.)

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## Top-Line FPBs:

- **Private Equity Aggregation Funds**  
(Intellectual Ventures, Coller)
- **European Investment Bank Funds**  
(Deutsche Bank, Credit Suisse, Alpha Patentfonds)
- **PLECs (Enforcers)**  
(Acacia, Niro, Spangenberg, etc)
- **Litigation Financiers**  
(Altitude, Rembrandt, NW Patent, Juridica, Arca, etc.)

# Types of Financial Patent Buyers (cont.)

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## Top-Line FPBs (cont.):

- **IP Development & Licensing Companies**

(Rambus, Tessaera, Interdigital, MOSAID, Wi-LAN, etc)

- **Operating (Product) Companies with Active  
"Value Licensing" Programs**

(Qualcomm, IBM, Alcatel-Lucent)

◆ Note: these two categories could also be considered to be *strategic* buyers

# Types of Financial Patent Buyers (cont.)

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## Defensive FPBs:

- **Buying Collectives (anti-NPE or anti-dominant player)**  
(AST, RPX, OIN)
- **OpCo's sued by competitors for patent infringement**
- **OpCo's seeking to lower future cross-licensing payments**
  - ◆ Note: the latter two categories also could be considered to be *strategic* buyers

# FPB Valuation Model

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The valuation methodology typically used by FPBs is:

**Step 1 - Calculate the Risk-Adjusted Net Present Value by:**

- Estimating the Best-Case Return from Litigation *and then*
- Applying Appropriate Discounts for
  - Patent-Related Risks
  - Cost of Capital (time value of \$)

**Step 2 - Review Comps for order-of-magnitude sanity check**

It should be readily apparent that this is  
***more art than science!***

# FTB Valuation Model (cont.)

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## What are the *Best-Case* ROI Assumptions?

- **Current Infringement**  
(vs. placing a bet on technology evolution)
- **Clear Infringement**  
(requires bulletproof claim charts)
- **Large Impacted Market**  
(requires compelling market data)
- **Substantial Damages**  
(by application of reasonable royalty to impacted market over time)

# FTB Valuation Model (cont.)

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## What are the Applicable Discount Factors for Patent-Related Risk? (cont.)

- Infringement avoidance (design-around potential, disruptive technology)
- Infringement detection (reverse engineering, internal process details)
- Encumbrances (outstanding licenses, RAND obligations, etc.)
- Invalidity risk (uncited prior art, KSR, Bilski, etc)
- Markman risk – potential narrow (non-infringing) judicial claims construction
- Enforceability risk (inequitable conduct, terminal disclaimer, etc.)
- Claiming issues (means-plus-function, single infringer rule, etc.)
- Title defects (board/shareholder approval of prior transfers, UCC-1 general intangible security interests, joint ownership, etc.)

# FTB Valuation Model (cont.)

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## What are the *Applicable* Discount Factors for Patent-Related Risk? (cont.)

- Portfolio make-up --
  - Size of portfolio/family
  - Issued patents vs. pending apps
  - US vs. foreign coverage
  - Portfolio structure - vertical vs. horizontal relationships
- Litigation history
- Changing legal environment
  - Case law (eBay, Bilski, entire market rule, etc.)
  - Legislative reform (e.g., damages apportionment)
  - Regulatory intervention (e.g., FTC def. of reasonable royalty)
- Etc., etc., etc.

# FTB Valuation Model (cont.)

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## Use of “Comps” as a Sanity Check on NPV Calculation

### Limitations –

- Little publicly available transaction (sale) data
- Inherent difficulty of determining what *is* a comparable patent portfolio
- Extrinsic deal factors in other transactions (e.g., cross-license, tech transfer)

# Economics

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## Options --

- **Outright purchase (lump sum)**
- **Revenue share ("back-end")**
- **Mixed – Front-end plus back-end**

**Fixed**

**Contingent back-end with patent reversion if financial milestones are not met**

- **Staged – Front-end plus fixed installment payments**

**Secured by Promissory Note**

**Patent reversion if deferred payments are not made**

- **Other**

# Deal Structures

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## Options –

- **Joint Venture – Contractual or LLC**
- **Conditional Assignment / Patent Mortgage**
- **Representation Contract**
- **Other**

# Risk-Adjusted NPV Example

	YEAR						
	1	2	3	4	5	6	7
Experts and expenses	\$ (500,000)	\$ (500,000)	\$ (500,000)	\$ -	\$ -	\$ (500,000)	\$ -
Damages (Your Expert)	-	-	-	-	-	-	150,000,000
Contingency Firm	-	-	-	-	-	-	(60,000,000)
<b>Net</b>	<b>\$ (500,000)</b>	<b>\$ (500,000)</b>	<b>\$ (500,000)</b>			<b>\$ (500,000)</b>	<b>\$90,000,000</b>
Discount Rate	75%						
<b>NPV</b>	<b>\$4,887,844</b>						

**Note:** this is the Top-Line FPB (ROI) view.

The Defensive FPB will substitute counsel fees for contingency reduction, but the applicable patent risk discounts should be the same.