

# Forgotten Gems

## How Successful Outlicensing Strategies Maximize the Value of Patent Portfolios

By Pete Pappas and Josh Aronson

Patents can be among a corporation's most valuable assets, but many corporations fail to exploit the value of their issued patents (perhaps because the maintenance of a large patent portfolio can be expensive and time consuming). Nevertheless, when a company implements a successful outlicensing strategy, forgotten patents, instead of simply gathering dust, have the potential to increase revenue and stifle competition.



### A Valuable Commodity

A successful outlicensing strategy maximizes the monetary value of an intellectual property (IP) portfolio. Unfortunately, many companies view the expenses associated with research and the protection of intellectual property as ordinary and unavoidable business costs. However, an average product line uses only 20% to 40% of a company's research results.<sup>1</sup> A business that shields its intellectual assets from external use loses money on the remaining 60% to 80% of its development efforts.<sup>2</sup>

A company should consider whether its IP portfolio can be a valuable commodity rather than viewing it as a burden. By carefully protecting and licensing its intellectual property, a business can maximize the value of these assets.<sup>3</sup> IBM's aggressive outlicensing program increased its licensing royalties by 3,000% over the last decade (*Jones*, 1). IBM currently generates nearly \$2 billion annually in licensing revenue.<sup>4</sup> Prior to its acquisition by AT&T, BellSouth's licensing program

reportedly earned "tens of millions of dollars a year" (*IAM*, 7).<sup>5</sup> By following the lead of these companies, American businesses generate over \$100 billion in cumulative licensing revenues per year (*Jones*, 1).

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These figures illustrate how licensing can do more than offset the expenses associated with maintaining a large intellectual property portfolio. If properly executed, outlicensing can generate new revenue streams and increase shareholder value (*IAM*, 2). Carol Beckham, former vice president of BellSouth's licensing corporations, believes that "licensing out one's innovations in the form of IP to other companies is part of the value proposition" (*BellSouth*). General Electric's (GE) legal group uses licensing fees to pay for "all of the patent maintenance, prosecution, and preparation fees, and to make a profit beyond that."<sup>6</sup> GE's goal is to replace the "traditional business funding" of technological efforts with excess licensing revenues.<sup>7</sup>

A strong IP portfolio bolsters a company's ability to negotiate in various corporate transactions, such as joint ventures and mergers and acquisitions. An ability and willingness to cross-license a wide range of technologies facilitates access to technologies owned by other parties (*Jones*, 2). The success of BellSouth and IBM indicates that it is an "opportune time for many companies to develop comprehensive asset management plans in order to maximize the value of their IP assets" (*Hildbrand*, 1).

### Implementing a Successful Program

"There is no single formula for [outlicensing] success" (*Jones*, 1). Businesses should consider implementation of licensing programs that "fit the unique constraints, conditions, and aspirations of the company" (*Jones*, 1). The effort and investment required for an outlicensing program will vary depending on the extent of a company's IP portfolio and the company's ambition. Establishing an ambitious licensing initiative may take a tremendous effort. Outlicensing can be conducted on a small scale with less investment, but larger IP portfolios may allow for a broader outlicensing investment

with a greater chance for a profitable overall return. Although larger companies often form dedicated licensing teams, an efficient balance between inside and outside resources may be the most cost-effective model for some patent owners.

Even when taking into consideration the different characteristics of each organization, common problems and issues will arise during the implementation of a successful outlicensing program. Intellectual property in the company must be mined, valued and organized before executing any license agreement. This undertaking requires support from the corporate officers and the establishment of an interdisciplinary licensing team.

## Patent Mining

Typically, the first phase of any outlicensing program is patent mining. To successfully complete this first step, a company must do “substantial groundwork” (IAM, 15) to carefully catalogue and outline all available intellectual assets. Carol Beckham has said that “the greatest challenge has been to mine the IP out of a company the size of BellSouth, with more than 85,000 employees worldwide” (BellSouth). BellSouth had to do “a lot of digging” (BellSouth) to find all of its intellectual assets. GE faced a similar challenge because the company owns more than 11,000 patents.<sup>8</sup> The location of the intellectual assets, document retention policies, registration procedures and maturity of a business will influence the time and resources necessary to effectively mine for patents (Hildbrand, 1).

Many of the difficulties presented by patent mining may be handled by “interdisciplinary teams composed of staff from business development, research and development, the legal department, technology, strategic planning, new product development, and whomever else is needed to provide the requisite skills, authority, and organizational reach” (Jones, 3). Without this interdisciplinary mix, a patent mining team may be ill equipped to make the necessary decisions. The team must “assess whether each patent is fulfilling its operational and strategic potential” and determine whether the “cost of prosecuting a patent outweighs the potential licensing fees” (Jones, 3). These decisions benefit from the combined expertise of business executives, researchers, in-house lawyers and outside counsel. The assistance of outside counsel is especially desirable for planning and auditing patent portfolios, as well as estimating the costs of prosecution.

### A Well-Organized Portfolio

The large amount of data gathered during the “patent mining” process should be well organized. An organized portfolio makes it easier for the company to check the legal status of each patent and ensure a clear chain of title for every asset (Hildbrand, 1). Organizing the intellectual property into technologically related groups enables potential licensees to quickly solve technical problems.

GE organizes its portfolio by technology groups because it includes “lots of solutions looking for problems.”<sup>12</sup> GE also claims that this method of organization helps its engineers conduct research to fill the gaps in the company’s current technology. The engineers’ awareness of GE’s previously acquired technology keeps them from conducting repetitive research that goes over time and over budget.<sup>13</sup> GE uses “Internet Technology Transfer” to store and advertise its portfolio of licensable patents online.<sup>14</sup> This service allows users to organize the portfolio in any manner with a simple click of the mouse. In addition, the Internet provides GE with the ability to make the portfolio accessible by all its employees and design centers throughout the world. This wide access ensures that all of the research facilities work toward common goals. The Internet also gives GE immediate exposure to a huge number of potential licensees.<sup>15</sup>

Even if a company decides not to pursue a licensing program, mining and organizing its intellectual property is beneficial. In addition to the advantages it provides researchers and engineers, the organized portfolio makes it easier to identify and pursue potential infringers.<sup>16</sup> The patent licensing division at Texas Instruments continually monitors its catalogue in an effort to locate infringers. Once located, the company gives potential infringers a choice: take a license or face a lawsuit (IAM, 2). Although some corporations conspicuously pursue potential infringers, many preserve anonymity by using outside counsel. The use of outside counsel is advisable when the infringer is likely to reject the license offer. When litigation is imminent, a well-managed patent portfolio assists outside counsel with the identification of potentially infringed claims.

An essential part of the mining process is valuating the portfolio. Placing a value on a company's intellectual assets is "notoriously difficult" but critical for "effective management of intellectual capital" (Jones, 6). Accurate valuations help to "quantify strategic decisions" and encourage "managerial discipline" (Jones, 6). Companies also need this data to determine the appropriate royalty rates. Many businesses use an "opportunity matrix" to value their patents.<sup>9</sup> The matrix includes all of the indicators of value for each asset in the portfolio. The forward citation analysis is one simple indicator frequently used. Because most patents are only cited by competitors, the number of future citations may provide a rough indication of the technology's value.<sup>10</sup> Valuation requires an interdisciplinary mining team to work together on a number of issues and consider the many factors involved with patent valuation. Generally, these factors fall into three categories: legal, commercial and technology.<sup>11</sup> In order to successfully evaluate each patent, a team must analyze the invention in all three of these areas.



## Licensing the Entire Portfolio

After compiling and organizing the portfolio, companies must decide which intellectual property assets to license. While some businesses willingly license the entire catalogue, others restrict external access to a small percentage of the portfolio (IAM, 15). The larger and more successful companies seem to prefer the former approach. Lucent, for example, freely licenses its entire portfolio. Lucent's CEO even promises to license "any or all of [the company's] patents to anyone on a reasonable royalty basis" (IAM, 2). By allowing and encouraging competitors to license its technology, Lucent

- Gains a market advantage by collecting royalty fees from the competition;
- Raises awareness and demand for the company's products or technology in the marketplace;
- Encourages the competition to refrain from devising next generation technologies due to the low cost license; and
- Motivates its employees to discover new technologies that maintain the company's position as a market leader (IAM, 15).

Lucent places a great deal of emphasis on limiting its competition from investing in development efforts. To help achieve this goal, Lucent licenses "know-how" along with its patents. Aside from increasing the price of royalties, Lucent believes that access to "know-how" further discourages other businesses from investing in their own research and development. Lucent uses this approach to help maintain its lead in the related technological fields (IAM, 9).

Sony and Philips also benefited from this strategy during the 1980s. By freely outlicensing patents related to compact disc players, these two companies established a new

music industry standard (Jones, 1). An open outlicensing policy encourages other businesses to test the inventions and provide valuable feedback about the technology (Jones, 2). Any company starting a licensing program should consider these various strategies when deciding which patents to license. Although counterintuitive, an open outlicensing policy like Lucent's can be very advantageous.

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## Commitment to the Strategy

Because licensing initiatives require the cooperative effort of employees from several departments, obtaining and maintaining corporate support is critical. The success of the initiative will depend on the “willingness of [the] entire company to pursue and support this strategy.”<sup>17</sup> Early in the process, a chief executive should make it clear that the licensing program is an important endeavor (*IAM*, 15). The CEO of Thinkfire and former president of Lucent’s IP Corporation, Scott McCurdy, believes that “[t]he board has to be brought in and the CEO has to give things more than just a nod” (*IAM*, 2).



The executives must not treat licensing as an ancillary, self-managing project. The successful licensing programs at BellSouth, IBM and Lucent all receive significant support from corporate management. All of these companies have successfully integrated the company’s licensing initiative into the overall business strategy (*Jones*, 1). The chief executives should “continuously reevaluat[e]” (*Jones*, 1) every licensing program to ensure that it best serves the company. To build and maintain a successful and ambitious licensing initiative, the board must make a strong commitment to the program.

## Corporate Licensing Teams

Regardless of management’s dedication, a bold proclamation from a CEO may not be enough to implement a successful outlicensing strategy (*IAM*, 15). Some businesses may wish to establish a separate corporate licensing team (*IAM*, 15). Because of the “significant challenges” (*Hildbrand*, 1) that intellectual property management strategies present, corporate licensing teams should function as “a dedicated business unit rather than as a group which functions under another well-established corporate department such as law or new business development” (*IAM*, 16). The members of a corporate licensing team, like the patent mining team, should be an interdisciplinary mix of “staff from business development, research and development, the legal department, technology, strategic planning, new product development, and whomever else is needed to provide the requisite skills, authority, and organizational reach” (*Jones*, 3). The group should be able to “work across all business units, add continuity and consistency to the patent licensing process, protect the company from agreeing to questionable licensing deals, and present a unified front to all licensees.”<sup>18</sup>

BellSouth’s outlicensing program serves as a model for this approach. BellSouth started two wholly owned subsidiary corporations dedicated to maximizing the value of its intellectual property. The BellSouth Intellectual Property Management Corporate (BIPMAN) protected and mined all of BellSouth’s inventions and innovations. Meanwhile, the BellSouth Intellectual Property Marketing Corporation (BIPMARK) offered BellSouth’s intellectual assets to other businesses. BellSouth staffed these corporations with over 30 professionals from a variety of backgrounds. The sole task of these employees was to further the aims of BellSouth’s licensing initiative.

According to the former president, Jeff Clark, and former vice president, Carol Beckham, of BIPMAN and BIPMARK, a separate and distinct licensing team is required because negotiating with a licensee is very difficult. The typical negotiation takes “a real long time” (*BellSouth*) but frequently fails to result in an agreement. Licensees from smaller companies often face budget cuts during negotiations that force them to withdraw (*BellSouth*). Even if negotiations proceed smoothly, the typical license agreement is still a very complex contract. Issues such as duration, royalty rates,

geographic scope and exclusivity raise difficult questions that much be addressed in every license agreement. A fulltime interdisciplinary group may help resolve the common issues. Without BIPMAN and BIPMARK, it is likely that BellSouth's licensing initiative may not have achieved a high level of success.

## A Worthwhile Investment

Establishing a successful outlicensing initiative is not a simple process, even with modest ambitions. The program at BellSouth demonstrates that an extensive licensing program may require a large commitment from everyone in the company. The CEO and board may have to dedicate a great deal of time and resources to successfully mine, organize and value the patents. An interdisciplinary team dedicated to licensing helps execute these tasks and negotiate the outlicensing agreements. Despite the large and expensive commitment, licensing's potential financial benefits make the investment worthwhile.

## Endnotes

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*Pete Pappas is the Practice Group Leader of Sutherland's Intellectual Property Practice Group, where he concentrates primarily in chemical patent prosecution and also handles mechanical patent prosecution, federal trademark prosecution, licensing and other intellectual property transactions, validity and infringement opinions, and litigation support. Josh Aronson is a member of Sutherland's Intellectual Property Practice Group, focusing his practice on office actions and patent applications for medical and drug-delivery devices, chemical processes, beverage additives and polyester additives. Before joining Sutherland, Josh served as an intern with the American Pacific Corporation, working in the company's chemical research lab on projects involving energetic molecules and polymers, which also served as topics for his doctoral thesis.*