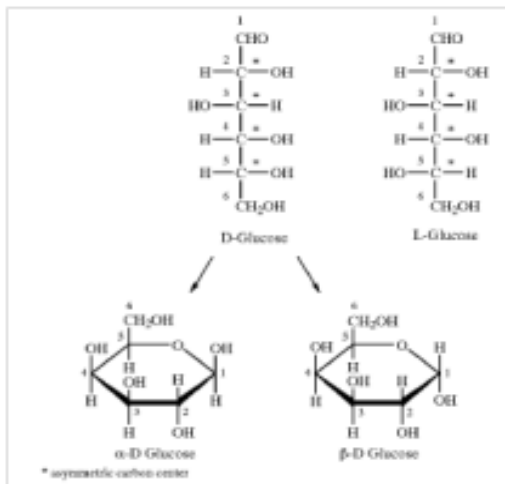


Why Are There Eight Million Patents? (Or how to increase the value of your company by 92%.)

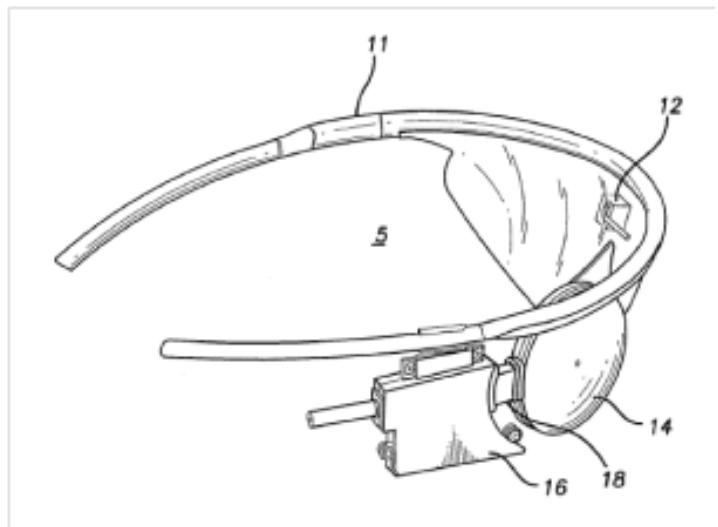
By Tom Kohler on January 31, 2012

On August 16th last year, [United States Patent No. 8,000,000](#) was issued by the USPTO. And with over [400,000 new applications](#) filed every year from 2006 through 2010, it is likely that patent number 9,000,000 will come even faster than the five years between Nos. [7,000,000](#) and 8,000,000.

Patent No. 7,000,000



Patent No. 8,000,000



Someone must think patents are worth something, in spite of the fact that only about 0.35 % of available patents are litigated in any given year (see my calculation at the bottom) and [only about 58% of those are successfully litigated](#). Of course there are some well published success stories, e.g., the [Cohen-Boyer patents](#) on recombinant DNA that brought in over \$250 million in licensing revenue to Stanford University, or [Robert Kearns](#), who successfully enforced his patents on intermittent windshield wipers against Ford and Chrysler, earning around \$30 million (and inspiring a [movie](#) about his life). But given the number of patents out there, such stories are certainly not the norm. So what drives all those patent filings?

It may be simple economics – patents create value → companies create patents. I recently came across a thorough and fascinating study that concludes that for start-up companies in technology-intensive sectors “a doubling of patent application stock for a given firm is on average associated with a **92% increase in pre-money valuation**.” ([Hsu and Ziedonis, Patents As Quality Signals For Entrepreneurial Ventures, p. 20, presented DRUID Summer Conference, Copenhagen, Denmark June 2007.](#)) The authors use a complex statistical analysis to arrive at this conclusion. They also provide a number of different scenarios with different variables taken into account. In one scenario, based on mean values encountered in their study, it is posited that a \$200,000 investment in patent applications may lead to a \$12 million increase in company valuation (see their footnote 16). Other

positive effects from increased patent activity are also identified (if a 6000% return on investment isn't enough for you): increased likelihood of securing initial funding from a prominent venture capitalist and increased likelihood of a successful IPO.

I have seen this effect first-hand in financing transactions, particularly with start-up companies in the medical device sector. Large schedules of patents and patent applications are treated reverentially by investors, with the number of patents and applications often receiving more scrutiny than the content of any particular patent or application on the schedule. But that is not to say that quality is not important. In one particular deal involving the sale of a company's assets, I was later told by the purchaser that the majority of the roughly \$14 million purchase price was based on the promise of a handful of provisional applications – filed only a month before the transaction closed and costing less than \$20,000.

Statistical analysis and anecdotal evidence thus suggest an investment in increasing your firm's patent numbers and patent quality has the potential for a return many times over. And that is the biggest reason why there are 8,000,000 United States patents and counting.

(Being an engineer and a lawyer, I could not stop myself from presenting this calculation: % patents litigated in a year = about [3000 patents sued upon in the year 2000](#) divided by 866,008, based on an assumption that 50% of approximately [1,732,016 patents issued](#) in the 17 years from 1983-2000 remained in force that year and were available for suit.)

Tagged as: [Business](#), [Patent](#), [Valuation](#)