
To sell or to license - that is the question

Many factors play into the decision to sell or license an IP portfolio. However, in large corporations the competing views of different departments may further complicate the issue

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The question of selling or licensing arises after an IP owner has decided to consider monetising all or part of its IP portfolio and has a sense of the portfolio's economic potential. With this in mind, the IP owner must decide whether to monetise by selling or licensing. This decision is complex, with a number of factors to be analysed and evaluated. An additional layer of complexity arises within larger corporations, as the decision affects various functions or departments which may have opposing views on the question. This chapter explores the factors to consider and provides options for addressing the obstacles to the chosen strategy.

Preliminary questions

The process starts with a strategic management decision to consider monetising the company's IP portfolio. But what drives the IP owner to reach this point? The decision is made for different reasons in every organisation, but a number of considerations are likely to play a part in the decision-making process:

- The IP owner has become more aware of the value of its intangible assets.
- The IP owner has an IP strategy that is tied to its corporate strategy.
- The IP owner is seeking additional revenue and cash to operate its business, to stay in business or to return to its shareholders.

The question that follows from this decision is: what is the economic potential of our IP portfolio? Unless the portfolio is very small, answering this question requires a complex analysis. At a minimum, the following characteristics – which are indicators of a greater economic potential – should be identified:

- The IP portfolio has an early priority relative to the technology lifecycle.
- The technology that is protected by the portfolio is implemented in products from other corporations.
- This implementation can be proven.
- The markets that the technology is addressing are high-volume, high-margin markets.
- The opportunity cost of designing around or invalidating the portfolio is significantly higher than the royalties for using it.

This analysis should be completed before the IP owner decides to sell or license all or part of the portfolio.

Basic differences between selling and licensing

Licensing promises the highest total return on monetising an IP portfolio. The calculation is simple: the IP owner can license the same asset (ie, the IP portfolio) to a number of different licensees, which in most cases will generate higher revenues than selling the asset once to one purchaser. Licensing takes longer to generate revenue and comes with risks; selling provides revenue now, with no risk.

Successful licensing requires an IP portfolio with a high economic value, but also requires additional investment. It must be driven by a team that can derive the economic potential from the portfolio. An experienced team must

be created and given the funding to execute a proactive licensing programme. Existing IP teams in organisations are often not designed or adequately funded to engage in proactive licensing. Investment is required for the team, for ongoing maintenance fees and for external consultants and suppliers to provide support in areas such as proof of use.

Moreover, in most cases the potential licensee is unwilling to pay a royalty voluntarily, which means that the IP owner will have to pursue litigation. This requires further investment and involves added risk.

In general, selling is a risky transfer from the seller to the buyer, with the buyer assuming the risks of ownership. Usually, the seller obtains a licence back to secure its own freedom to operate.

Sales of IP portfolios tend to involve an intermediary patent broker. The different types of potential buyer that can be pursued include the following:

- An investor that wishes to establish and operate a licensing programme will consider the risk and the ‘time to money’ for a successful licensing programme and discount the purchase price accordingly.
- A defensive patent aggregator will purchase the IP portfolio to ensure that it is not asserted against its members by the current owners (or anyone else).
- A strategic buyer that uses the technology will purchase the IP portfolio to eliminate a potential infringement problem and potentially to assert the portfolio against its competitors.
- A strategic buyer that is looking to enter the market in which the technology is used may require ammunition in case a competitor approaches it with a licensing programme or for other strategic reasons, such as keeping certain organisations out of the market.

In all cases, the seller can gain only a fraction of the portfolio’s economic potential. In addition, if the seller wants to negotiate the best price, it must expend resources in finding the buyer and preparing substantially the same analysis that would be needed for a successful licensing programme.

Deciding factors

Certain but lower revenue today, with no

further investment, can be achieved through selling, whereas far greater – but uncertain – revenue can be achieved by investing in a licensing programme. The ultimate choice depends on a number of factors, many of which are closely related.

Conflicting strategies and internal impacts

The possible conflict between an IP monetisation strategy and the company’s internal strategies (as pursued by sales teams, business development teams, investors and others) is a crucial factor to be considered. In some cases, internal business strategies may overrule and ‘kill’ proactive licensing strategies for an IP portfolio, even though the portfolio has considerable economic potential. Impacts on customers, suppliers and other partners must all be considered, along with investors’ strategies for returns on their investments. The possible consequences of litigation – as a plaintiff, but also potentially as a defendant in a countersuit – must be carefully reviewed. The greater the potential negative impacts of licensing on the IP owner’s business, the more likely it will be to sell the portfolio in order to separate the operational business from any licensing activities related to the portfolio.

Organisation size and exposure to cross-licensing

The IP owner must consider who the potential licensees are and how they will react. If the portfolio will be asserted against potential licensees that are outside the IP owner’s market, do not have a portfolio that could be asserted against the owner or are significantly larger than the owner, then the latter’s exposure to a net payment on a cross-licence should be minimal. In such cases this factor should not prevent the IP owner from licensing its portfolio. In other situations, where the IP owner faces significant exposure in a cross-licence situation, sale may be the better choice.

Risk

Selling an IP portfolio essentially eliminates risk. Licensing presents a number of risks, including:

- The possibility that no revenues are realised (either because the patents are invalidated or because infringement cannot be proven), or that the revenues are lower

than expected.

- The possibility of a cross-assertion or a countersuit and the potential negative impact on the operational business.

An organisation that is more tolerant of risks – and can afford to take them – will be more likely to pursue licensing, whereas a more risk-averse organisation will be more likely to sell. Therefore, financially sound organisations are more likely to license and distressed organisations are more likely to sell.

Ongoing investment

Closely related to risk and financial condition is the potential need for ongoing investment. Licensing patents requires such investment, so selling may be the better option for an IP owner that is unable or unwilling to commit to such investment.

Time-to-money factor

The time-to-money factor can be considered in two different contexts:

- A situation where the IP owner has limited time due to economic constraints, but the potential licensee or buyer has no such pressure, puts a would-be licensor in a weakened position, as the potential licensee will use all of its options to extend the process, knowing that the IP owner is under financial pressure. A quick sale strategy may be the better choice.
- Where the IP owner has no time limitations, but the potential licensee or buyer has limited time due to business constraints – for example, where it is about to launch or has already launched a new product – the IP owner is in a much stronger position. The opportunity costs for the potential licensee or buyer are high and are increasing. Licensing is a more attractive option for the owner, although there is a risk that it may overestimate its position and miss the right time to licence or settle.

In either case, a deal should be closed quickly, as time is the enemy of all good deals.

Size

The size of the IP portfolio is a vital factor. A small group of patents may have extraordinary

economic potential; today, however, the likelihood of securing hundreds of millions of dollars (or even tens of millions) from a large corporation for a small IP portfolio is relatively small. The considerations from the perspective of a potential licensee or buyer are simple: what will be the cost of invalidating the group of patents and how long can the IP owner withstand litigation? If the internal evaluation on the would-be defendant's side shows that it might be cheaper to fight, that is likely to be the choice.

Another significant element is the portion of the IP portfolio that is not being sold. The unsold portion retained by the IP owner must be large enough and cover the necessary technology areas to support its ongoing business and commercial strategies. In contrast, licensing allows the owner to monetise its portfolio while maintaining ownership to support its ongoing business.

Other options

Further strategies may be more appropriate for a particular IP owner's situation or may be applied to part of an IP portfolio to supplement selling or licensing. Two of these options are discussed below.

Sale with a back-end

Where an IP owner is interested in the revenue potential of licensing, but is concerned about the risks, the potential for a cross-licence or the necessary investment, a possible solution is a sale with a back-end. All or part of the portfolio is sold and legally transferred to an independent holding company. This holding company may be in a tax-optimised location (eg, Luxembourg, Switzerland or Singapore). The purchase price can be partly fixed, with a component linked to future success, or else fully success-related – 'success' normally being defined in terms of a share in any royalties earned from the transferred portfolio. The IP holding company will assign licensing agents and litigators to establish and operate a licensing programme. The previous IP owner is kept separate from litigation or licensing activities, as it is unrelated to the IP holding company, but benefits from the success that is related to the purchase price of the portfolio.

The IP holding company structure allows

for the complete separation of the IP portfolio and its related licensing activities from the operational business of the previous IP owner. For corporations that face high levels of business exposure, high cross-licensing exposure and high risk of impact on their operational business, the IP holding company represents an attractive option.

Increase in business

If a current or potential customer is using a technology protected by the IP portfolio of a supplier or possible supplier, the customer has indicated that it likes and needs the supplier's technology. This presents another interesting monetisation possibility: an increase in operational business through increased sales to a current or new customer by showing patent infringement, the need for licensing and the benefits of an increased business relationship.

The preconditions for this option are the same as those for successful licensing. In this case the IP owner assembles an economic package in two parts, offering to supply the product or service that the potential licensee normally buys from a competitor and to provide a licence for the necessary intellectual property. This can create mutual benefits. The potential licensee gets a (potentially better) product or service and a licence to use the intellectual property, eliminating its IP problem. The IP owner gets more than just royalties (normally only a one-off settlement), as it increases its operational business, which leads to higher and more sustainable margins than the royalty settlement option.

In most cases, the owner of the IP portfolio must have an experienced internal team to run such a programme. Alternatively, it must pay by the hour to acquire these services externally, as most licensing agents working on a contingency basis are interested in licensing programmes that generate settlements.

Conclusion

The decision to sell or license depends on various factors that the IP owner must consider and evaluate together. In general, licensing will deliver the highest returns for IP monetisation, but higher returns come with higher risks and the need for additional investment. IP owners must consider and evaluate all the factors

discussed here to determine the returns, risks and costs associated with both selling and licensing. Armed with this knowledge, they can make an informed decision on how best to monetise their IP portfolio. The answer to the question of whether to license or sell is... it depends! **iam**

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Mr von Scheffer is a member of the board of LES Germany, vice chairman of LES International's communications committee and an accredited expert in patent evaluation, technology transfer, licensing, IP strategy and finance for the European Commission, the United Nations, the Organisation for Economic Cooperation and Development, the World Intellectual Property Organisation, the European Patent Office and the German Patent Office.

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Mike Thumm is responsible for driving licensing programme success at Pachira. He has strong roots in supporting the world's largest clients in semiconductor and microelectronics patent licensing. Before joining Pachira, he led the IP services team at Chipworks, where he was responsible for providing compelling evidence of patent infringement in support of negotiations and litigations worth hundreds of millions of dollars. Under Mr Thumm's leadership, the IP services team increased its market breadth and expanded into new areas, driving growth. During his tenure at Chipworks, he also served as chief financial officer, where he established Chipworks' first corporate partnership aimed at assisting companies in monetising their patents.

Highly regarded for his business and technical acumen, Mr Thumm has been an invited speaker at key industry events and has written articles on patent licensing for major trade publications. He is a member of the Licensing Executives Society.