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# Corporate IP Programs: A Discussion on the IP Marketplace and Portfolio Valuation

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**OCEAN TOMO**  
INTELLECTUAL CAPITAL EQUITY

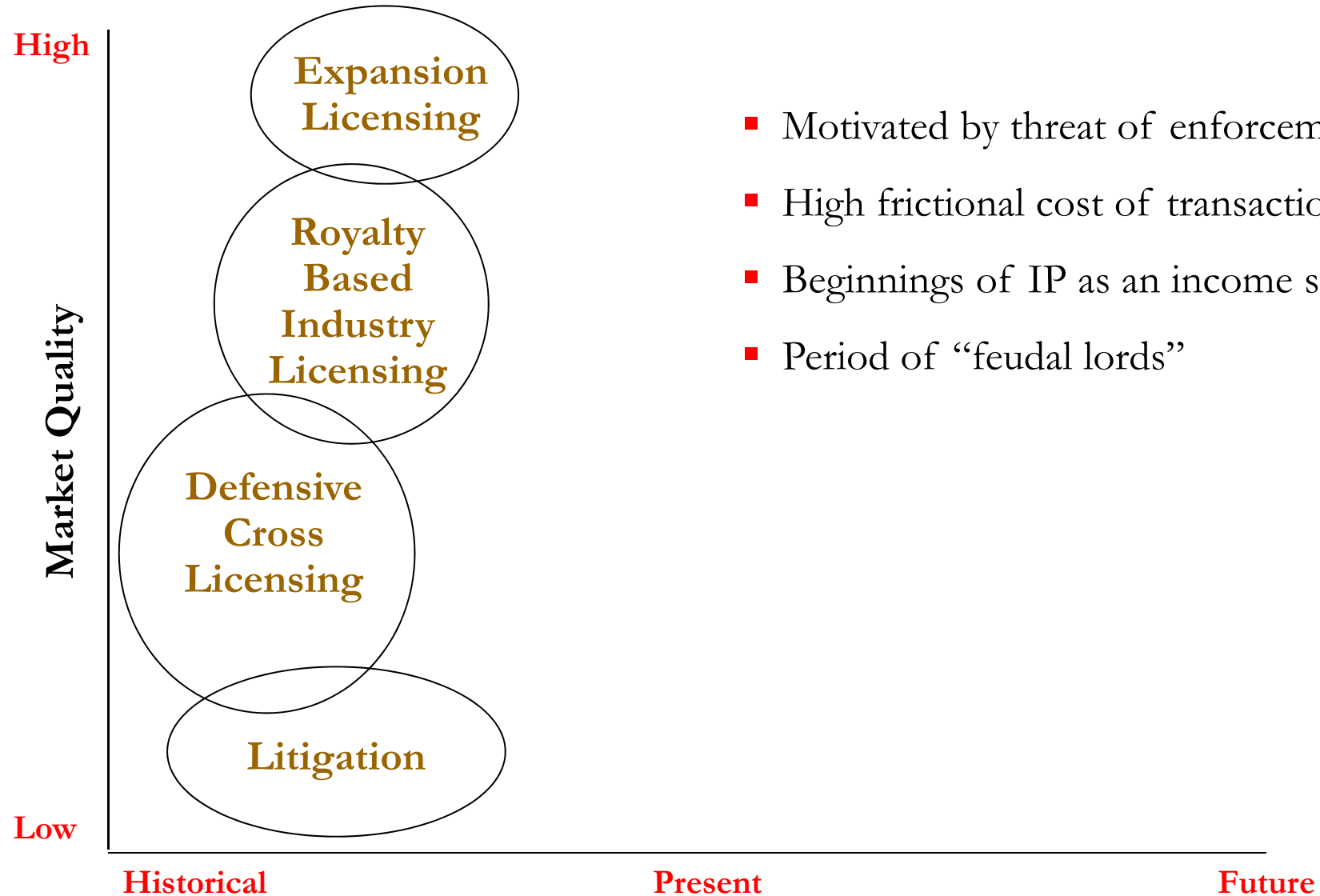
# Agenda

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1. **The IP Marketplace**
2. **What to do Now to Extract Value**
3. **Methods of IP Valuation**
4. **Pre-Valuation Due Diligence**

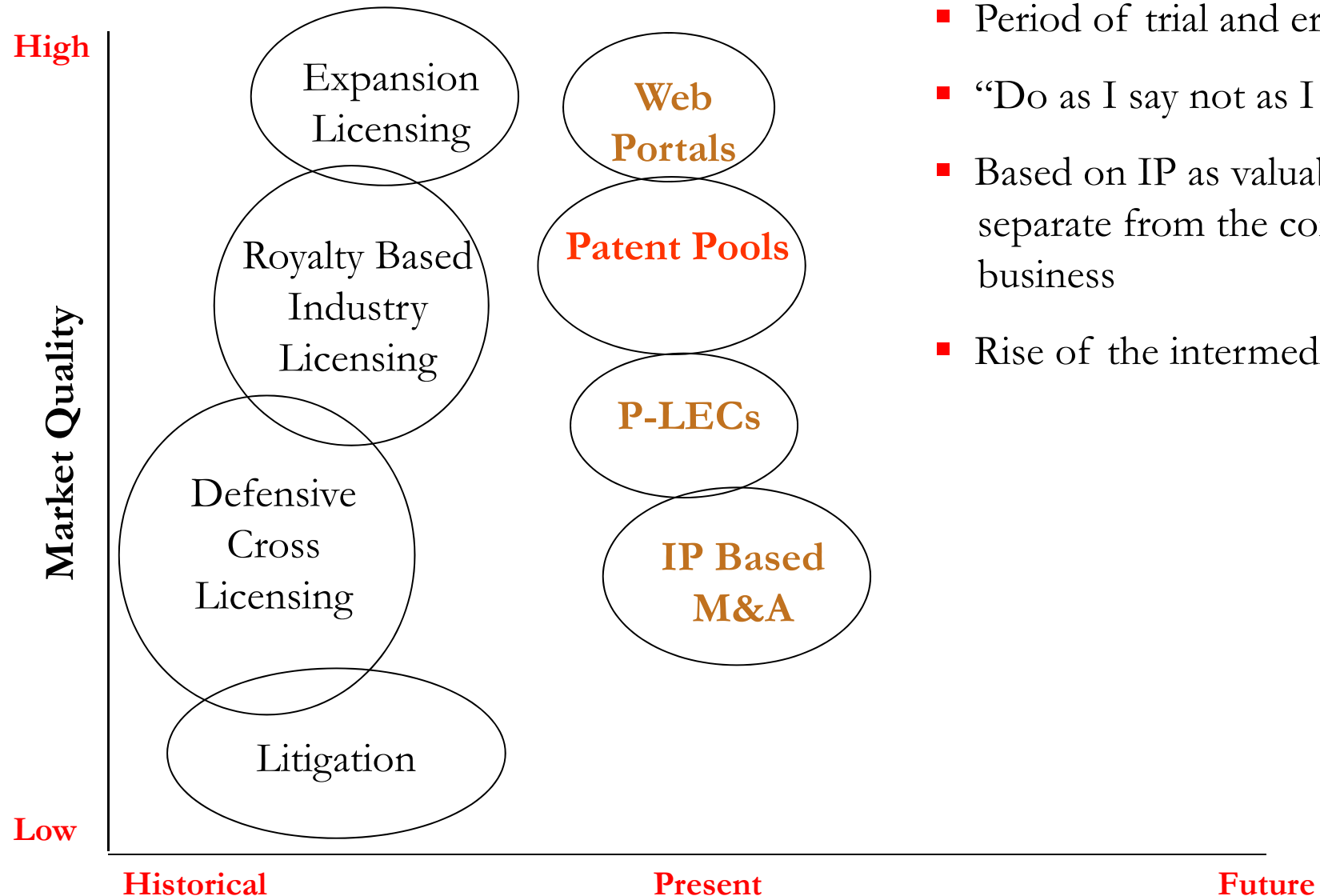
# IP Marketplace: The Past

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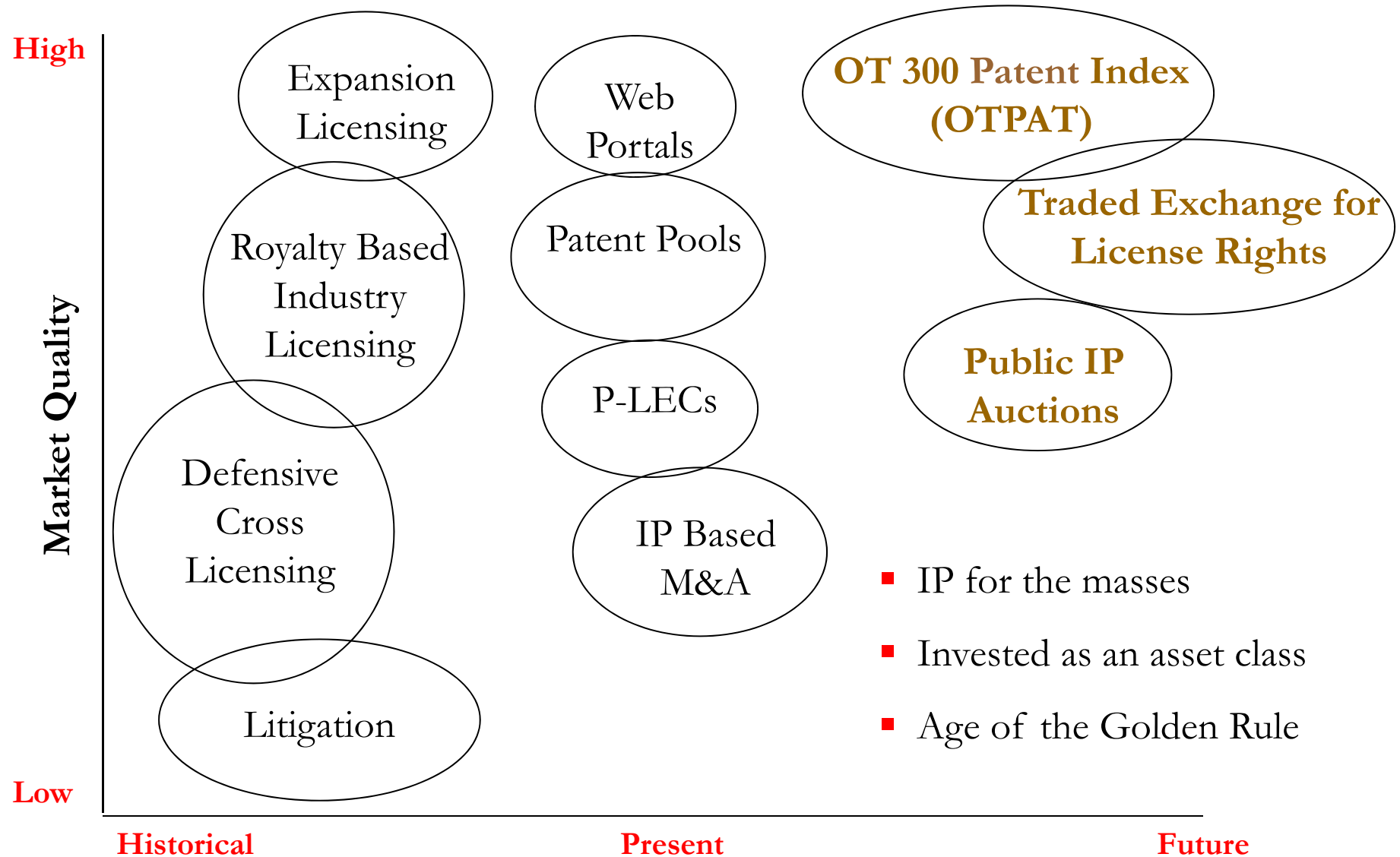
- Motivated by threat of enforcement
- High frictional cost of transactions
- Beginnings of IP as an income stream
- Period of “feudal lords”

# IP Marketplace: The Present



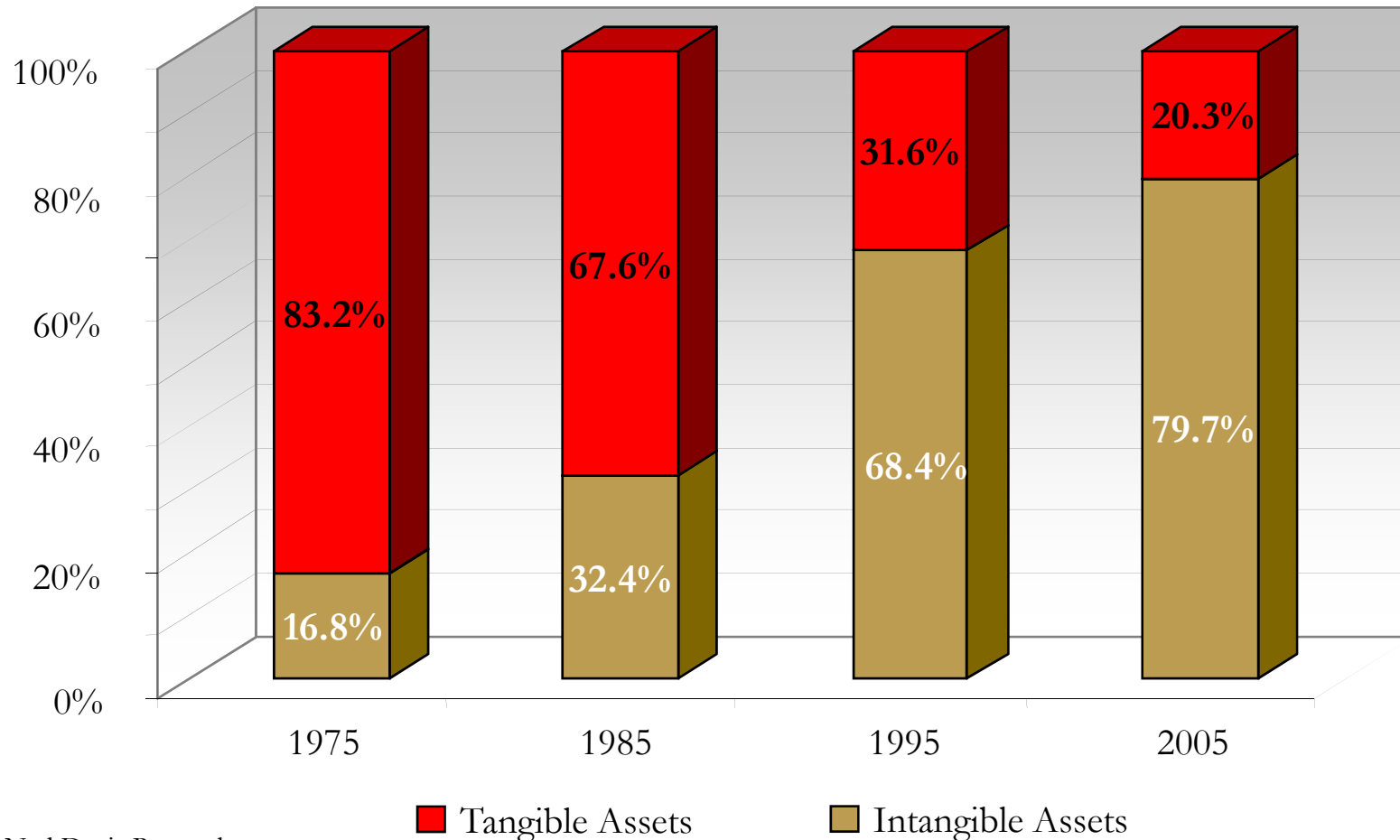
- Period of trial and error
- “Do as I say not as I do”
- Based on IP as valuable separate from the core business
- Rise of the intermediaries

# IP Marketplace: The Future



# IP Marketplace: Public Equity

## Components of S&P 500<sup>®</sup> Index Companies' Market Value



Source: Ned Davis Research

# Some Stats and Info

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- **Global licensing revenue is greater than \$150 billion and is growing at 25% to 35% per year**
- **IBM collected more than \$1.5 billion in royalties last year (and donated 500 patents for open source)**
- **Microsoft paid more than \$1.4 billion in royalties last year (and is looking to cross license with the 30-40 top technology companies)**
- **Intellectual Ventures has raised more than \$350 million to execute its strategy of acquiring patents for [guess!!??]**

# Overlooked Assets

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Some **49%** of companies said they relied primarily on intangible assets to create shareholder wealth, yet only **5%** had a robust system to measure and track the performance of intangible assets.

*Intangible Assets and Future Value*

Accenture Ltd.

2003 Survey of 120 Senior Executives.

# Business Week: Best Fund Managers 2006

\* Returns as of 2/28/06

<u>Fund Name</u>	<u>Fund Manager(s)</u>	<u>Performance</u>		
		<u>1 Year</u>	<u>3 Year</u>	<u>5 Year</u>
T. Rowe Price Equity Income	Brian Rogers	7.56%	18.57%	6.72%
Legg Mason Value Trust	Bill Miller	8.43%	20.12%	4.42%
Janus Mid Cap Value	Thomas Perkins Robert Perkins Jeffrey Kautz	12.95%	24.73%	13.13%
Oppenheimer Main St. Small Cap	Nikolaos Monoyios Mark Zavanelli	19.31%	29.69%	14.09%
Stratton Growth	James Stratton	11.48%	29.75%	12.62%

# But ... Your Resume Says What!?!??

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John Doe, Esq.  
123 Main St.  
Anywhere, USA 12345

Fortune 500 Company, Inc., Anywhere, USA      *2003 to present*  
***Chief IP Counsel***

- Responsible for **managing** company's intellectual property portfolio collection activities.

# IP Creates Value Through a Variety of Mechanisms

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## Exclusivity Value:

- Price premium
- Reduced manufacturing cost
  - Increased market share
- Enhanced customer satisfaction
  - Blocking value

## Option Value:

- Current technology and protection may provide an avenue for future investments

## Defensive Value/ Freedom to Operate:

- Creates an IP arsenal to discourage lawsuits
- Provides ability to compete, but little advantage

## Trading Value:

- Value in trade for entering into cross-licenses, for licensing-out, or for sale

# What to do Now? Leverage IP In Deals

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1. **File early and often, especially in negotiations with partners and vendors, and focus on key value propositions of business processes and software**
2. **Perform due diligence to understand the true strength of your IP**
3. **Assert IP position early in business negotiations, leveraging patent applications as well as patents**
4. **Show your hand if necessary to convince the other side of your superior IP position**
5. **Whenever possible, show your business clients how the IP may positively impact or even drive a deal**
6. **Train business clients to think about IP when there is an impasse or dispute in their deals**

# What to do Now? Leverage IP To Generate Revenue

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## *Target One-Off Licensing Projects In The Early Stages*

1. Find “low hanging fruit” (and publicize successes)
2. Focus on non-core and core IP licensing opportunities
3. Look for opportunities to license the combination of IP and software/technology
4. Find competitive and non-competitive entities that are using or may need the IP
5. Create “win-win” scenarios whenever possible (carrot vs. stick licensing)
6. Hire consultants to understand the relevant field

# What to do Now? Leverage IP To Generate Revenue – cont.

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## *Strategic Long-Term Licensing - Identifying Core IP*

1. Talk to business leaders to find the core competencies
2. Talk to strategic planning teams to determine if the core competencies will be critical in the future
3. Prioritize the core competencies by importance to the business
4. Drill deep into the core competencies (be an expert)
5. If there are IP protection gaps, fill them
6. At the earliest possible stage, begin internally selling the idea of licensing core IP

# The Future: IP-Based Financing

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- **IP Asset Backed Securitization**

- Type of asset-based financing backed by contractual payment flows
- Requires sale of underlying assets to bankruptcy remote entity
- Relies only on the cash flows from the securitized assets for repayment
- Credit of entity becomes less relevant than quality of IP
- Typically, it's a cheaper source of funds
- Loan is Non-recourse

- **IP Sales/Lease Back**

- **IP Collateralization**

*Transforming Underutilized IP Into Working Financial Assets  
To Build Shareholder Value*

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# Price versus Value

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**“Price is what you pay.  
Value is what you get.”**

**-- Warren Buffett**

# Price: Courts Know Damages!

Parties	Award	Date	Source	Court
1 Polaroid v. Eastman Kodak	\$873,158,971	Jan-91	17 USPQ2d 1771	D. Massachusetts
2 Michelson v. Medtronic Sofamor Danek	\$529,000,000	Oct-04	National Law Journal	W.D. Tennessee
3 Eolas Technologies v. Microsoft	\$521,000,000	Aug-03	Wall Street Journal	N.D. Illinois
4 City of Hope Medical v. Genentech	\$500,100,000	Jun-02	New York Times	Sup. Ct. California
5 Johnson & Johnson v. Guidant	\$425,000,000	Sep-03	National Law Journal	Arbitration Panel
6 Johnson & Johnson v. Medtronic	\$270,000,000	Sep-03	National Law Journal	CAFC
7 Haworth v. Steelcase	\$211,499,731	Dec-96	43 USPQ2d 1223	W.D. Michigan
8 Hughes Tool v. Smith International	\$204,810,349	Mar-86	229 USPQ 81	C.D. California
9 Procter & Gamble v. Paragon Trade	\$178,400,000	Jan-98	Press Release	D. Delaware
10 Exxon Chemical v. Mobil Oil	\$171,000,000	Aug-98	Wall Street Journal	S.D. Texas
11 Guidant v. Medtronic AVE	\$166,681,773	May-02	Judgement	Arbitration Panel
12 Viskase v. American National Can	\$164,900,000	Jul-99	Press Release	N.D. Illinois
13 Masimo v. Nellcor	\$164,000,000	Aug-04	CBS MarketWatch	C.D. California
14 Hughes Aircraft v. United States	\$154,000,000	Jun-94	Wall Street Journal	Federal Claims
15 Intergraph v. Intel	\$150,000,000	Oct-02	Wall Street Journal	E.D. Texas
16 3M v. Johnson & Johnson	\$129,000,000	Dec-92	Dow Jones Newswire	CAFC
17 Fonar v. General Electric	\$128,705,766	Feb-97	Final Judgement	CAFC
18 Mobil Oil v. Amoco Chemical	\$120,000,000	Aug-98	Press Release	D. Delaware
19 Stac Electronics v. Microsoft	\$120,000,000	Feb-94	National Law Journal	C.D. California
20 Internet Magic v. Netfax	\$114,000,000	Feb-02	National Law Journal	Sup. Ct. California

Source: IP Litigation: Assessing and Managing The Risks, James R. Sobieraj - Brinks, Hofer Intellectual Property Seminar

# Price: Defendants Know Settlements!

	SETTLEMENT	DATE	PARTIES	SOURCE
1	Michelson v. Medtronic	\$1,350,000,000	Apr-05	Associated Press
2	Sun Microsystems v. Microsoft	\$1,250,000,000	Feb-04	Press Release
3	Texas Instruments v. Hyundai	\$1,000,000,000	May-99	Wall Street Journal
4	Texas Instruments v. Samsung	\$1,000,000,000	Nov-96	Wall Street Journal
5	Medinol v. Boston Scientific	\$750,000,000	Sep-05	Associated Press
6	NTP v. Research in Motion	\$612,500,000	Mar-06	Wall Street Journal
7	Northrop Grumman v. Honeywell	\$440,000,000	Apr-04	Associated Press
8	Intertrust Technologies v. Microsoft	\$440,000,000	Dec-01	Press Release
9	Pitney Bowes v. Hewlett-Packard	\$400,000,000	Jun-01	Wall Street Journal
10	Yahoo v. Google	\$328,000,000	Aug-04	National Law Journal
11	EMC v. Hewlett-Packard	\$325,000,000	May-05	Associated Press
12	Intergraph v. Intel	\$300,000,000	Apr-02	Wall Street Journal
13	Medtronic v. Siemens	\$300,000,000	Sep-92	Wall Street Journal
14	MicroUnity v. Intel	\$300,000,000	Oct-05	Business Wire
15	University of Minnesota v. Glaxo	\$300,000,000	Oct-99	Press Release
16	Intermedics v. Cardiac Pacemakers	\$250,000,000	Sep-98	National Law Journal
17	Intergraph v. Intel	\$225,000,000	Mar-04	Associated Press
18	Gemstar v. General Instruments	\$200,000,000	Nov-00	National Law Journal
19	University of California v. Genentech	\$200,000,000	Nov-99	Press Release
20	Gemstar v. EchoStar Communications	\$190,000,000	Mar-04	Satellite Week
21	Boston Scientific v. Medtronic	\$175,000,000	Sep-02	Press Release
22	Taiwan Semiconductor v. SMI	\$175,000,000	Feb-05	National Law Journal
23	Intergraph v. Intel	\$150,000,000	Oct-02	Business Wire
24	Genentech v. Eli Lilly	\$145,000,000	Jan-95	Wall Street Journal
25	Intergraph v. Hewlett-Packard	\$141,000,000	Jan-05	National Law Journal

Source: IP Litigation: FTI Consulting

# Value: Cost Approach

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- **Value:** Cost to replace or recreate the asset
- **Theory:** Licensee is willing to pay as much as it would cost to develop the asset on its own but no more
  
- What types of costs should be included in the calculation?
- What are the strengths of this approach?
- What are its weaknesses?

# Value: Market Approach

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- **Value:** Arm's-length price paid in comparable transactions
- **Theory:** Licensee is willing to pay as much as others have paid for the asset but no more
  
- What constitutes a comparable transaction?
- What are the strengths of this approach?
- What are its weaknesses?

# Market Approach: Analyzing Comparables

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- **Specific rights conveyed in transaction**
- **Arm's-length transaction**
- **Special financing terms available**
- **Economic conditions at time of transaction**
- **Inclusion of non-IP assets in the transaction**
- **Functional characteristics of the guideline IP**
- **Technological characteristics of the guideline IP (stage of development)**
- **Economic characteristics of the guideline IP**
- **Legal characteristics of the guideline IP**
- **Other factors**

# Market Approach: Sources of Comparable Transactions

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- SEC
- Recombinant Capital (Recap.com)
- Royaltysource.com
- Windhover Information (Windover.com)
- Court records
- Licensing Economics Review (LER)
- LES publications (les Nouvelles)
- Industry presentations
- Licensing experts

# Value: Income Approach

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- **Value:** Present value of the expected cash flows from the subject intellectual property or expected increase in business value due to the intellectual property
- **Theory:** Licensee is willing to pay some portion of its economic gain from using the intellectual property
- What portion of the cash flows should be shared with the licensee?
- What are the strengths of this approach?
- What are its weaknesses?

# Income Approach: Key Calculations

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- Calculate incremental revenues (market share or premium prices) due to IP
- Calculate incremental cost savings due to IP
- Calculate relief from hypothetical royalty or lease payments
- Methods that calculate the overall business enterprise or similar economic unit as a result of owning the IP versus one that does not own the IP
- Appropriate discount rate calculation/estimation

# IP Pre-Valuation Due Diligence: Legal Considerations

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- Ownership analysis
- Maintenance records
- Completeness analysis
- Prior-art research
- Infringement/litigation analysis
- Encumbrance analysis (cross-licenses)
- Employee/consultant records
- Freedom-to-operate issues
- Other



**Determine existence,  
ownership and control**

# IP Pre-Valuation Due Diligence: Business Considerations

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- Next best alternative
- Cost to design around
- Benefits of design around
- Comparable transactions
- Gross revenues
- Gross/incremental profit
- Pre-tax profit
- Cost savings
- Incremental revenues
- Complementary assets
- Accounting for risk
- Other



**Determine economic,  
strategic and potential  
infringement value**

# Thank You!

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