

Business Opportunity Alternatives

By Ron Laurie

Part One of this series discussed the following forms of the business opportunity model of patent monetization: 1) outright sale of the patent; 2) exclusive field-of-use licenses; and 3) nonexclusive licenses and transfer of know-how. This month's installment addresses corporate transactions and various investment and financing vehicles.

CORPORATE TRANSACTIONS

The sale of a technology company whose corporate value or market cap is largely represented by “intangible assets” is, to some extent, a patent monetization transaction. The consideration for the sale can be all cash, all stock, or a combination of the two. The sale can occur via an asset sale, stock sale, forward merger, or reverse triangular merger, and a number of non-IP factors will influence the choice, such as assumption of seller liabilities and tax considerations; however, there is one situation where IP may affect the choice. In a reverse triangular merger the “seller” remains intact as a corporate entity and is acquired by a specially formed subsidiary of the buyer. In certain cases, the RTM form can avoid the loss (or renegotiation) of key in-bound licenses that have an anti-assignment restriction.

It is not unusual for a company to spin-out (or spin-off) a particular corporate business unit, division, or technology that is either no longer “core” to the business of the company or is not sufficiently profitable. The divestiture can be complete, *i.e.*, the seller retains no further interest in the divested business (spin-off), or the seller can maintain an ongoing financial stake in the new venture (spin-out). And, as in the case of sale of patents *per se*, the seller may want to retain limited rights to the IP that is owned by the new entity, *e.g.*, by way of an exclusive field-of-use grant-back license. One of the most difficult, and often contentious issues in the divestiture of less than an entire business is which patent rights remain with the seller and which go with the spin-out. This is typically resolved with some combination of ownership allocation via assignment and licenses to the non-owning party, which may be limited to the field of the retained business, and may be exclusive or nonexclusive (usually depending on the respective leverage of the parties).

One of the most interesting corporate-level patent monetization vehicles is the formation of a joint venture around a new corporate entity, a “Newco,” and the transfer by one or more of the joint venture partners of a subset of their patent rights to the Newco. For example, an aircraft manufacturer may have patents covering a local area network (“LAN”) architecture for the control and communication systems on an aircraft, but the patent claims may be broadly written to cover “vehicles” rather than “aircraft.” The aircraft manufacturer could form a Newco joint venture with an automobile manufacturer. In exchange for equity in Newco, the aircraft manufacturer would contribute an exclusive field-of-use license under its LAN patents in the automotive field, and the auto manufacturer could contribute operating capital and management expertise in the automotive area. Another model involves companies in complementary but noncompetitive fields pooling their expertise and IP in a new area that exploits both partners’ capabilities. In such a case, each partner would grant an exclusive field-of-use license to Newco limited to the field of Newco’s business (which is defined so as to not overlap with the business of either joint venture partner). In addition, one or more of the partners could contribute operating capital, unpatented know-how, machinery and equipment, technical employees, and/or management executives to Newco.

INVESTMENT AND FINANCING VEHICLES

An interesting new variation on the corporate spin-out theme involves what is essentially outsourced product and IP development financed by capital markets. Institutional investors have recently discovered that intellectual property, and patents in particular, comprise a commercial asset class like corporate securities and real estate, and like these traditional asset classes can be monetized in ways that produce financial returns to professional investor groups similar to private equity limited partners and REITs. This interest has produced a new corporate spin-out model for non-core technologies and associated IP that has, for various reasons, become “stranded” within large technology companies and likely will die if it remains where it is. The technology assets are spun out into a development company that has a finite life of say, six to 24 months, during which time the technology and IP is improved, extended, groomed, and packaged for one of a variety of exits, including M&A, creation of an operating company, creation of an exclusive field-of-use licensing company, creation of an assertion-based

(nonexclusive) licensing company, etc. The technology/IP originator assigns the IP to the spin-out (possibly with an exclusive field-of-use grant-back license in its core business area) and takes a minority equity interest in the spin-out entity. Operating capital during the holding period comes from high net-worth individuals or institutional investors. The value proposition to the technology originator is simple — a minority interest in something is better than full ownership of nothing.

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Finally, patents can be monetized by using them as collateral for what is essentially a loan. This may take the form of a conventional bank loan secured by IP or one of the recently introduced IP-backed asset financing vehicles, such as sale-and-license-back arrangements or the securitization of future royalty streams.

CONCLUSION

Based on the above discussion, one way to conceptually distinguish the assertion model from the business opportunity model is that the former deals with patents as a legally enforceable exclusionary right while the latter deals with patents as a commercially tradable asset class. When one views intellectual property, and patents in particular, in this way, the analogies to commercial exploitation of other asset

classes become evident. For example, many of the exploitation models associated with real property can be applied to patents, *i.e.*, aggregation, subdivision, development, brokerage, etc. Similarly, patents can be compared to corporate securities and the various services provided by traditional investment banks can be applied to patents, including broker/dealer services, merger and acquisition advisory services, equity underwriting, and so on. In fact, all of the business opportunity monetization options discussed above can be consolidated in one entity, the *IP Investment Bank*.

