Aggressive IP strategies open up new revenue streams

Forward thinking management structures and new fangled strategies are all well and good when a company decides it should make more money from its IP. But in almost every case, theory only turns to success when a business acquires a reputation for strongly protecting and enforcing what it owns

By **Jeffrey Sullivan**

In May 2005, a Massachusetts jury awarded Freedom Wireless US$128 million in damages, ordering Boston Communications Group to pay the award for infringing two patents owned by Freedom Wireless relating to prepaid cellular phone services. It was a verdict that provided just one more example of the many recent cases in the United States and elsewhere in which large (sometimes staggering) sums of money have changed hands due to alleged infringement of protected intellectual property rights.

In another example, in 2004 a Tennessee jury awarded a medical doctor US$110 million in compensatory damages, US$400 million in punitive damages and a 10% royalty based on Medtronic Inc's gross revenue from spinal implant devices that infringed the doctor's US patents. Medtronic's estimated total payments for its infringing activities have been estimated at over US$1 billion.

Disputes and lucrative payments for intellectual property are not limited to patented inventions. In 2003, the United States Court of Appeals for the Ninth Circuit affirmed a US$24 million judgment in favour of Tyco Electronics Corporation when it found that Bourns, an electronic components manufacturer, had misappropriated trade secrets from Tyco. More recently, in March 2005, Lexar Media was awarded more than US$380 million in monetary damages against Toshiba, based on Toshiba's alleged misappropriation of trade secrets relating to flash memory technology.

Although these and similar large awards for patent infringement and misappropriation of trade secrets came about as a result of litigation, winning or settling lawsuits is not the only means to extract value from a company's intellectual property. Consensual licensing of core technologies has also proven to be an increasingly lucrative business proposition. Acacia Research, a company that has been set up to acquire patents and collect licensing fees, reportedly earns close to US$25 million per year in royalties from its television content-blocking V-Chip patent portfolio alone.

These and other striking examples of substantial revenue generation from intellectual property have been drawn from the United States, with its huge high technology product market and litigation-friendly legal system. But intellectual property assertion and monetisation play an increasingly important role for businesses on a worldwide basis, as capitalising on intellectual property assets, whether acquired or developed in-house, has proven itself to managers as an effective method for creating revenue through litigation-based judgments, settlements or voluntary licensing agreements.

The challenge for an organisation becomes, therefore, to build an effective intellectual property protection programme such that the organisation can capture and aggressively use its intellectual property assets to create and increase value for the entire organisation.

Laying the foundation

Before an organisation can capitalise on its IP, or even develop and manage its IP assets, it must put in place a proper foundation to enable the effective development of its innovative technology. Internal practices must be put in place in order to capture the IP generated by the company's technical investment and advances. For instance, new employees should routinely be required to sign employment agreements making it clear that they are hired to invent and that the company owns any IP that the employee develops during his tenure.

While such policies will suffice to secure the company's rights in some jurisdictions, such as the US, they may not effect a surrender of all the employee's rights in other jurisdictions. The employment agreement and company policies should also outline an inventor's obligations to assign any invention to the company, as well as the employee's confidentiality obligations and use of company equipment for the sole purpose of company business. The company's policies should be available in written form and provided to new employees, and periodically distributed to existing employees.

Next come the organisation's external policies. An organisation should have a publication policy that prohibits sensitive information, such as trade secrets or patentable technology, from leaving its confidential environment without proper protection. Even if joint development agreements, consulting contracts or supplier policies are in place, the company's legal department or outside counsel should be intimately involved before proprietary technical developments or information are shared with non-employees. Such a policy should also apply to innovative information coming into an organisation from outside sources. Joint inventors of patented technology are presumed to be joint owners and thus have the full spectrum of rights to their patented technology, which includes the right to make, use, sell or offer to sell the patented invention without the consent of and without accounting to the other owners.

IP preservation practices

Once the organisation has put its IP programme foundation in place, it must establish policies to ensure that potentially valuable IP embodied in new technological developments is consistently captured and optimally protected. Implementing IP preservation practices may be as simple as providing notebooks for recording daily activity or invention disclosure forms that assist an inventor in memorialising his innovative developments. Although relatively simple to implement, such mechanisms are critical for establishing priority rights in each invention, which becomes absolutely crucial in securing patents in rapidly developing technologies in which competitors are all attempting to patent the same technology. Even if the organisation chooses to keep the innovation as a trade secret, such records can be used to prove that the company possessed the idea prior to the time that similar ideas were disclosed to the company by third parties.

These IP preservation practices can be outlined in a brochure or IP policy manual and made available to employees for review. This manual, along with training, should be presented to new employees as they join the organisation, as well as on a regular basis to existing employees. Perhaps the most effective method of ensuring employee participation in the IP programme, however, may be the use of monetary and recognition awards. These can serve as an effective catalyst for employee involvement. An IP protection programme may, conversely, be of limited value or effect if it is not prioritised by the company, or not embraced by the employees. Giving employees a stake in the programme may accomplish both goals, and make for a more effective and ultimately lucrative programme.

Because mere ideas are not patentable in themselves, the final stage of the IP preservation practice should include some form of systematic invention review in order to ensure that an idea has been fully fleshed out and reduced to practice. This requirement is satisfied only if nothing more than ordinary skill would be necessary to reduce the invention to practice, without extensive research or experimentation. The invention review process should therefore include patent counsel, inventors and management so as to ensure that the IP preservation practice captures an invention's complete embodiment, complies with the patent laws and is in line with the organisation's business objectives.

Protecting identified IP assets

Once an organisation has effectively identified its most innovative technology, what comes next? There are a number of vehicles for intellectual property protection available, and whether an organisation chooses to keep an invention as a trade secret, file a patent application or seek no protection at all for a particular piece of technology depends on the particular subject matter of the technology, the organisation's business goals and the competitive environment.

Trade secrets

Trade secret law protects technological and business secrets from misappropriation by others. The subject matter that potentially qualifies for trade secret protection is broader than that for patents and includes marketing

The other side of the coin: defending against patent trolls

Along with the increasing emphasis on IP monetisation, one of the more significant recent developments in the IP landscape has been the emergence of patent trolls, the term applied to companies that, while having no technological operations of their own, acquire and aggressively assert dubious patents against entire industries, hoping to obtain settlements based upon alleged infringers' desire to avoid the high costs and uncertainty of litigation (especially in jurisdictions, such as the US, that afford significant advantages to plaintiffs in litigation or that allow for the imposition of substantial, unrecoupable litigation costs on defendants).

Aggressive monetisation of intellectual property, while not typically a direct defence against patent trolls, may allow an organisation to offset the costs associated with patent troll-imposed costs by increasing incoming licensing revenue. Thus, when the offensive and defensive sides of an organisation's intellectual property programme are viewed from an overall budgetary standpoint, including outgoing patent troll-imposed costs and incoming licensing revenue, the company's overall intellectual property functions can serve, on an aggregate basis, as a profit centre as opposed to strictly a cost centre. In an increasingly competitive corporate world, managers who increase the number of profit centres and decrease loss-making aspects of their business will reap the rewards of such profit-oriented management, and IP departments are promising candidates for such new revenue and profit streams.

How can companies best protect themselves against the costs that patent trolls seek to impose upon them? As mentioned above, one method of indirectly protecting an organisation from these costs is to offset these costs with increased incoming licensing revenue, because typically an organisation's IP portfolio cannot be used fruitfully against a patent troll. This is so because a patent troll, in almost all cases, is usually only a holding company for patent portfolios. Patent trolls do not typically originate the patents or associated technology but instead merely buy them solely as an assertion asset. Further, patent trolls do not in most cases sell any commercial embodiment of an alleged invention and thus are immune from counter-suit for infringement (which, in traditional patent disputes between substantive technology companies, constitutes a common and effective defence against IP litigation).

Patent trolls implement a strategy aimed at maximising settlement and licensing fees from a large group of targets, while at the same time trying to limit the risk of adverse court rulings and avoiding expenses associated with litigation. But even if a patent troll litigates, it typically will not incur large discovery or other litigation expenses because trolls (as shell companies) have little documentation and no commercial operations and because they typically are represented by lawyers operating on a contingent-fee basis. Trolls implement their strategy primarily by demanding settlements proportional to the defendant's anticipated litigation costs.

Trolls thus capitalise on the uncertainty of infringement trials (including, in some jurisdictions, the possibility of huge jury verdicts or enhanced damages awards for wilful infringement) by offering potential defendants the opportunity to pay the same amount as – or slightly less than – they would pay in legal fees for litigating an infringement dispute through trial, while averting the risk of an adverse judgment. This strategy can be particularly attractive to potential defendants in the US market because, under the American Rule, by which each party bears its own litigation costs, even a defendant that prevails at trial may never recover any portion of its attorneys' fees or costs. And the downside for defendants may be much worse than simply paying unrecoupable defence costs. If a defendant loses an infringement trial, it may be required to pay actual damages, as well as attorneys' fees and costs, along with potential punitive damages if the alleged infringement was wilful.

The best (or least-worst) defence against patent trolls may be a good offence. Patent trolls tend to pursue most eagerly the easiest targets. In the US, where patent trolls have to date been the most active, easy targets have included foreign-based companies that are perceived as unlikely to resist, and foreign or domestic targets that do not have good IP awareness or strategic IP planning. Unpredictable jury verdicts, high litigation costs and the fact that patent trolls do not have commercial operations that can be the target of a counter-suit, all play to a patent troll's advantage. Patent trolls know that unprepared targets, especially non-US targets, are not accustomed to expensive discovery costs and exposure of their most confidential information, particularly when their executives and technical staff may be

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data, sales information, customer lists and innovative technology. Unlike patented subject matter, trade secrets may be protected for an indefinite period, so long as the information remains valuable and secret. Trade secret law does not, however, provide protection against persons who independently develop or reverse engineer the subject matter of the trade secret.

In choosing to pursue a trade secret strategy, the organisation must consider whether the subject matter can be detected, or independently developed, by competitors. If so, then trade secret protection may provide little, if any, protection. And if the subject matter can be independently developed and patented by another, the organisation might even be prevented from making, using or selling the subject matter that it had independently developed and kept internally as a secret.

On the other hand, the organisation must consider the product lifecycle of a given invention. A company generally cannot preclude another from making, using or selling its patented invention until a patent issues, which in some cases may take three or more years from filing to issuance. If an invention's product life cycle through the development-growth-maturity-decline stages is largely completed before the patent issues, then wading through the effort and expense needed to secure patent rights may prove to provide only an illusory benefit.

Provisional patent application

In the US, filing a provisional patent application may serve to preserve patent rights for a period of one year from the filing of the provisional application until the filing of a non-provisional, or full, patent application. Filing a provisional application may be an effective strategy if the organisation is unsure of the invention's viability in the marketplace, or if more time is needed to secure funding for manufacturing or identifying potential licensing schemes. A provisional application may then be abandoned with minimal sunk costs if the invention is not shown to be useful to the company. Alternatively, if the invention is shown to be useful, it can be converted to a non-provisional patent application within one year from its filing.

Although the filing and preparation fees for a provisional patent application are less than the fees for a non-provisional application, and the drafting of a provisional application can be relatively simple, the provisional application must still adequately describe the invention. If the invention is not sufficiently described in the provisional filing, or if new material needs to be added to the provisional specification in order to facilitate enablement, then the applicant may lose the benefit of the priority date - ie, the early filing date - of the provisional application.

Non-provisional patent application

Filing a non-provisional patent application may prove appropriate if a given technology has been developed enough to warrant patent protection to exclude others, or to generate licensing revenue. There should be a clear strategy for drafting the patent claims (which define the scope of proprietary protection) so that the proper scope of the invention is covered. Moreover, unlike a provisional application, a non-provisional application is subject to examination. The organisation should be prepared to allocate sufficient resources for the preparation and prosecution of the non-provisional patent application. Once filed, the application may still be abandoned, but considerably more money will have been invested than if a provisional application had been filed.

Seeking no IP protection

The final strategy option is the decision not to secure IP protection. A decision not to seek IP protection for an innovative idea dedicates the idea to the public. This strategy may be appropriate if patent protection is statutorily unavailable because, for example, the technology does not involve a process, machine, manufacture or composition of matter. Trade secret protection, likewise, may prove inappropriate if the subject matter is not a secret. Finally, neither trade secret nor patent protection may be appropriate if the subject matter is not relevant or helpful to furthering the organisation's business goals or has limited ability to create value for the organisation.

Managing IP once acquired

Once IP rights are secured, the organisation can begin maximising the value of its IP portfolio. In order to be most effective, an IP assertion campaign must include a willingness at least to consider bringing litigation against infringing parties. Competitive intelligence gathering is critical to the decision of whom to approach with a licence offer and whom (and when) ultimately to sue.

One method of gathering such information is through a freedom to operate (FTO) investigation. An FTO investigation determines, albeit without absolute certainty, whether the production and commercial use of an organisation's new product infringes the intellectual property rights of others. An FTO investigation not only helps to determine the organisation's risk of infringement, but also identifies likely market competitors and thus possible infringers of the organisation's own IP.

The possible infringers that have been identified from the investigation can then be prioritised according to the size of a likely royalty stream they may respectively offer, as well as the likelihood of success in securing a licensing agreement. An initial licensing offer can in turn be presented to the possible infringers, or the organisation can employ a more aggressive shoot first and ask questions later approach. The latter approach begins by filing a complaint, which may or may not be served on the targeted infringer, and then beginning the licensing negotiating process with the target.

Choosing an approach to demanding a licence will depend upon the size and strength of the possible infringer. A larger defendant with deep pockets may be more capable of paying, but also less willing voluntarily to pay a significant settlement or enter into a lucrative licensing agreement. Protracted litigation with a defendant unwilling to settle, of course, becomes more expensive, delays any potential licensing revenue and (in some jurisdictions) potentially puts the fate of a company's prospective licensing royalties in the hands of a jury. The decision to initiate litigation must be taken with care because in subsequent actions, any rulings adverse to the IP owner (as, for instance, under the legal doctrines of claim and issue preclusion) may limit the value and enforceability of the company's IP. On the other hand, securing a large judgment or settlement may make other infringers more likely to come voluntarily to the licensing table.

However, targeting a smaller defendant first may also prove advantageous to the extent that such targets may be less willing to engage in protracted litigation. Securing a number of licensing agreements with smaller infringers builds momentum, may be more effective in convincing larger infringers to enter into a licensing agreement and generates revenue that can be used to offset litigation costs incurred against larger infringers. The downside of this strategy may be that a smaller defendant may decide not to enter into a licensing agreement for the same reasons it would be unwilling to engage in litigation - lack of funds. Finally, initiating a lawsuit against a defendant that may be effectively judgment-proof would be fruitless.

The alternative, and initially less aggressive, approach to IP assertion would be to send an alleged infringer a licensing offer

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subjected to extensive depositions in which, if not properly prepared, they may make damaging admissions or errors.

By aggressively developing an IP protection programme, an organisation will understand the intricacies of its IP rights and overall technological operations, and will be prepared to take the offensive (and prepare a strong defence) when threatened with a lawsuit. Because the IP staff will have already thoroughly studied the issues relating to its own IP and technology, they will be in a better position to advise management on the strength of its position. Once a patent troll threatens litigation, filing a declaratory judgment action against the patent troll can place an organisation on a better footing, allowing it to seek a ruling of non-infringement or invalidity in a jurisdiction and venue of its choosing. Thus, even when business reasons compel making some settlement with a patent troll, a strong and detailed response to the troll's threats of litigation may facilitate a quicker and more advantageous settlement.

If nothing else, patent trolls have (quite unintentionally) done their victims the favour of graphically calling attention to the importance of IP issues and the high stakes associated therewith. Similarly, their aggressive (if amoral) exploitation of the significant substantive and procedural advantages afforded to IP owners in litigation, even when the asserted IP is of highly questionable value, should serve to encourage legitimate owners of real IP to avail themselves of these advantages in a more ambitious and active approach to IP assertion.

letter. The letter should provide as much detail as possible in order to facilitate a serious licensing negotiation. The letter, however, should avoid - if possible - the appearance of creating a legal controversy, lest the recipient file a declaratory judgment action to have the controversy resolved in court. In some jurisdictions, such as the US, a declaratory judgment is available to an alleged infringer (who becomes the plaintiff in a declaratory judgment action) if the patent owner's conduct creates a reasonable apprehension that the declaratory judgment plaintiff will face an infringement suit if it commences or continues the activities outlined in the licensing offer letter. This procedure allows the alleged infringer to select the forum and gain the upper hand in controlling the timing of the litigation process. The more aggressive approach, in which an IP owner files a lawsuit first, then negotiates a licensing arrangement, avoids the potential declaratory judgment problem.

An IP portfolio can be used not only to generate licensing fees and damages awards if infringed, but also in a cross-licensing arrangement. An organisation's patent portfolio can be compared to a competitor's portfolio to determine whether a mutually advantageous cross-licensing agreement may be reached. The process of evaluating a company's portfolio and that of its competitors provides information useful in avoiding infringement of the competitors' patents and, if cross-licensing proves possible, could round out an organisation's core technology rights. A cross-licensing arrangement could also be used as a defensive strategy when a competitor accuses an organisation of patent infringement. In closely-related industries in which rivals employ very similar technologies, it may be that competitors mutually infringe upon each other's innovations and cross-licensing may prove appropriate in order to avoid expensive tit-for-tat litigation.

Maximise value

Aggressive monetisation of intellectual property through licensing, cross-licensing or litigation can develop into a highly lucrative strategy once an organisation effectively builds and manages an IP protection programme. Affirmatively capturing and asserting intellectual property rights is inherently an offence-oriented strategy that can be used to generate a substantial IP revenue stream for an organisation.

Though implemented primarily in order to develop strategic portfolios and revenue-generation plans, an IP protection programme can also shield an organisation from possible infringement through the use of cross-licensing. Either way, a well-thought-out IP protection programme will maximise the value of an organisation's core technologies by enabling innovative ideas to be transformed into assets that can be asserted aggressively, thereby generating new sources of company income and justifying the increasing investment that companies are making in technology development and IP legal budgets. ■

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