Taking IP into the boardroom

If IP is the integral corporate asset we believe it to be, why do so few C-suite executives engage with it? Maybe it's because IP managers do not properly engage with them. At Philips, however, that is not the case. Here's why

By **Ruud Peters**

"Intellectual property is one of a company's most valuable assets." In the IP community, this statement is the equivalent of Copernicus' thesis that the earth revolves around the sun. IP-savvy managers don't need convincing of this fact. Between 70% and 80% of a company's assets are intangibles. The majority of these intangibles are IP: patents, trademarks, designs, copyrights and so on. This is the plain, simple truth.

The only trouble is, the rest of the world does not seem to take much notice. The majority of top managers do not list IP among their company's most valuable assets. If you were to bump into the CEO of your company in the corridor and talk to him or her about the essential impact of IP on the company's fortunes, the chances are you would get a puzzled look. In many companies, IP is not even a regular item on the board's agenda.

In our insistence on the importance of IP, we are a bit like Copernicus' followers in the 16th century: we know we are right, but we can't convince the powers that be of the truth. But why are we unable to get our message across? Why can't we make the board see the light? What should we do to catapult them from the 16th century into the 21st century?

Fortunately, there are exceptions to the rule. At some companies, IP managers do have access to the board. I myself have been the CEO of Philips Intellectual Property & Standards (Philips IP&S) for 10 years now. Once a year, I discuss the strategic review and my annual operating plan with Philips' board. We have quarterly meetings at which we discuss both financial and non-financial issues. If and when necessary, we set up extra meetings or conference calls to discuss hot topics. I report directly to the board every month.

In my experience, various conditions have to be in place for IP to get the attention it deserves at board level:

- First, as an IP community, we have to learn to speak the language other managers and the board understand; that is, the financial language of business.
- Second, we need to have a very close working relationship with the different product businesses within our companies, aligning our strategies with theirs.
- Finally, we need to run our own IP department as a business. This includes focusing on – and being responsive to – our clients: the product businesses within our company.

Running our IP department as a business also means that we should try to achieve ownership of all IP-related issues in the company and that we employ people with business and financial experience, as well as a technical-legal IP background.

Be warned

Before I describe these conditions in more detail, I would like to make a cautionary remark to my colleagues who are dying to have direct access to the boardroom. Of course, it is great to have that access. You can make a difference early on in the process of strategy formulation. The discussions with the board sharpen your mind, as board members tend to come up with questions you haven't thought of before. But at the same time, be careful what you wish for! Once you have access to the board, you cannot hide anymore. You are exposed; you are accountable for your results, you have to deliver, quarter after quarter, year after year. There are no more easy excuses. Having a regular relation with the board is a challenge, with all the positive and negative connotations that word implies.

A question of language

That said; let's start with the language issue. If the puzzled CEOs whom we have confronted with the statement that "IP is one of our company's most valuable assets" don't immediately try and end the conversation, they will probably answer you with something like this: "Nice try, but explain to me how these assets work for my company; how they contribute to the bottom line; how they create shareholder value."

CEOs will struggle with these questions if we haven't provided the board and the rest of the company's top managers with clear answers in a language they understand. In other words, we must always talk about IP in business terms: costs, profits, margins, value, growth, competitiveness. Otherwise, any intent to grab their attention is a non-starter. In the end, investing in IP and in IP management is worthwhile for our companies only if the value created exceeds the investment by an attractive margin. In such general business terms, this is not always easy to demonstrate, but that is our task. Therefore, we must make sure we have some good evidence – some clear, practical examples to illustrate our assertions.

Demonstrate the value

A relatively easy way to stress the value of IP is to come up with figures regarding licensing income, especially if this licensing income makes a significant contribution to the total earnings of a business unit. However, other forms of value creation through IP can be just as important. Apart from a direct cash contribution, IP can help us to increase our market share and our margins; it can also lower our costs for market access. I remember explaining to the board how, in one of our businesses, we paid far fewer royalties compared to the competition because of our own IP position. The board was very grateful for this information and immediately wondered why this business wasn't more profitable despite this IP-based cost advantage.

It can also be very enlightening to show how much a profit margin has dropped after a company's exclusivity position has deteriorated because some key patents in a product line have expired. In the pharmaceutical sector, of course, this is common knowledge. But in many other sectors, where one product such as a defibrillator may be covered by a set of patents, we have to translate the expiration of patents into business language for our colleagues to grasp its importance.

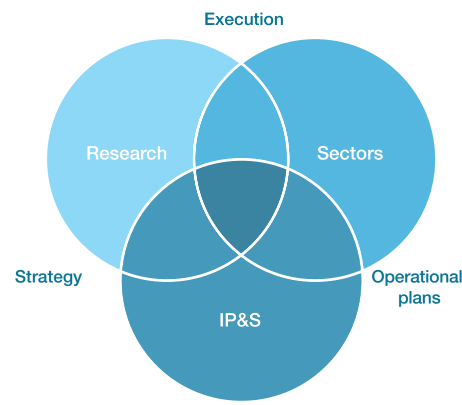
When speaking about IP-related risks, we should also learn to speak in business terms. For example, if our company is hit by a patent lawsuit and managers from the product group want to know what the risks are, it is no good talking extensively about 'first instance', 'second instance', 'Markman hearing' and the like. In the end, they will look at us and say: "So we are basically rolling the dice?" That is not an answer they like. Try to speak to them in business terms of risk: what is the possible damage to our business under different scenarios? How can we prevent or at least limit the possible damage by managing the risk? Vague, highly specialist language is not popular among managers and rightly so. They want clear, actionable assessments. That is what we should give them.

Speaking a common business language is an essential condition for a closer alignment with the different product businesses within our company. And without this alignment, it will be impossible to get the board's attention. If we can ensure that IP strategy is an integral and important part of the overall strategy of a product business, the manager of that business will also mention IP when he or she speaks to members of the board. As a result, the importance of IP will filter through to the board members. If, on the other hand, there is a gulf between the IP department and the product businesses, the product managers will never speak about IP with the board. In that case, our puzzled CEO will retort: "If IP is so important for the company, how come my board members and other top managers never talk about it?"

Strategic focus

In the IP community, it is accepted wisdom that "a business strategy without an IP strategy is no strategy". That's true, but we shouldn't forget that there is another side to the coin: an IP strategy that is not linked to the overall business

Figure 1. **Strategy alignment at Philips**



Strategy alignment with board and sectors through:

- Annual IP strategy review with board
- Participation in strategy meetings sectors
- Review of IP strategy with sector/BU/CTO management
- Quarterly meetings IP&S BG management teams and sector management teams

> “At Philips IP&S, we have one overarching mission: create IP solutions to support the growth, competitiveness and profitability of Philips’ businesses”

strategy is not much of a strategy either. At Philips IP&S, the managers who are responsible for IP in a certain product business are well connected with the businesses. At least once a quarter, my IP management teams sit down with the corresponding management teams of the business itself to talk strategy. What’s more, my managers are closely involved in the implementation of the strategy, in the discussions on how to translate the strategy into clear operational plans, defining what daily work needs to be done in the organisation. In my view, that is the only way to define and execute an IP strategy: your product businesses need to understand it, support it, be involved in it. Otherwise, it simply will not work. And of course, only if an IP strategy is intertwined with the rest of the business strategy will the board take notice.

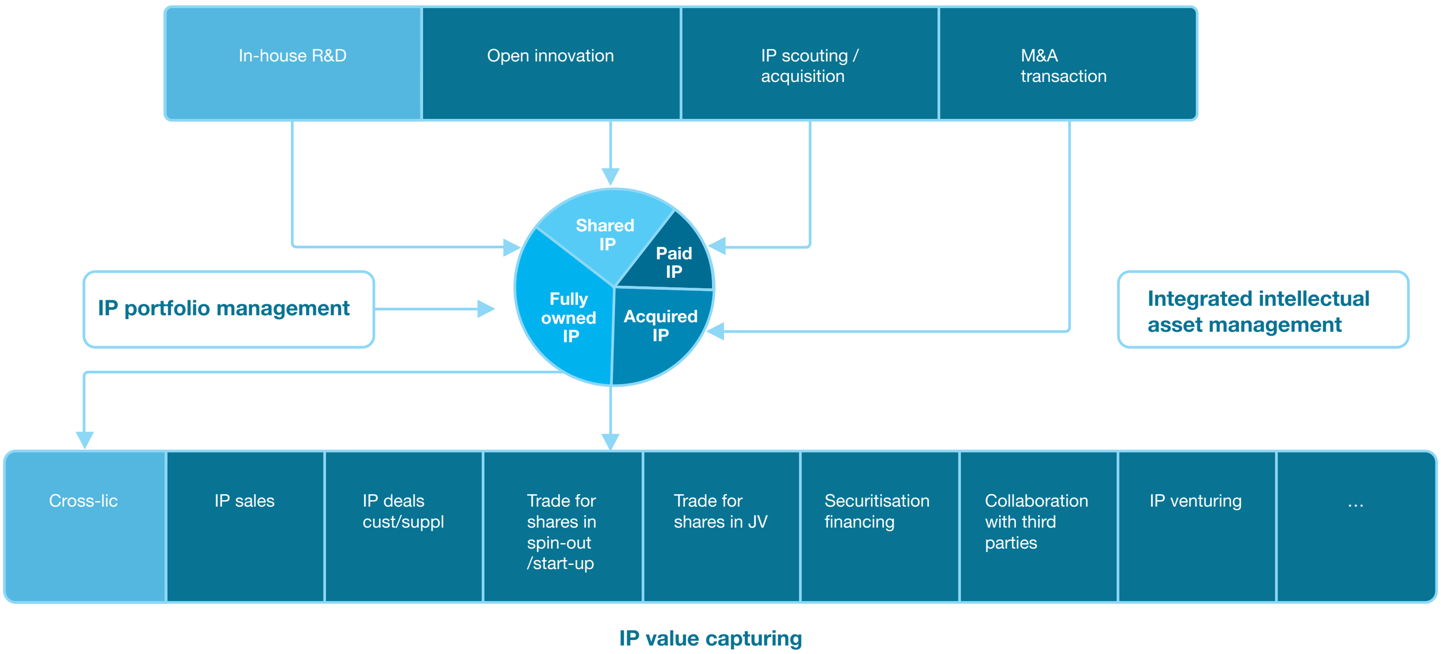
After all, IP is not a goal in itself; it is a means to strengthen the company. At Philips IP&S, we have one overarching mission: create IP solutions to support the growth, competitiveness and profitability of Philips’ businesses. This mission statement expresses the close connection between IP strategy and overall strategy.

Precisely because IP is a means and not a goal in itself, it is impossible to say what the IP strategy of Philips is. We don’t have one strategy, we have many, because we have many businesses: from medical imaging equipment and home healthcare products to LED lighting solutions and appliances such as coffee makers, shavers and electric toothbrushes. Our IP strategy for each business, therefore, depends first of all on the characteristics of that business. B-to-C or B-to-B? Growth market, mature market or shrinking market? High or low barriers to entry? Many small players or only a few big ones?

The next set of questions that will determine our IP strategy is related to Philips’ position in a market. Is our market share high or low, growing or shrinking? Is our business highly profitable or not? Do we have a strong or weak IP position in that business? Are we a technological leader or a follower? Do we want to grow, stabilise or get out of that market?

Based on the answers to these questions, we will determine our IP strategy, aligning it closely with the business strategy. We define what IP portfolio suits our strategy best. This is important: the IP portfolio should be the result of the strategy, not the other way around. Once we have defined the portfolio we need, we ask ourselves how we can achieve it: purely internal research; collaborative research in the spirit of open innovation; licensing in; buying existing portfolios based on our IP scouting; IP-based M&A activity? And then, of course, there is the question of how to create value from the IP portfolio: licensing out; a strong defence of exclusive futures of our products; input in joint ventures or start-ups; cross-licensing agreements that guarantee us room to move in an important market; and so on. There are, therefore, many ways to extract value from IP apart from monetisation through licensing. It all depends on the specific IP strategy for a specific market.

Figure 2. **Unlimited IP value capturing opportunities**



The IP landscape has evolved over recent years and now presents a company such as Philips with a variety of opportunities. No longer is it a case of only using IP created internally, instead there are multiple ways in which IP can be developed and then exploited to create value. It is the job of Philips IP&S to understand what these are and to adapt them to the needs of of the company's businesses.

Business is business

Apart from speaking the language of business and aligning our IP strategies closely with the overall business strategies within our company, we should also run our own IP department as a business in order to be taken seriously by the other businesses and by the board. Running your IP department as a business has various aspects to it – for example, customer focus. We have to look outward, not inward, when dealing with our most important customers: the product businesses within our organisation. This means that we have to offer solutions instead of just identifying IP-related problems. When a business manager comes to us with a very specific problem, we can't just say: "This is our standard solution for those sort of problems, take it or leave it." Instead, we have to customise a solution. Don't just tell them what they cannot do; tell them how to do what they can do.

Running IP as a business also means being responsive and understanding the time horizon of our clients. Often, they want a solution now, whereas the average IP organisation has a 20-year mind set. We tend to think about solutions in terms of many months or even years. If our clients want a quick solution, though, we should try to provide them with one. They see us as a black box; they don't care what we do internally to find the right solution, as long as it solves their problem. Of course, we can't change the reality of, for example, the patent system and its slow timeframe, but we should definitely try to match the business dynamics of our clients.

As a real business, an IP unit should also try to obtain full ownership of all IP issues. A good example is IP-related court cases. These should be dealt with by legal experts within the IP business, not by the legal department of the company. One of the most important things we did after I took over as CEO of Philips IP&S was to pull all IP-related activities into our organisation. Often, you can do this by proactively tackling an issue instead of doing nothing or just referring it to another unit of your company. This work never ends. For example, at IP&S we have proactively come up with a one-company solution for domain names at Philips, as an alternative to a rather scattered approach. Another example is our initiative to ensure that an IP risk assessment is part and parcel of the product creation process within the business units.

Embedding IP inside R&D and M&A decision making

In February/March 2008 (issue 28), IAM*'s cover story focused on the story of Philips IP & Standards. In this Ruud Peters explained the input that IP&S has on R&D and M&A decisions in the company. Here is an extract ...*

"We meet and then deploy R&D plans with all the company's labs," Peters explains. "We look at what they should focus on and what they should be delivering." This involves working with lab managers to use IP to identify areas in which research efforts are best directed. "We look at how we want the relevant portfolio to grow, develop the R&D strategy that will enable us to build key positions and then set targets," Peters says. Progress is monitored throughout the year.

Traditionally the IP function at Philips had merely reacted to what the labs came up with. However, the resulting portfolios of rights did not always fit in with the company's strategic plans. It became apparent that a far more effective way of operating was to define what was needed and then work towards producing that. "If you want to achieve something with a portfolio, you have to know how to build it in the first place," Peters says. "If we determine what we want, we don't end up with things that make it hard to generate value. This makes R&D much more efficient." As a result, IP&S produces highly detailed annual plans for each lab, which set out exactly what is expected. Managers are then assessed on their delivery. "If you make reaching these targets part of the requirement for the job, you drive the system," Peters says.

And the focus is not only on creating patents. With an eye to potential licensing deals further down the line, it is also essential to capture the know-how necessary to work any new invention. "When you create technology, you create know-how. When we have created products in the past it was done thinking that they would only be used by Philips. Now that is no longer the case," Peters says.

IP&S has a similarly central role in M&A negotiations. While many company IP departments continue to lobby to be in on deal discussions in their earliest days, at Philips this is already a reality. Indeed, several recent acquisitions have been driven by the IP owned by the target company. For example, in June 2007, Philips bought Color Kinetics, a leading supplier of solid state lighting and products for high-quality white light. As a result, says Peters, the company now has the strongest patent portfolio in the world in this area.

But it's not just those deals where IP is the driver that see IP&S involved from the start. "We do a lot of acquisitions and our job is to look at the company being targeted to see how well its products are protected, whether its IP position is secure in the marketplace and whether we will benefit from what it owns," says Peters. To do this effectively, he explains, it is vital to know the technology landscape, the threats that could create blockages in the future or would entail licences having to be taken – something that could destroy profit margins. "It is important for us to be in there right from the start as this means we can avoid taking corrective actions once a deal has essentially been done," Peters says.

In the old days, Peters continues, the IP team would come in much later and would have to get involved in internal and external negotiations to sort problems out as everyone involved in the transaction had effectively signed off on it. "We need to avoid those kinds of situation and instead seek to steer the deal making in line with the IP policies that we have," he says. Another benefit of having IP&S involved early, Peters adds, is that it may see ways to get a better deal for Philips. "On some transactions we have been able to use IP issues to extract a better price; while on other deals we have advised that they should not go ahead and they have been abandoned."

Hire well

Maybe the most important aspect of being a business is getting the right people into your IP organisation. For a real business-like IP outfit, it is not good enough to have highly qualified people who know all the details of technical IP issues. We also need people who understand wider business ideas, who are versed in finance and economics, who know how to value and how to extract value from IP. We need people who can handle multiple subjects. These types of people are not always easy to find; it is one of our major challenges for the future.

Our experience at Philips proves that it is possible to get the attention of the board for IP issues and to ensure that the IP business is treated as the important business it is. Speak the language that the board and other managers understand. Show the cash and non-cash value of IP in business terms. Make sure that the IP strategy is closely integrated with the strategies of the product businesses; work closely together with those businesses. Organise your own IP unit as a business unit, with customer focus, responsiveness, top-class people and the drive to achieve ownership of all IP-related issues.

If we do all that and if we are passionate as well as patient, we stand a good chance of changing the perception of IP within our company. It took many decades or even centuries for Copernicus' theory of the orbit of the earth to find general acceptance. If we take the right steps, it should not take us that long to convince the world of the value of IP assets. *iam*

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