

After its Nortel defeat, Google has no option but to look elsewhere

Losing out in the US\$4.5 billion Nortel patent auction was undoubtedly a major setback for Google. The company must now spend the money it saved on building a dynamic and strong portfolio that can protect the Android platform. The good news is that it can be done. The bad news is that cash-rich Apple will seek to make it as hard as possible

The first thing to remember about the result of the Nortel patent auction, which concluded on 30th June, is that Google really wanted to get its hands on the bankrupt company's portfolio of rights. The second is that once Apple teamed up with the existing deep-pocket members of the Rockstar Bidco consortium that became a near-impossible task. The third is that US\$4.5 billion is a huge amount of money - far more than anyone was expecting prior to the sale getting underway.

For a long time Google was the favourite to take the highly coveted Nortel prize. Its stalking horse bid of US\$900 million for the portfolio, tabled at the beginning of April, raised plenty of eyebrows itself and made clear just how serious the company was about bolstering its comparatively weak patent position. The message was a clear one: "We are not going to mess around here; anyone joining us for the June auction needs access to a large amount of money - time wasters will not be tolerated."

And so, over a period of two months, plenty of players who might have been expected to take part in the bidding decided to drop out. Eventually, in addition to Google, there were just four

parties involved: Apple; Intel; Rockstar Bidco, a consortium consisting of Microsoft, EMC, Sony, Ericsson and RIM; and Norpax, an offshoot of defensive patent aggregator RPX Corp. Notable by their absences were the likes of Intellectual Ventures, Huawei and ZTE.

Under pressure

Having gone public with its bid, however, Google also put itself under pressure. Its competitors now knew just how important the Nortel portfolio was to the company. When the auction got underway on the morning of Monday 27th June, Google was in need of a positive result. There was a sense that having made the statement, it had to deliver. But, as is now known, that did not happen. When a bid by Intel was accepted as the answering one to Google's stalking horse opening, the process got underway. After round one, parties began to pull out, then negotiations between parties took place and 18 further rounds of bidding were held (see box on page 8). The pivotal development occurred after round four, following a decision by the Rockstar Bidco consortium, to take no further part in the bidding. At that stage, Apple was granted permission from the auction organisers to talk to the consortium's members and a deal was agreed between them - the five became six. And from that moment on, despite an alliance with Intel, Google's fate was sealed.

The six companies Google was up against just had more money to call on than it and Intel did. They also knew exactly how badly Google wanted to be successful. On the basis of what hurts my enemy can only do me good, there was

no way they were going to give Google what it wanted. The task for Google therefore became one of damage limitation; in other words, to push the price up as much as possible to get it to the stage where losing out would, in the long term, be less expensive than winning. In the 19th round of bidding, Rockstar tabled an offer of US\$4.5 billion and Google decided that that point had been reached. Whether that turns out to be the case, of course, remains to be seen.

Splitting the cash

Although we do not know exactly what the Rockstar partners agreed, we do know what three of them put into the final kitty. Immediately after the auction, Ericsson announced that its share was US\$340 million; soon afterwards RIM stated that it had put in US\$770 million. Then, in mid-July, a 10-q filing from Apple revealed that it had contributed US\$2.6 billion, well over 50% of the total. That leaves US\$900 million for Microsoft, EMC and Sony to split. Whichever way they have done that, it is clear that none of them was a primary mover; it was Apple's game. Reports that for its money, Apple will get outright ownership of Nortel's long-term evolution (LTE) patents, as well as others that read on Android technology, do not seem unfeasible. What is clear is that Apple's already decent patent position is now a whole lot better.

That said, not all the patents in the Nortel portfolio were winners. Since the auction, it has been claimed that, in fact, of the 6,000-strong number of rights that were put up for sale, only 2,000 or so were patents in

force. In an email to the IAM blog, Art Monk of UBM TechInsights pointed out that if this were the case, application of the widely accepted 3% ratio - whereby just 3% of the patents in a portfolio have real value - would mean that the Rockstar Bidco consortium may only have landed 60 "real diamonds"; which equates to paying US\$75 million per patent.

However, Monk said, the price could well be worth it: "Have such diamonds been seen before and what would they look like? Yes, essential patents fall into this category and particularly in the wireless communications industry. They are called essential patents because they read on a mandatory communications standard such as, Bluetooth, UMTS, WiFi and the like. Any entity shipping products or delivering services that conform to the standard is infringing and thus needs a licence. Essential patents have superlative negotiation value between heavyweight wireless handset and infrastructure providers. Should one try to go out and buy such diamonds individually, it is not uncommon to hear numbers starting at US\$40 million and heading beyond double that for a single patent family. So, bidding for 60 such diamonds to a point where the average is US\$75M does have some rationality to it and does have a valuation tie to the market for essential patents."

Money to spend

The good news for Google is that it still has the money it did not spend on the Nortel portfolio in the bank. It also gets a few million dollars for being the stalking horse that did not win. The company will need to spend some of that cash on building a portfolio that can compete. Over the last few years it has been steadily increasing its level of activity internally - in 2010, for

continued on page 8

example, it was granted 275 patents by the US Patent and Trademark Office, compared to 141 in 2009 and just 58 in 2008. But while that is a start, it is not enough. In addition, the company is going to have to buy-in. And there may just be an opportunity to do that.

In July, the board of InterDigital announced that it “has initiated a process to explore and evaluate potential strategic alternatives for the company, which may include a sale or other transaction”. Said chairman Terry Clontz: “Over the past year we have seen the value of intellectual property rise substantially as major players in the mobile industry

increasingly understand the strategic and economic value of this type of asset. As a result, the Board believes it is an appropriate time to explore potential strategic options that may enhance shareholder value.” Indeed, just after the issue of this statement, it was reported that Google was, in fact, in exploratory discussions with InterDigital. However, it was also reported that Apple may be interested too.

And it’s not just InterDigital. The Nortel auction has alerted others as to the potential value there is in patents covering the mobile and smartphone spaces - billionaire investor Carl Icahn, for example. He has suggested that Motorola consider the sale of some of its assets in this area. If Icahn is thinking in that way,

then it is reasonable to assume that others are too. While a Motorola sale is not likely, it should not be ruled out completely. After all, deals can be structured in such a way as to ensure that the seller has continuing full and unfettered access to what it has let go.

No room for another loss

While Google may have decided that it and the Android platform can just about live with an Apple that now has control over the Nortel portfolio, it cannot afford to be so sanguine about its competitor getting hold of other significant portfolios. Android-based mobile phone manufacturer HTC has recently seen a preliminary International Trade Commission judgment go

against it in a patent infringement case that was brought by Apple. Should that decision be confirmed, Apple would be in a position to block HTC imports into the US. This has already prompted Google’s executive chairman Eric Schmidt to state that “we will make sure they don’t lose”.

Saying it, though, is rather easier than doing it. What Google needs is leverage; that means more patents. But with Apple sitting on a cash pile of over US\$75 billion, its next move is going to have to be carefully planned and conducted in top secret. One thing is absolutely sure: Google cannot afford to be outbid by its rival the next time a strong mobile telephony patent portfolio comes up for sale. ■