Context-Dependent Value

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Theory and Practice of Patent Valuation

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a thin market…

- transactions are few
- items are unique by definition
- transactions individually tailored
- validity is indeterminate
- value is context-dependent
- unstable, uncertain, risk-laden legal environment

in this environment….

- valuation is a black art
- value extraction is even blacker
- “value extraction” can undermine investments of others
- arbitrage induces maximum value extraction
  - but with heavy transaction costs
  - potential for less than zero sum game

Why must an invention be a commercially hot number to be patentable? If it is a total dud, how is the public injured by a patent on it? A monopoly on something nobody wants is pretty much of a nullity. That is one of the beauties of the patent system. The reward is measured automatically by the popularity of the contribution.

Giles S. Rich, *The Principles of Patentability*, 28 Geo. Wash. L. Rev. 393, 407 (1960), *reprinted in* John Witherspoon, ed., *Non-Obviousness: The Ultimate Condition of Patentability*, at 2:1, 8 (BNA 1980).

[B]oth researchers and companies in component industries simply ignore patents. Virtually everyone does it. They do it at all stages of endeavor. From the perspective of an outsider to the patent system, this is a remarkable fact. And yet it may be what prevents the patent system from crushing innovation in component industries like IT.

Mark Lemley, Ignoring Patents (2008)

TI has something like 8000 patents in the United States that are active patents, and for us to know what's in that portfolio, we think, is just a mind-boggling, budget-busting exercise to try to figure that out with any degree of accuracy at all.

Frederick J. Telecky, Jr., Senior Vice President and General Patent Counsel, Texas Instruments, FTC/DOJ hearings Feb 2002

some creative uses

- inhibit market entry with portfolio strategy
- ambush complex products and IT standards
- exploit imbalance in litigation resources
- instill uncertainty in competitors' customers
- settlements with NPEs that encourage pursuit of rivals
- use of portfolios to defeat exclusivity
- use of RAND licensing to extract cross-licenses
- (temporary) out of portfolios for surrogate attacks
- situational assertions (IPOs, product launches)
- "tranching" patent rights by context

context

- vulnerabilities of owner
  - patents worth more to NPE w/o offsetting liabilities
- inadvertent embedding
  - ex ante value vs hold-up value: carrot vs. stick
- number of infringers
  - free rider problem in invalidating patents
- determinacy

sources of information failure/ opacity

- indeterminacy of claims construction (esp for abstract subject matter)
- secrecy about contemplated and filed applications before publication
- amending scope after publication, especially in continuations
- tension between enabling information and disabling information
- high cost of validity and infringement opinions
- practical impossibility of clearance searching
- disincentives to invalidating low-quality patents
- limited enabling disclosure in software and business method patents
- liability for willful infringement inhibits reading patents
- “thickets” and thicket strategies
- lack of information on assignments and licenses
- settlements leave dubious patents standing and legal issues unresolved
- ambiguity surrounding obviousness

HOW TO MAKE A PATENT MARKET

*Mark A. Lemley**
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Imagine a stock market in which buyers and sellers couldn't find out the prices at which anyone else sold a share of stock. If you wanted to buy (or sell) a share of stock, you would have to guess what it was worth. The result, everyone would agree, would be massively inefficient. Willing buyers and sellers would often miss each other. The price at which a sale did close would vary widely from sale to sale. And those who had a source of private or inside information would be able to exploit others. Some trades might occur in such a system, but surely not anything like the volume in today's stock markets. Surely no one would intentionally design a system in which trades had to be "blind" in this way.

Patents, however, exist in just such a blind market. Want to know if you are getting a good deal on a patent license or technology acquisition? Too bad. Even if that patent or ones like it have been licensed dozens of times before, the terms of those licenses, including the price itself, will almost invariably be confidential. Patent owners who want to put their rights up for sale face the same problem.

The result? Willing licensors and licensees can't find each other. Patent auctions often fizzle, because without a thick market—one with an array of buyers and sellers bidding on price—no one can know whether they are getting a steal or being had. When parties do license patents, the prices are (to the extent we can tell) all over the map. And the rest of the world has no idea what those prices are. This, in turn, means that courts lack adequate benchmarks to determine a "reasonable royalty" when companies infringe patents. The lack of a real, rational market for patent licenses encourages companies to ignore patent rights

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