



The Strategic Use of Patents in the Early Stages of a Startup

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Purpose of This Workshop

- ❑ discuss patents from a *Strategic Perspective*
- ❑ describe techniques for creating value with patents
 - ✧ *particularly at an early stage*
- ❑ discuss how to “use” your patents, not just “file them away”
- ❑ discuss how to set up a “Strategic IP” entrepreneurial organization

Assumptions:

- ❑ Already know what patents are
- ❑ How they are done
- ❑ Basic knowledge of trade secrets, copyrights, trademarks, etc.



Why focus on Patents instead of other forms of IP?

- ❑ They are the most tangible form of IP.
- ❑ They are the most legally protected form of IP.
- ❑ In most industries and markets...
 - ✦ They have the greatest effect on SHV.
 - ✦ They have the greatest effect on your market success.
- ❑ Patent databases provide a powerful source of Business Intelligence.



Attitudes are changing toward Patents.

OLD THINK:

- ❑ IP is best left to patent attorneys.
- ❑ Patents are only legal instruments.
- ❑ Patents are all about suing or being sued.
- ❑ Patents are boring.
- ❑ We don't have time to do patents.

NEW THINK:

- ❑ IP has become a new corporate strategy issue for the CEO.
- ❑ Patents are strategic business tools.
- ❑ Patents open up lucrative new market opportunities.
- ❑ Patents are powerful financial assets and competitive weapons that can enhance a company's commercial success and increase SHV.
- ❑ Patenting must become a core competency.



State Street Bank

- ❑ In 1999, the US Supreme Court affirmed a lower court decision:
 - ✦ State Street Bank vs. Signature Financial Bank
- ❑ The decision affirmed that
 - ✦ Software-enabled business processes are indeed patentable.
- ❑ As with other types of patents...
 - ✦ They must be novel, useful, and non-obvious.
- ❑ Since then, there has been an explosive growth in the patenting of:
 - ✦ Business models
 - ✦ Marketing strategies
 - ✦ And other abstract innovations.

Some Famous/Infamous Patents:

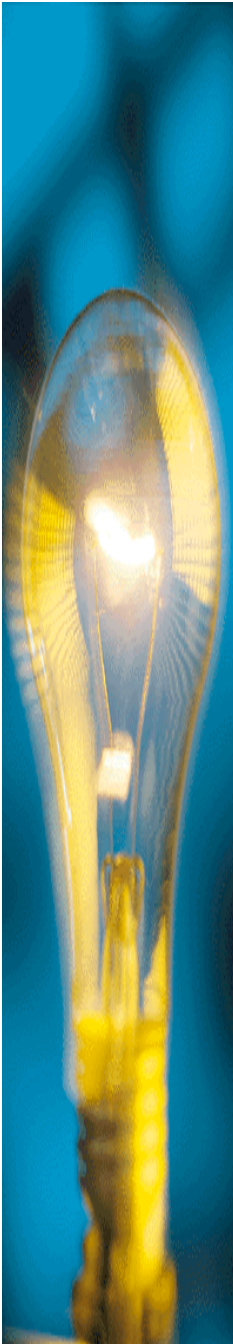
Amazon **what:** “one-click” ordering system
used against: Barnes & Noble
result: they had to go to a “two-clicks” system
charges: “a completely obvious use of cookies”

Priceline **what:** “name your own price” reverse auction
used against: Microsoft

Dell **what:** “build-to-order” business process
used against: no one yet (maybe Compaq?)

TI **what:** basic DRAM
used against: Japanese Semiconductor Mfgs.
result: kept the company alive during downturn

plus many, many more!





Greg Aharonian & Patnews

- ❑ the USPTO's loudest critic
 - ✦ (clamoring for reform)
- ❑ an independent "patent buster"
- ❑ Patnews - Greg's email-based newsletter
 - ✦ Approx 3900 subscribers (lawyers, techies, USPTO, et al)
- ❑ See www.bustpatents.com
 - ✦ It's devoted to exposing and busting bad patents.
 - ✦ Use it to learn what NOT to do!



Some Historical Perspective:

- ❑ Software patents were sharply condemned 10-15 years ago (some people still condemn them).
 - ✦ not at IBM Research, though!
- ❑ Biotech patents were condemned before that
 - ✦ around 20 years ago.
- ❑ And so were Telephony patents
 - ✦ over 130 years ago.
- ❑ Most common critique:
 - ✦ These patents will prove harmful to scientific discovery and innovation.
- ❑ Actual result:
 - ✦ Innovation and discovery has actually significantly intensified.

Q: What other type of patent is being criticized today?



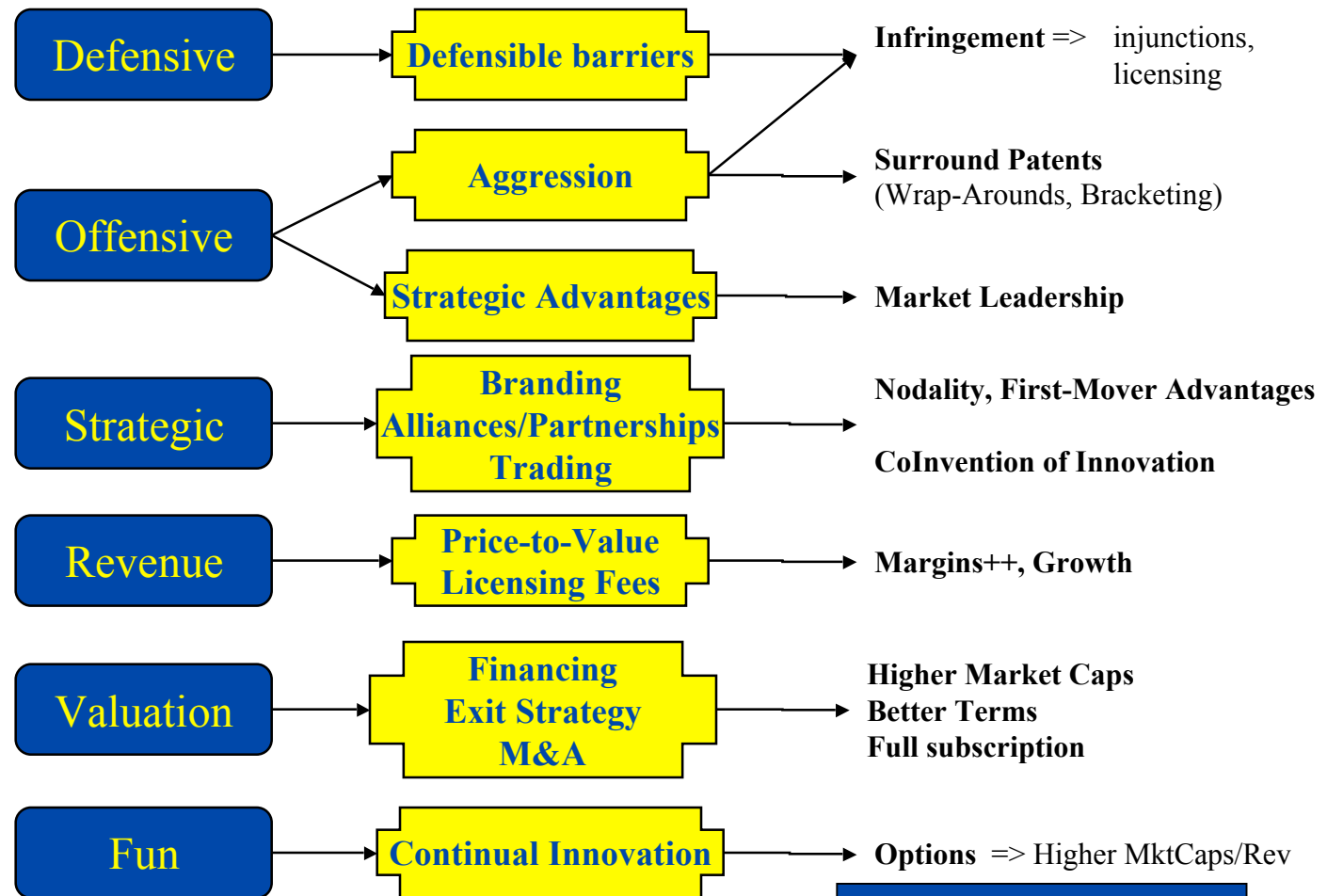
One thing is totally clear!

“Whatever changes may occur in patent law tomorrow, business method patents are an inarguable fact of life today that no company can safely ignore.”

Kevin G. Rivette

Aurigin

Why you should be eager to exploit Patents now!



Doug DeGroot

Hey, and these are just some of the possibilities!



Clustering & Bracketing

- ❑ Clustering:
 - ✦ Adding to your Core Patent (mfg, dist, mkt, etc.)
 - ✦ All possible uses, extensions, related concepts.
 - ✦ Building a patent wall around your product/model.
 - ✦ Goal: Protect your baby!

- ❑ Bracketing:
 - ✦ Doing the same thing to someone else's baby!

- ❑ Q: Why would you want to do either of these?



Usage: Valuation

- Seed Stage: Valuation can double at this stage.
- Term Sheet: Can be used to negotiate “ratchet” clauses.
- M&A: Half or more of your value will be “off balance sheet” items (“invisible capital”)
- IPO: same as above
Patents “proven out” by this time (?).
Active licensing program, kereitsu in place.
- Revenues & Margins Licensing revenues flow directly to bottom line.
Higher margins/revenue reflect directly onto higher “multiples.”
- Projected Cash Flows: *It's all about Options & Option Theory!*



Usage: Margins

Consider this classic example: IBM & Richard Thoman, CFO

Annual patent licensing royalties:

1990 - \$30 Million 2000 - \$1 Billion
a 3,300% increase

This is a recurring revenue stream!

It is basically Free Cash Flow.

It is equivalent to 1/9 of IBM's current pretax profits.

To obtain this extra margin from sales...
would require an extra sales of \$20 Billion

Q: Given that extra \$20K you have lying around,
should we expand our market reach even more
or go for some patents?



***Usage: Hostile Acquisition
Safety Net
Forcing a License***

Consider: There is some key process or technique you seriously need to maximize your success.

The owning company, however, will not license their patent to anyone at this point.

Your costs to develop a “work around” are too high.



Make patents part of your company's entrepreneurial culture.

- ❑ Develop the habit of leaving paper trails.
- ❑ It's about Business Strategy,
 - ✦ so that makes it the responsibility of the CEO and the Board (at least!)
 - ✦ Hold them responsible!
 - ✦ Add it to their Bonus & Incentive plan.
- ❑ Train employees in the patent creation process.
- ❑ Work patents into your broad-based Options Program.
- ❑ Train employees in Brainstorming, Scenario Building, Market Foresight, SHV, etc.



Where to Start?

- ❑ Start with a company IP audit.
 - ✦ Get a handle on the size and strength of your patent assets.
- ❑ Totally understand your industry's/company's supply & value chains.
 - ✦ both up-stream and down-stream.
 - ✦ understand your industry's Competitive Forces (Porter).
- ❑ Regularly brainstorm all possible workarounds
 - ✦ patent the best; disclose the rest.
- ❑ Regularly brainstorm all possible uses of your patent(s) and document (make notes, at least!)
- ❑ Acquire some expertise, if you need it.
- ❑ Develop a total IP strategy!
 - ✦ patents, copyrights, trade secrets, trade marks, etc.



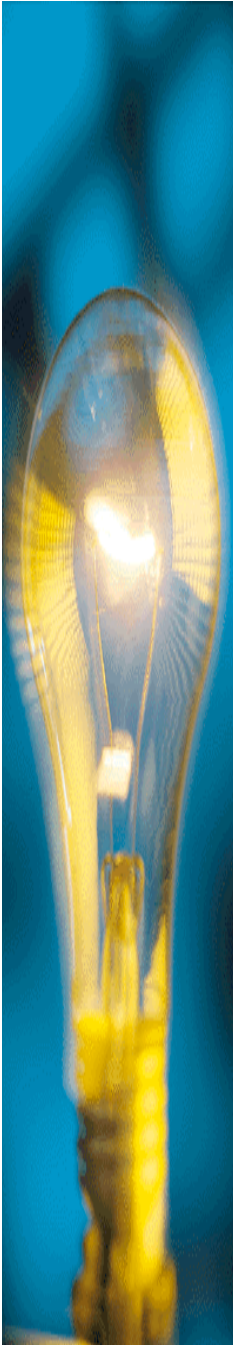
Some Problems to Beware.

- ❑ No Prior Art? *Then make some up!*
- ❑ Kitchen Sink Patents:
 - ✦ Wildly overbroad claims
 - ✦ (e.g., Sightsounds' patent claiming exclusive rights to all downloading of music/video over the net)
- ❑ Technique/Technology, but no Usage Models!
 - ✦ Just do it!
- ❑ Do **NOT** co-invent your stuff with the wrong people!
 - ✦ your Customers or Distributors, for example.
 - ✦ Listen and Suggest, but don't co-invent.
 - ✦ If they add even one little aspect, it's theirs too (cf NDAs)



Other Suggestions:

- ❑ Exploit the Provisional Filing process.
- ❑ Pursue both “first to file” & “first to invent”.
- ❑ File strategically: NL, UK, US, X?
- ❑ Prepare for business-method patents in Europe.
- ❑ Assume global value, regardless of your stage.
- ❑ Learn to exploit patent databases and IP data mining tools.



Thank you for coming.

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