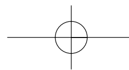

Column
IP VC

Written by
Dr Malte Köllner

Calling on old friends

There are any number of exciting IP strategies being advocated and pursued these days. Whether they can be applied to high-tech start-ups, however, is not so clear

In this column we are going to re-visit well-known types of IP strategy in order to discuss their usefulness for VC-financed high-tech start-ups.

One way of categorising IP strategies is to emphasise the difference between defensive and offensive use of rights. Personally, I have never really been able to differentiate between the two. If you sue someone for patent infringement, is that being offensive? And if you just file without litigating, is that defensive? Maybe, but it does not really make much sense. Maybe the defensive use is just a US variant (see below) that is not reasonable in Europe.

There are better categorisations at hand, so we are better off leaving that whole defensive and offensive thing behind.

The closed R&D paradigm

The traditional IP strategy triangle had three corners:

- Licensing.
- Monopoly.
- Freedom-to-operate.

Freedom-to-operate is something a European patent attorney with the European Patent Convention in mind cannot understand. Filing a patent does not give you any freedom-to-operate. Your patent and your technology might still be dependent on someone else's patents. In fact, the concept really only made sense under the old US law, where you had no prior use defence. Being one of the first inventors did not help very much if somebody else had a younger patent covering your product. In such circumstances, you could still be forced to stop production. The only defence against this was filing a patent. This would give you prior and thus better rights than the other party. And this would support your freedom-to-operate. In Europe, however, you always had the prior use defence. So there never was this need to file patents in order to increase your freedom-to-operate.

So, let's look at licensing or monopoly.

It is *à-la-mode* to be for open licensing and a free exchange of R&D results; and the open R&D paradigm certainly has some very good justifications. But do these also apply to VC-financed high-tech start-ups?

If you freely give a licence at moderate terms to everybody, what are the consequences? Well, there are a lot of competitors offering your technology on the market. This will not change after a potential trade sale. Therefore, buying you is not very interesting. Taking a cheap licence like anybody else is all that is necessary. After all, taking a licence is much cheaper than buying the whole ... bakery.

It may be different if, like Qualcomm, for example, you have a world standard. Then, you can license everybody and generate a lot of cash. But what do you want in such a situation? Do you want to be bought? Probably not, you want an IPO. IPOs, however, remain the exception. Trade sales and liquidations are the rule.

Thus, monopoly is your best choice.

Stick or carrot?

As we have decided to prefer monopoly to licensing, we do not really have to worry which category of licensing strategy we are going to choose. However, there may be business models in which licensing is worthwhile pursuing. So let's stay on this subject for a moment.

Generally, two main strategies are put forward with regard to licensing: stick licensing and carrot licensing. The latter involves you showing your potential business partners the wonderful carrot, symbolising you brilliant technology, with the hope that they will get an appetite for what is on offer. The former, on the other hand, means you try to catch them red-handed and then take a stick in order to beat the cash out of them. Experience shows that, in general, stick licensing is more successful than carrot licensing. I cannot see any reason why this should not be true for high-tech start-ups.

So, if your business model requires a licensing strategy, you should do whatever you can to increase your turnover. And if that involves a stick, then so be it.

The pyramid

Now let's turn to the well-known pyramid of IP strategies, from top to bottom: visionary/strategic; profit centre; cost control; and defensive. What do the terms mean?

- "Defensive" means you just protect your products by applying for patents, eg, the US way.
- Cost control means you start a programme of portfolio management to optimise cost savings and maximise the effectiveness of your patents.
- Profit centre means you try to refinance your IP expenditures directly through licensing. Not always an easy task.
- Visionary/strategic means you create IP actively in areas where it could have the highest impact.

And given all this, where would you reasonably situate a VC-financed start-up?

- Visionary, of course! Otherwise it would not have received VC investment in the first place, stupid. Well, erm, maybe this is a little bit too simple.
- Strategic? You better be! Like everybody else. Otherwise you have made a mistake.
- Profit centre? This might be difficult for a start-up with only a handful of patents, which is looking for its first few clients. Still, you would be happy if it turns out to be feasible.
- Cost control? Probably yes, although, when in doubt, you file a patent or uphold it, since patents are valuable assets when it comes to financing rounds and company valuation.
- "Defensive"? Sure. As explained above, you want the monopoly.

So, basically, the well-known IP strategy pyramid does not help a VC-financed high-tech start-up very much in designing its IP strategy. The pyramid is more of a model for larger enterprises.

So, what have we learned? To be honest, the IP strategy of VC-financed high-tech start-ups is very old-fashioned.

***Dr Malte Köllner** is a patent attorney and a partner of Triangle Venture capital Group, Germany*
m.koellner@triangle-venture.com