

CHAPTER 5

Preparing for the Valuation

Before launching into a detailed valuation exercise, a valuator should do a fair amount of preparatory work. This work involves analyzing the legal rights that make up the patent being valued. As we explained in Chapter 2, patents are a multifaceted property interest that involves a complex bundle of legal rights. Understanding which rights are involved with a particular patent and how those rights are to be employed is crucial to understanding what value can be generated from the patent. Immediately launching into some form of income, market, or cost method of valuation analysis without first considering the following fundamental questions will almost certainly lead to an inaccurate valuation or incomplete analysis:

1. What exactly is being valued: the use of the invention, the patent rights, or both?
2. What are the specific legal characteristics of the patent rights being valued?
3. How will the patent rights be used?

We addressed the first question (does the valuation cover the use of the invention, the patent rights, or both) in Chapter 1. This chapter covers the remaining two questions.

In this chapter, we

- Explain how the bundle of rights that come with a patent affect its value.
- Explore the alternative uses that can be made of a patent because different usages can generate very different values for a patent.

UNDERSTANDING THE BUNDLE OF LEGAL RIGHTS

The work required to value a patent bears many resemblances to the work that should go into any type of property valuation. Take, for example, a

classic real estate appraisal. Most real estate appraisal checklists will remind the appraiser to determine the following:

- What is the ownership interest that is being valued?
- What is the description of the property being valued?
- Are there any encumbrances on the property rights?
- What are the characteristics of the neighborhood surrounding the property?

For patents, a similar exercise needs to be done. Although the questions are formulated slightly differently than for real estate and the focus of the inquiries is largely about understanding a complex web of legal rights, the essence of the exercise is the same. Box 5.1 provides a comparison of the standard real estate appraisal preliminary work questions and the corresponding analysis that is required for a patent valuation. This chapter examines each of these patent-valuation preliminary questions and explains how to incorporate such information into a patent-rights valuation analysis.

BOX 5.1: SIMILARITIES BETWEEN THE PRELIMINARY WORK REQUIRED FOR A REAL ESTATE APPRAISAL AND THAT REQUIRED FOR A PATENT VALUATION

Real Estate Appraisal	Patent Valuation
Ownership interest in the property	
1. Does the “owner” possess valid title to the property? ✓ Can the chain of title be established?	1. Does the “owner” possess a valid interest in the patent? ✓ Is the patent still in force? ✓ Are there any potential invalidity challenges, such as obviousness, lack of novelty, enablement of best mode defects, or filing errors?
2. What type of property ownership does the party have? ✓ Is the interest fee simple (absolute title to and possession of the land)? ✓ Is the interest leased fee (a third party has a lease right to the property)? ✓ Is the interest a leasehold estate (it is the lessee’s interest in the property that is being valued)?	✓ What is the remaining life of the patent? ✓ Can the chain of title be established?

3. Is there any co-ownership of the property?

2. What type of patent ownership does the party have?

✓ Does the party own the patent? If yes, is the patent subject to any existing license agreements?

✓ Is the party the licensee? If yes, is the license exclusive or nonexclusive?

3. Are there any joint owners?

✓ Are necessary assignments properly completed?

Description of the property

1. What is the description of the real property?

✓ What are the property's boundaries (e.g., what are the property's metes and bounds)?

✓ What does the property include within its boundaries?

1. What is the description of the patent rights?

✓ What are the "claims" for the patent?

Encumbrances on the property rights

1. Are there any liens against the property?

2. Are there any restrictions on the owner's right to exclude?

✓ Are there any easements?

1. Are there any liens against the patent?

2. Are there any restrictions on the patent owner's right to exclude?

✓ Did the government fund the research for the invention?

✓ Are there any "shop rights"?

✓ Are there any compulsory license requirements?

Understanding the neighborhood

1. How do neighboring pieces of property affect the value of the property?

1. How do neighboring patent rights affect the value of the patent?

✓ Are there blocking patents?

✓ Are there synergistic patents?

OWNERSHIP INTEREST IN THE PATENT

As with real estate valuations, questions about the ownership interest in a patent involve three issues. It is necessary to determine whether the

owner possesses a valid interest in the patent, what the type of ownership is, and if there are any joint owners.

Does the "Owner" Possess a Valid Interest in the Patent?

There is no point in valuing a patent unless a valid ownership interest in the patent can be established. Is the patent still in force? Are there any potential invalidity challenges to the patent? What is the remaining life of the patent? Can a chain of title be established to show that the current holder of the patent rights has proper title to those rights?

Is the Patent Still in Force?

One of the first inquiries that a valuator should undertake is to determine whether the relevant patent is still in force. Just because a patent was granted does not mean that it remains in force. The simplest way for a patent to lose force is failure to pay the required maintenance fees (also referred to as renewal fees or patent annuities). The economic premise behind maintenance fees is to discourage the maintenance of dormant and low-value patents. If the patent is not worth paying the maintenance fee, which is typically not very high, the patent holder will abandon the patent and allow the knowledge covered by the patent to enter the public domain. Most developed countries have some type of maintenance fee system.

In the United States, maintenance fees are required for utility patents, but not for design and plant patents (see Chapter 2 for a discussion of the different types of U.S. patents). Maintenance fees for utility patents must be paid to the U.S. Patent and Trademark Office (PTO) within 3¹/₂, 7¹/₂, and 11¹/₂ years from the date that the patent was granted¹ (see Table 5.1). U.S. patent law allows for a 6-month grace period for paying a maintenance fee, although a late payment surcharge is then added to the maintenance fee.² If the maintenance fee and surcharge (if applicable) have not been paid by the expiration of the grace period, the patent will expire at the end of that grace period.³ If a patent has expired due to failure to pay maintenance fees, limited options do exist to revive the patent.⁴ A maintenance fee analysis should be done for each country or jurisdiction covered by the patent right that is being valued.

Potential Invalidity Throughout the world, a large number of patents are incorrectly granted by patent examiners each year. These patents should have been denied, for example, because the invention was obvious or lacked novelty, the inventor did not satisfy the enablement or best

TABLE 5.1 U.S. Patent Maintenance Fees for Utility Patents

Due Date (Measured from Grant Date)	Maintenance Fee		Grace Period	Grace Period Surcharge		Expiration Date (Measured from Grant Date)
	Standard	Small Entity		Standard	Small Entity	
3½ years	\$1,130	\$ 565	6 months	\$150	\$75	4 years
7½ years	\$2,850	\$1,425	6 months	\$150	\$75	8 years
11½ years	\$4,730	\$2,365	6 months	\$150	\$75	12 years

Source: U.S. Patent and Trademark Office.

mode requirement, or the patent application was not filed within the 1-year grace period (see Chapter 2 for a discussion of the requirements for a valid patent). Although granted patents are presumed to be valid,⁵ these incorrectly granted patents risk invalidity challenges from third parties that may decide to

- Request a reexamination of the patent, which could result in the patent being limited or declared invalid.
- Infringe the patented technology and seek to limit or invalidate the patent at trial if challenged.

When valuing a patent right, the valuator should have an understanding of the patent's reexamination and litigation history. If the presumed value of the patent right is sufficiently high, it may be worthwhile to conduct a prior art search to estimate the probability that a subsequent infringement case will be brought and the probability that such a case would be successful.

Remaining Life of the Patent If the patent remains in force, the valuator should determine its remaining life. For most of its history, the United States measured its patent terms from the date the patent was issued. That changed, however, in 1995. For patents filed after June 8, 1995, the potential duration for a patent is 20 years from the date the patent application was filed. For patents in force on, or issued on applications filed by, June 8, 1995, the potential duration for the patent is the greater of 20 years from the date of filing or 17 years from the date the patent was granted. For patent rights that involve foreign patent protection, a review of the relevant duration law for each country or jurisdiction covered by the patent right should be conducted.

The remaining life of the patent places a quasi cap on the premium pricing that may flow from a patent's exclusivity rights. Alternative

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