



## CET WORKING DOCUMENT

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### EXECUTIVE SUMMARY

Traditionally, patent assets and the corresponding rights have changed hands either as part of a larger transaction or through specific and direct agreements related to those rights. Recently however, the transfer of patent rights from one entity to another has evolved to include patent auctions.

Patent auctions, like other auctions, allow a seller to list a patent asset as a “lot”, which can be bid on by prospective buyers. Currently, there are two types of patent auctions, live auctions and online auctions. Despite some early criticisms, it appears that significant purchases have already been made.

The emergence of patent and other IP auctions introduces several issues for the profession to consider, issues such as the need to caution clients about due diligence, the ability to demonstrate the potential value of IP, the opportunity to recover costs, and that over time such

auctions may provide useful information for conducting IP valuations.

There are also various interesting ethical considerations for practitioners related to conflicts of interest, giving advice regarding the value of an IP asset, and whether a duty of candour exists for practitioners that possess information relevant to the validity of a patent at auction.



## PATENT AUCTIONS

Traditionally, patent assets and the corresponding rights have changed hands either as part of a larger transaction or through specific and direct agreements related to those rights. This approach is typically transparent to both sides and involves a great deal of due diligence and negotiation, often over a significant period of time. Recently however, the transfer of patent rights from one entity to another has evolved to include a less transparent and faster approach: the patent auction.

Patent auctions, like other auctions, allow a seller to list a patent asset as a “lot”, which can be bid on by prospective buyers. Similar to a traditional sale of patent rights, the lot typically includes the rights to a family of patents and/or patent applications. Currently, there are two types of patent auctions, live auctions and online auctions. As the name suggests, live patent auctions are live events. Live patent auctions are time constrained and are limited to a collection of in-person and possibly a few remote bidders. On the other hand, online patent auctions are virtual events that transpire over a relatively longer period of time and are open to any potential bidder with access to the auction’s website.

This paper will provide an overview of the two auction types mentioned above, followed by a brief discussion of the observed realities and potential issues surrounding patent auctions.

Existing patent auctions are modeled after English-style auctions: participants openly bid against one another, with each subsequent bid being higher than the previous bid. Live patent auctions use a human auctioneer to control the bidding at a physical location. During live patent auctions, bidders may call out their own bids, have a proxy bid for them or may even place bids remotely.

Over the last few years, Ocean Tomo Auctions, LLC, a subsidiary of Ocean Tomo, LLC, has held a live IP auction in Chicago each fall as well as spring auctions in locations such as San Francisco, Amsterdam and London. These IP auctions accept submissions not only for patents but also trademarks, copyrights and domain names. The following discussion will focus on patent auctions. The patent auctions are held during a portion of an IP conference, the lots are published in advance, and attendees must register to attend. Any patent that is up for bid has been screened by Ocean Tomo using a proprietary patent rating system. To preserve anonymity, bidders are not required to wear name tags, they can simply use paddles or even place bids over the telephone.

Currently, Ocean Tomo live patent auctions are technology agnostic and thus bidders expecting to bid on, e.g. a pharmaceutical patent, will also witness the bidding on patents related to other technologies, e.g., a software patent. Practically speaking, this does not seem to pose much of a problem since the infectious urgency of sale, often termed “auction fever”, provides an atmosphere that can itself be entertaining. For lots that are not sold to a

winning bidder (i.e. do not meet the minimum acceptable bid or “reserve amount”), Ocean Tomo enables sellers to connect with the bidders post-auction for subsequent negotiations.

To attend a live auction, you can register as a bidder or as a non-bidder: bidders pay a higher registration fee than non-bidders. To list a patent, a seller must enter into a seller consignment contract with the auctioneer. For example, the seller pays 1,000 USD per single patent listing at the minimum reserve (currently 10,000 USD) or 3,000 USD per single patent listing with a consignor-specified reserve amount. To list groups of patents or “patent pools”, the seller pays 3,000 USD at the minimum reserve amount and 6,000 USD at a consignor-specified reserve amount. Auctioneers such as Ocean Tomo distribute an auction catalogue prior to the event which, for each lot, lists the patent numbers, assignees, brief descriptions of the property being sold, forward citations for the patents and any additional information provided by the seller. The forward citations identify assignees of patents which have referenced the listed patent. The auctioneer also provides an expected value for the lot, which is determined using their patent rating system. For example, at the recent Amsterdam live auction, a patent for: “A Scalable Transaction System for a Network Environment”; was given an expected value of 600,000 USD. To provide some context, this patent eventually sold at the event for almost two thirds of the expected value – at just over 380,000 USD.

Consistent with traditional auction practice, the seller will receive 85% of the final bid price while the bidder will pay a 10% buyer’s premium. For example, for a patent that sells for 100,000 USD, the seller will receive 85,000 USD and the bidder will pay 110,000 USD. According to Ocean Tomo, they have consistently had over 350 attendees at each of their live IP auctions<sup>1</sup>. How successful the auctions have been depends on who you ask. To put things into perspective, at the recent live auction in Amsterdam in June 2008, 29 of 60 lots sold at an average sale price of almost 450,000 USD with the highest sale being almost 2,500,000 USD – for a patent related to digital media technology<sup>2</sup>.

Although not required, it can be expected that buyers would perform some form of due diligence beforehand. Aside from the information provided in the catalogue, Ocean Tomo also provides, through an independent third party, an online secure data room for qualified bidders that gives them access to detailed information provided by the seller regarding the IP. Bidders are also given the option of arranging private due diligence meetings with the seller prior to the event as well as during the event. To protect anonymity, conference calls between sellers and prospective buyers can be arranged through the auctioneer. In addition to these available options, the mere fact that the lots are published prior to the event allows bidders to take all necessary steps to perform as thorough a due diligence as they would for any transaction.

Despite facilitating due diligence before and during the live auction, Ocean Tomo does not appear to require that sellers post anything to the online secure data room or to even provide a minimum amount of information – the buyer is ultimately responsible for conducting a satisfactory due diligence. Moreover, although the auctioneer screens the patents prior to the

auction, there is no associated guarantee of validity or enforceability. Ocean Tomo does however provide patent valuations as a separate service using their patent rating system. The cost of conducting such a valuation is likely no easier to predict than the cost of conducting a thorough due diligence.

Online patent auctions are virtual events hosted by an entity through a website, similar to other online auction sites such as eBay™. Rather than being constrained to a relatively short, live event, most online auctions allow a seller to select the length of the bidding window, e.g. 1 day, 1 week, 2 weeks, etc. Although this may mitigate the auction fever when compared to a live patent auction (an advantage for the buyer), it opens up the bidding to more prospective buyers anywhere in the world (an advantage for the seller). One example of an online patent auction site is Free Patent Auction ([www.freepatentauction.com](http://www.freepatentauction.com)). Free Patent Auction is a non-commercial, not-for-profit organization providing a completely free service to both buyers and sellers. This service is non-exclusive, meaning that sellers can promote and sell their patents outside of the service. Free Patent Auction does not assist in the negotiation or actual transaction or any due diligence, they simply provide a forum for sellers and buyers to connect.

Listing a patent online is relatively simple. The seller registers for the service, uploads information regarding the listing, sets a price and sets a duration for the listing. Reserve prices can be set, the patent can be categorized according to technology, and various other options are available. The categorization of the listings allows potential buyers to focus in on technologies that are of interest. The details provided by the seller can also be edited during the listing period and the online forum allows buyers to contact sellers for more information. Furthermore, by virtue of being listed online, the patent listing can show up in search engine results and can reach buyers around the world at any time of the day. To preserve anonymity, user IDs can be selected accordingly.

When compared to live patent auctions, online patent auctions are less expensive and seemingly more flexible, they do not seem to create the same level of auction fever as a live patent auction, and there is the risk that a listing can go unnoticed. The services provided through a live auction and the credibility that the attendees can bring to the atmosphere seem to provide an intangible advantage to the live auction approach. However, the simplicity and low overhead associated with an online auction allows even small businesses and individual inventors to test the waters before committing any significant cost to the sale of their IP.

On the face of it, a patent auction would seem to be a hasty alternative to a traditionally rigorous patent selling process. However, there are several interesting elements of the patent auction that may explain why patent auctions seem to be finding their place in the world of IP transactions.

One advantage of a patent auction is the anonymity it can provide, which is typically

unavailable when transacting directly. From the seller's perspective, the anonymity enables one to gauge the market's reaction without revealing who the seller is. From the buyer's perspective, the anonymity enables the buyer to make a serious attempt at bolstering their patent portfolio without giving the perception that there is a hole in their portfolio or an urgent need to address freedom to operate or infringement issues.

Patent auctions also provide an organized forum that allows both big and small players to participate together. For individual inventors and small businesses, this may be the only feasible way to monetize their patent assets or offload patent maintenance costs. Given that online patent auctions are typically free, for some there may be nothing to lose. As online patent auctions gain credibility they may even begin to find favour in the same way eBay™ has become a mainstay and, as a result, more sophisticated services may emerge. Could we eventually see patent "want ads" in the future?

Patent auctions are not without criticisms or limitations.

There is the public policy issue of whether patent auctions give easier access to patent trolls. However, Ocean Tomo reports that only one – "maybe two" lawsuits have emerged from patents sold at one of their live patent auctions<sup>3</sup>. Nevertheless, the long term effects of a more fluid exchange of patent rights remains to be seen.

Aside from the excitement that auction fever can create at a live patent auction, the effect of auction fever has been blamed for driving up the price and causing hasty decisions<sup>4</sup>. This would certainly not be a downside for the seller but could leave buyers unsatisfied when the excitement wears off.

Some of the live patent auction events have been criticized for providing much fanfare but few buyers<sup>5</sup>. Given that 29 lots sold in Amsterdam, it is possible that such criticisms are premature. Live patent auctions have also been criticized for not following a theme causing many potential buyers to wait through many, what are to them, irrelevant lots<sup>5</sup>. This is a relatively minor problem that will likely be addressed in time as the popularity of the live patent auction grows.

Despite these criticisms, there seems to be much optimism about this relatively new process and, given the apparent success of the recent live auctions and the potential for the "big sale", we can likely expect patent auctions to become more common in the future.

The emergence of patent and other IP auctions introduces several issues for the profession to consider:

- 1) Clients interested in this process should be cautioned that they are largely responsible for conducting their own due diligence.
- 2) An auction can be useful in demonstrating the potential value of IP assets.

- 3) An auction can provide an opportunity to recover costs associated with obtaining IP rights.
- 4) Looking forward, the results of auctions (e.g. sale prices), may provide useful information for conducting IP valuations.

The above also raises interesting ethical questions for practitioners:

- 1) Given that the buyer is meant to be anonymous, does acting for a seller at an auction raise any conflict of interest issues for the practitioner, in particular if the practitioner eventually learns that they also act for the buyer?
- 2) Are practitioners qualified to give advice to clients regarding the value of IP assets?
- 3) Is there a duty of candour for practitioners to disclose information relevant to the validity of a patent being auctioned? (e.g. where new prior art is uncovered in a corresponding application)

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1 [http://www.oceantomo.com/auctions\\_FAQ.html](http://www.oceantomo.com/auctions_FAQ.html)

2 [http://www.oceantomo.com/press/Amsterdam\\_Post\\_Release\\_6.30.08.pdf](http://www.oceantomo.com/press/Amsterdam_Post_Release_6.30.08.pdf)

3 Kanellos, Michael; "Inventors Look for Cash, Recognition at patent auction"; April 2, 2008; CNET News; accessed at [http://news.cnet.com/8301-10784\\_3-9909524-7.html](http://news.cnet.com/8301-10784_3-9909524-7.html)

4 Gibbs, Andy; "The Cure for Patent Auction Fever"; ipFrontline.com; March 14, 2006; accessed at <http://www.ipfrontline.com/depts/article.asp?id=9901&deptid=3>

5 Kanellos, Michael; "Few Buyers at Patent Auction"; April 6, 2006; CNET News; accessed at [http://news.cnet.com/Few-buyers-at-patent-auction/2100-1014\\_3-6058737.html](http://news.cnet.com/Few-buyers-at-patent-auction/2100-1014_3-6058737.html)