WHY INTELLECTUAL PROPERTY MATTERS

Intellectual property is not a legal backwater best left by CEOs to their lawyers at a big outside law firm. It is at the core of what drives businesses and many other types of organizations forward. Every institution holds intellectual property of varying degrees of importance to the fulfillment of its mission. It’s what an organization’s community knows in the aggregate and what its people can do. Intellectual property is often a key driver of new business lines. It can also be a driver of revenues, both directly and indirectly, in the form of free cash flow. And it can be a creative way to build new connections to your customers, patrons, business partners, and prospects.

Two recent stories—each from a different field of business, and both true—illustrate why you should care about your intellectual property strategy.
The Smartphone

Let’s say you want to develop a new smartphone to compete with Apple’s blockbuster iPhone. You know, off the bat, that there are thousands of patents standing between you and the launch of your new smartphone. In intellectual property lawyer speak, you may hear someone tell you that there are thousands of patents that “read” on the phone you are proposing to build.

Samsung had such a plan in mind a few years ago. It set about to develop a new, competitive smartphone to take back some of the market share claimed by the likes of Apple. But as Samsung found, a semiconductor company called InterDigital, based in King of Prussia, Pennsylvania, had a series of patents based on innovations over several decades. After a long-running and distracting patent-infringement fight, in January 2009, Samsung agreed to pay InterDigital $400 million over four years. Nokia was already on the hook for a $253 million payment to InterDigital. (Set aside for the moment the hard problem of whether InterDigital’s work constituted real innovation or the operations of a “patent troll,” also known as “non-practicing entities”—a method of merely holding up companies from obtaining licenses—as some allege.)

So why wasn’t this a problem for Apple, the maker of the iPhone? Or for Research in Motion (RIM), which makes the BlackBerry? Neither of these giants of the smartphone
industry ran into this same trouble in court, at least on this score. The reason is that they both had negotiated licenses up front with InterDigital. The InterDigital intellectual property was already part of their portfolio—their “bundle of rights”—when they went to market with their product.²

Perhaps Samsung will end up passing Apple and RIM in the smartphone business. (They have some promising smartphones on the market that run Google’s Android system, which is fast gaining a market share as of 2011.) And perhaps the InterDigital licensing matter had little to do with the outcome, in which Apple and RIM have been thriving, and Samsung has struggled to succeed in the US market. No matter what, Samsung lost time, focus, and money as a result of getting tangled with InterDigital.

The lesson: like it or not, the intellectual property that other organizations have amassed matters a great deal in terms of enabling you to pursue your emerging business goals. Like it or not, you have to accept that the rights of other organizations will set the playing field—and may affect the ultimate outcome of the game.

As in the case of Apple and RIM, it will pay off to do your homework first and initiate your business plan grounded in a keen assessment of the risks that lie around you in the intellectual property ecosystem. You may decide to run certain risks and plow ahead as planned, or you may pause to consider alternate means of proceeding. At a minimum,
your strong understanding of the intellectual property landscape will surely help to decide how much to invest in the business line, how to assess its prospects, and the range of possible outcomes.

**The Lovable Character**

The Children’s Television Workshop (CTW) launched *Sesame Street* in 1969. In developing the concept, it consulted pediatricians, psychologists, and educators of many stripes. It came up with a hit television series. Along the way, it dreamed up a series of characters to teach children through educational television. Through the characters and the creativity of the programming, the CTW managed to develop a strong connection with the kids who tuned in to its shows.

One of the characters, Elmo, struck a particular chord with children. Elmo is usually up to something interesting—though tame, of course—and carries it out in a sweet, bumbling manner. It’s not clear if Elmo is a boy or girl. Young children just learning to speak and interact with the world—ages two or three, especially—relate to Elmo in an uncanny way. It is hard to describe the connection that kids feel toward Elmo. But as many parents know, it can be extremely strong.
The CTW was founded to create educational television shows, not to manufacture products. It’s also a nonprofit. But that has not stopped it from making a great deal of money from the relationship that Elmo has with fans. For more than a decade, the CTW has been licensing certain trademark rights and copyrights that it holds in Elmo—all with friends Big Bird, Grover, and others—to for-profit organizations. It has set out to create and exploit a licensing market for their characters not just in the United States but also around the world. And they’ve been exceptionally successful in this regard.

Now picture yourself, as a parent, walking down the juice aisle in the supermarket. Your three-year-old is in the child seat of the shopping cart. You reach for the lowest-priced apple juice, and just then, your child notices Elmo on a smaller, pricier bottle. After a brief, intense negotiation, you switch apple juices. You end up buying the more expensive bottle. You pay more for less in the way of apple juice, but avoid a major public battle with your little one. The net effect of this everyday story is that millions of dollars flow to the CTW and higher profits accrue to the manufacturers that take out a license to use Elmo’s image on consumer-facing food products.

There’s another benefit that is important to mention at this stage. It’s possible that the CTW would have gone down the road of licensing the use of its characters purely
for the money. But it’s gotten another benefit from this strategy: much greater reach for its characters and ideas. Through these deals, other people pay the CTW for the right to spread the word about its characters. So long as the CTW makes good choices about its partnerships, the net effect of licensing is not just money but also greater value in the brand itself (up to a point) and more kids coming back to watch the programs that feature the characters. A sound licensing strategy drives both parts of the CTW’s double bottom line.

One might tell a similar story about Dora the Explorer, owned by Viacom, the parent of Nickelodeon and Nick Jr., because the tweens and teens segment is particularly hot today. Disney’s High School Musical, for instance, is considered an especially desirable brand to license. Or Disney’s hit princess characters—based, by the way, not on characters that Disney’s on-staff “creatives” dreamed up but instead on popular stories long in the public domain, such as Snow White and Beauty and the Beast. Both Viacom and Disney are profiting handsomely from the sales of their hit characters and entertainment properties. While Viacom doesn’t have the same public-interested mission that the CTW does, the effective licensing of Dora materials contributes to the likelihood that a child will visit Dora’s Web site or look for her shows in the on-demand section of their cable offerings, which drives a virtuous cycle.
These stories each make a slightly different point about the importance of intellectual property to your organization. The first is about the significance of obtaining and using patent rights, with a proactive rather than reactive mind-set. It’s clear that one would rather be Apple or InterDigital than Samsung or Nokia. The second narrative, about trademark and copyright interests, demonstrates how the educators and producers behind *Sesame Street* have created an extraordinary public service enterprise, and have additionally fueled it with character-related, cash-producing marketing as well as free exposure for their brands. In each of these cases, smart intellectual property strategy has led to big returns for the organizations that have leveraged the intangible but highly valuable knowledge-based assets of their organizations.

**What Is Intellectual Property, Exactly?**

What can you protect through intellectual property rights? Generally, original ideas, expressive works, and the words and images (and even sounds and colors) that describe brands can be protected through intellectual property systems. For example, a novel method of manufacturing something can be patented through the US Patent and Trademark Office and its counterparts around the world. The process often takes several years to obtain an issued
patent, but you can frequently produce benefits for your organization even through the act of filing a patent application. (In some cases, business methods can be patented too, though current trends in the law point toward greater and greater difficulty in patenting such processes.)

When you come up with a new logo or brand for your service or product, you can register that “mark”—a trademark or service mark—at the state and federal levels in the United States as well as other jurisdictions around the world where you plan to do business. The same goes for copyrighting a new song, book, movie script, or the like.

It is worth pausing for a moment to acknowledge that we’re in the midst of a major, multiyear political dispute about intellectual property. Though not the primary topic of this book, there’s a vibrant discussion in the United States and other countries about whether intellectual property rights have grown too much over the past two hundred years. For instance, the extension of the copyright term in 1998—the Sonny Bono Copyright Term Extension Act—tacked on twenty years to the length of time that a copyright holder has to enjoy their exclusive rights, now for a period measured by their lifetime plus seventy years—gave rise to a US Supreme Court challenge. The challengers, led by law professor Lawrence Lessig, made a forceful argument against copyright term extension, but came up short by a vote of seven to two. The efforts of the Recording Industry Association of America to enforce the copyright
interests of its members, the music recording labels, has prompted a backlash among customers and a movement called “Free Culture” on college campuses. The debates over patent reform are just as robust. The largest of the questions are: How and when do intellectual property rights inhibit or stimulate innovation, and how can we optimize the system from a public policy vantage point? These are important political discussions, and it would be smart to be aware of and perhaps participate in them as they develop further. (A few of the books, blogs, and other Web sites in the reading list at the end of this book cover these debates along with the related intellectual property issues. I say a bit more on this front in chapter 9.)

For my purposes here, let’s take the intellectual property regime as it is. My premise is to consider together what you might do, as a company, within the legal and business framework of intellectual property as it exists today. In the best intellectual property strategies, you will anticipate and benefit from future trends as well.

The process of acquiring intellectual property begins with an analysis of how best to go about it. Before you can enter a new market or launch a new product, not only do you need to have a thorough knowledge of your business ecosystem; you also have to come up with the human and financial capital to make it successful. You hire a team and convince someone—your board, a bank, a customer, or an angel investor—to put up the capital that you know is
needed to fund the necessary work. Now is also the right time, at the beginning of the product development or expansion cycle, to think about your intellectual property business strategy.

An individual or members of a team sometimes develop intellectual property within a single organization. Some of the money to be made in intellectual property is in the ability to exploit this information and know-how within your own organization. Think of the Samsung example. Your organization may hold smartphone-related patents, based on your own innovation, which create the freedom of action to develop the smartphone that you have in mind. These patents might also serve as a bargaining chip for a cross-license with a competitor, where you agree to license your rights to them in exchange for a license back to you associated with your rights. Or it might be that you simply have to pay up front for a license, as Apple and RIM presumably did, to build your smartphone. The same might be true if you intend to enter a new market with an existing product, where a competitor has rights in a given country that you seek to enter, since intellectual property rights tend not to be global in nature, unless you invest heavily from the start in obtaining worldwide protections. You would also need to consider, in turn, whether to protect your new innovations as you develop the phone, through both patent and trade secret protection, to stop others in remote jurisdictions from copying your product
and flooding the international market with lower-cost imitation goods.

A similar analysis would help you to determine whether you could use a given name to describe your new service. You’ll need to choose the brand name carefully, for two reasons. First, you’ll be investing a lot in marketing that brand, so you want it to be defensible against others using it in the future. Just as important, you want to avoid someone coming after you for infringing on their right to use a given name in commerce to describe a service—or be prepared to switch to marketing using a new name. You might want to check how your proposed brand name translates into other languages, like the classic example of the Chevy Nova in the Spanish language, which meant “no go.” In the digital age, this analysis would extend also to the domain name space, where a search will help determine what domain names you will be able to claim for your product or service. Many organizations will register domain names similar to their own name in order to prevent others from doing so once there’s value in the brand—a practice known as “cybersquatting” or “typo-squatting.”

This analysis will take you down the road of considering whether to apply for a trademark or service mark, and at what level. It can get expensive to file, maintain, and monitor intellectual property protections in multiple jurisdictions over time—but it can also lead to enormous opportunities in future licensing or other business revenue.
For instance, in a future joint venture or acquisition scenario, the fact that you have perfected your rights in a leading brand might lead to a premium paid by the other side in the deal.

You might consider, instead, whether to license a brand name from someone else in order to help you sell more units or service plans. Perhaps the phone you have in mind is not a full-function smartphone but rather a plastic non-working phone marketed to small children. You will need to stamp a picture of the most popular character for the moment, whether it is Dora the Explorer or Elmo, on the toy to convince kids to pester their parents into buying it. In either of these cases, you’d need a license from the owner of the relevant intellectual property rights to market your plastic phone.

This same intellectual property analysis plays out in a wide range of industries before a product or service can be released for sale or otherwise offered to the public. In the movie business, lawyers and their teams obtain copyright clearance from many different people to put out a feature film; in turn, the movie itself may enable the creators to count on revenues for years to come from licensing aspects of the film. Think of Star Wars, for example, and the long tail of revenue that has been generated for the owners of that intellectual property well after the movies have stopped running in the theaters. The same is true for some musical productions and sound recordings, books, and vir-
tually every complex creative endeavor. It’s also the case for nonprofit producers of documentary films, like Boston’s WGBH, the producer of the award-winning Frontline program, among many others.

In each of these instances, the first premise is that you need to acquire the rights to certain intellectual property in order to reap benefits from them later on. In establishing your rights clearly, you create the freedom of action for your organization to enter into new markets with new products. A wide and deep intellectual property portfolio on your balance sheet means you’ll have broader freedom of action without new outlays of capital. Whether or not you have to go into the marketplace to buttress the rights that you have, you will need a fairly sophisticated cost-benefit analysis to determine whether and how much to invest on the front end in intellectual property protection or licenses from others. The intellectual property licensing business is big business, with good reason. There’s even another layer of the business: insurance and financing issues related to the acquisition and management of intellectual property rights as it becomes clearer that they represent an important asset class.

Just as it is about creating freedom of action to operate and generating revenues, your intellectual property strategy is also about risk reduction. If you are launching a serious new start-up, you wouldn’t think of using a do-it-yourself kit from the Internet to form a new corporation if
you have big plans. The money spent on lawyers to create a new corporation and divide up the equity is a worthwhile investment against problems down the road. As your company grows, spending money on lawyers to structure equity agreements for new employees and plan for defenses in takeover scenarios is likewise a good investment. The same logic applies when it comes to building an intellectual property portfolio, which can emerge as a key aspect of your overall equity in the business. Each of these investments in lawyers—setting up a company, planning for smooth and continuous operations, and establishing an intellectual property portfolio—functions as a crucial insurance policy for your organization as it grows.

Investments in your intellectual property portfolio reduce risk by establishing greater clarity around what you can do as an organization without violating the rights of others, even in an unintentional way. By amassing intellectual property rights, and registering or publishing information about these assets—whether in ideas, forms of expression, or brands—you establish and retain for your organization the ability to do more or less whatever you like with those rights later. That might mean exploiting them on your own, licensing some or all of those rights to others, or giving the rights freely away to others. Put another way, these investments ensure, first and foremost, that your organization has freedom of action later. As just one example, the documents that you painstakingly get every new employee to
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sign—inventor’s rights agreements, say—ensure that the work you are paying for redounds to the benefit of your organization, not the start-up that your employee leaves to join. These investments in work related to intellectual property reduce risks that are almost certain to arise in future years while your intellectual property rights are still under the protection of the government-mandated limits on what others can do with them. Even in a nonprofit setting like a university, it can be important to ensure that your employees have signed over some or all of the rights in what they produce to you, unless for some reason you want them to retain those rights.

Up-front investments in intellectual property also can reduce the risk and cost of litigation. In the intellectual property field, litigation is incredibly expensive. Virtually everyone (other than the intellectual property litigators and certain organizations whose business purpose it is to sue others) wishes to avoid intellectual property litigation. The costs of lawsuits are enormously high—let alone the possible costs of negative publicity and the distraction caused by extended litigation. A bill for $3 to $5 million in legal fees per side in a medium-sized matter is common. The possibility of damages—which can reach into the hundreds of millions or even billions of dollars—can easily justify the expenses on the plaintiff’s side, and can likewise provide a strong incentive to defendants to negotiate a settlement to avoid a costly courtroom battle. It’s not much
of a reach to speculate, for example, that Google’s large settlement with Yahoo! early in Google’s rise to prominence—in which Google transferred about $328 million in stock to Yahoo!—was a function of Google’s recognition that the damages could be immense—and Google’s own growth stunted—if Yahoo! were to have prevailed.⁷

It should come as no surprise that having certainty in intellectual property rights can lead to earlier and cheaper settlements. Control of intellectual property rights of your own can sometimes even preclude such action in the first place. In cases where both parties know the strength of the other party’s rights, the total cost of the transaction—in lawyer’s fees and other direct expenses—will likely be lower. The investment that you (and your competitors) make in clearly establishing your intellectual property rights may keep down your lawyer’s fees and other costs associated with uncertainty down the road.

Establishing an Intellectual Property Strategy

As a CEO or senior manager of any sort of organization, you should establish a dynamic intellectual property strategy. The strategy needs to be explicit, such that day-to-day decisions can be evaluated against it and so that the decisions drive toward helping you make the right institutional goals. Too much decision making related to intellectual
property is made randomly or in a way that is isolated from the whole. This strategy needs to be dynamic so that you are adjusting it over time to take full advantage of the field’s fast-changing circumstances, opportunities, and risks. The strategy needs to be nuanced. It has to be tailored to specific types of assets and not a one-size-fits-all formula.

In establishing and implementing such a strategy, consider four core recommendations. First, treat intellectual property as a flexible asset class and manage it accordingly—even when precise valuation is uncertain. Second, be open to ways of using outside intellectual property that was not developed within your organization (in ways that are perfectly legal, of course). Third, consider the primary use of intellectual property as ensuring your own freedom of action to compete effectively, rather than an offensive weapon. And last, establish a mechanism within your organization that guarantees that you remain flexible and develop the capacity for creative foresight with respect to intellectual property strategy over time.

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