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RPX CEO AIMS TO MAKE PATENT MARKET COST EFFICIENT

BY DAN LONKEVICH

John Amster, the co-founder and CEO of RPX Corp., is trying to take some of the emotional sting out of patent disputes.

No one likes to be sued or extorted as many technology companies claim to have been by the so-called patent trolls over the past six years.

The number of trolls — or "non-practicing entities," to use the less charged language favored by Amster — have risen to more than 900 at the end of 2013 from 546 in 2008 and 251 in 2005.

The NPEs counter that they are just representing the legitimate interests of companies and inventors who have been cheated or whose property has been infringed by larger technology companies.

RPX has positioned itself between the technology companies and the NPEs, characterizing itself as a "defensive" patent aggregator and a provider of patent-infringement loss control services.

"We're not philosophically opposed to patent monetization," Amster said in an interview from a conference room in RPX's headquarters in San Francisco. "We do think there's a right way and a wrong way to do it. We focus on the substance, the business model and the tactics."

However, some critics say that RPX is part of the patent troll problem.

"The best argument people come up with against us is that we promote paying for patents," Amster said. "Our point is you're already paying for them now with the high cost of litigation and you're paying more than you should."

According to a report produced by RPX, NPEs sued more than 2,600 different companies in 2013 and filed 3,608 infringement cases, up from 3,042 in 2012. This resulted in 4,843 total defendants, which was 13% more than in 2012.

NPEs filed 63% of new patent litigation cases, the fourth consecutive year they accounted for more than half of filers.

Overall, plaintiffs filed a record 5,411 patent infringement cases in 2013, up 15% from 2012 and more than double since 2009, representing an annualized increase of 19%.

An NPE is an entity that purchases portfolios of patents with no intention of developing products or services, using the patents instead to make infringement claims against other companies.

RPX also acquires patents for its subscribers without the intention of ever developing them. However, the company has never brought a single infringement suit.

Amster said the patent trolls are not going away even after the Supreme Court's recent rulings that they could face legal costs for frivolous cases. He said the rulings in Octane v. ICON and Highmark v. Allcare and legislation being written on Capitol Hill are unlikely to have much impact because frivolous cases represent a small portion of dollars spent on litigation.

Patents "are a valid and well established right with real value," Amster said.

The problem is less about the trolls and more about how patents are valued and how disputes about value are handled, which is through the courts, he said. "No other industry tolerates such cost inefficiency."

Amster co-founded RPX in 2008 with Geoffrey Barker, who is an executive director and former COO.

Eran Zur was also a co-founder of RPX and served as president from 2008 to 2012. He currently is managing director and head of the intellectual property finance group at Fortress Investment Group LLC.

Prior to that, Amster was general manager of strategic acquisitions at Intellectual Ventures Management LLC. Patent investment firm Intellectual Ventures, headed by former Microsoft Corp. chief technology officer Nathan Myhrvold, has been accused itself of being a patent troll.

Before joining Intellectual Ventures, Amster was managing director and founder of the mergers and acquisitions practice at Ocean Tomo LLC, a Chicago-based investment bank that specializes in intellectual property.

He began his career as an attorney with the law firm of Weil Gotschal & Manges LLP, where he worked on M&A, equity investments, venture capital, IP licensing and patent litigation.

Amster is working to make RPX a source of information and data on specific patents, NPEs, technology companies and law firms to help clients make business decisions about patents. He said he wants RPX to be "the Bloomberg of patents."

That's consistent with Amster's stated belief that patent holders' real enemy is not the patent troll, but the process by which patent disputes are resolved. The information that is critical to that process is opaque and controlled by a few.

"For whatever reason, patents are an area in which legal analysis gets a very high degree of deference in an organization," Amster said. "It requires a high degree of legal analysis for every decision. We're not sure that should always be the case."

While most patent infringement cases involve what he called "bespoke legal analysis," Amster said RPX believes companies could benefit from an analysis of data on previous cases.

"That's a very foreign concept to the patent world because it is so legal focused," he said. "Whenever a company is sued for infringement, it has a tendency to see it as a clean slate. We say you shouldn't see it that way. That should seem obvious to a CFO, but a lot of them don't feel qualified to opine on patent issues. It's an interesting phenomenon on which the c-suite should be focused."

According to RPX, about 43% of the $13 billion spent in 2013 on patent infringement cases went for legal fees.

Some operators of NPEs agree that those are large numbers.

"There's a huge vested interest in this not becoming an efficient market and it's coming mainly from the legal community," said Erich Spangenberg, the founder and CEO of IPNav, the most active non-practicing entity in the market in 2011 and 2012, according to RPX data.

"The legal system is not suitable for solving the inefficiencies of the patent market," he said.

At Dallas-based IPNav, Spangenberg has often found himself on the opposing side of patent infringement cases from RPX. He says he has developed respect for what the company is trying to accomplish.

Spangenberg said he doesn't currently own any stock in RPX, although he has been both short and long in the stock over the years.

The inefficiency of the patent market "is begging for a solution and it can't come from legislation because legislation often hurts as much as it helps," Spangenberg said.

"The genius of RPX and the reason it's going to change the market is you finally have one company that has all the data," he said.

Spangenberg said that "RPX will probably become the clearinghouse for the patent market," something other companies have tried and failed to do.

Indeed, Spangenberg said Ocean Tomo, Intellectual Property Exchange International Inc. in Chicago and Intellectual Property Exchange Pte., which was formed in connection with the Singapore government, all failed to catch on because they lacked data.

"RPX just has a huge advantage over all these efforts — data," Spangenberg said in an e-mail. "The information they have amassed and continue to amass allow RPX to do things the rest of the players can't do."

Members of the patent bar agree that the intellectual property market is inefficient. However, they place the blame not on legal fees but on unreasonable expectations from litigants and defenders.

"It's not a perfect market," said Gregory Lippetz, a partner with Jones Day in Palo Alto, Calif. "Lots of plaintiffs bring suits with unrealistic expectations of value. And defendants sometimes say, 'We will not pay one cent unless the patent is fundamental.' It skews predictability."

Even so, Lippetz said "there's clearly a market need" for what RPX provides. "What portion of the market will capture that need, I just don't know."

Chandran Iyer, a partner with Sughrue Mion PLLC in Washington, said RPX delivers a valuable service to its clients, some of whom are also clients of Sughrue Mion.

"If Google, HTC and Apple get sued, instead of each of them paying the patent owner, they can pay a membership fee to RPX that's less than what they'd pay, and RPX works out a licensing arrangement," he said. "They're, in effect, a bundler."

However, “you need patent trolls to have a company like RPX,” Iyer said. “It’s a symbiotic relationship.”

Amster stressed that RPX’s business model isn’t trying to put NPEs out of business, just the ones that file frivolous and abusive lawsuits.

But even for the non-abusive NPEs, RPX is hoping to make the process less profitable.

The patent market had worked well enough until some disruptive NPEs upset long-held expectations, Amster said.

For example, he said that, for years, the best defense against an infringement claim was a counter claim for infringement of a different patent. That strategy was thought to lead to compromise between two companies developing patents. It doesn’t work, however, against an NPE which has no interest in developing patents.

Spangenberg said that he doesn’t fear the impact RPX’s business model will have on IPNav’s business, even though it is one of the most active patent monetizers in the market. IPNav owns several thousand patents and was the most active litigator the market in 2011 and 2012. It has since modified that strategy to put less focus on volume and more on the quality or value of the patents, Spangenberg said.

Asked what he thinks of being derided as a troll, Spangenberg said, “I embraced it long ago, thinking eventually it will become meaningless.

“It happens any time there’s something transformative in the market,” he said. “It’s nothing new, just people who haven’t studied history.”

RPX may be showing people the benefit of studying patent history. As of March 31, it had acquired more than 4,300 patent assets in the open market. The asset purchases represent some 1,800 avoided litigations to its clients, the company says. RPX also successfully negotiated more than 500 litigation dismissals from more than 60 litigations.

Amster said RPX looks at about 800 patent portfolios a year and spends more than $100 million a year on purchases. In total, it’s purchased more than $810 million since the company was formed in 2008.

RPX collects more than $240 million a year in subscription fees from its 178 clients who are some of the same telecom, media and technology companies that decry trolls. RPX uses those fees to purchase patents and license them to its members. The asset purchases also give RPX a unique way to gauge the value of patents based on new and past settlements of similar patents.

This also allows RPX to assist its clients in settling patent litigation by analyzing past settlements for similar patents to reveal average settlement amounts for each NPE.

In addition to buying patents, RPX also represents groups or syndicates of companies, who want to team up to buy portfolios of patents.

RPX spent some $46 million in 2012 to buy a portfolio of patents from an NPE established by Altitude Capital Partners and its manager Rob Kramer, a former managing director at Fortress Investment Group LLC.

Before RPX bought out Kramer and Altitude, they had generated more than $700 million of licensing revenue from an aggressive strategy.

RPX and its clients received the ownership rights to more than 500 patents in the U.S. and 50 more outside the U.S. that had been held by Digitude Innovations LLC, an Altitude portfolio company, and certain sub-license rights to patents licensed exclusively to Preservation Technologies LLC, a unit of Digitude.

The RPX group also won the dismissal of 22 lawsuits in which 10 RPX clients were defendants, and restrictive covenants that prevented Kramer and Altitude from licensing patents against the RPX client network for an extended period of time.

Arguably, RPX and its clients could have saved considerable expense had they purchased the portfolio before Kramer was able to do so. Indeed, they might have prevented the $750 million in licensing fees Kramer won.

Nevertheless, they’re willingness to buy him out when they did most likely allowed them to save considerable money that would have been paid out in the future.

This loss mitigation strategy stands in sharp contrast to the argument of some technology owners, who avoid compromise with NPEs.

Such a fight-hard strategy allowed Newegg Inc. to win a five-year legal battle with the NPE Sovereign Software LLC, shielding the web-based electronics dealer from a potential $20 million to $25 million payout.

Amster said that while Newegg and its general counsel Lee Cheng deserve credit for the victory and the deterring effect it may have against future claims, the strategy is not always wise nor without risks.

RPX estimates that Newegg spent more than $3.5 million fighting Sovereign, which is considerably more than the amounts other Sovereign defendants paid to settle such claims.

Newegg's Cheng didn't respond to a request for comment.

Earlier this year, RPX announced a new patent infringement liability insurance product underwritten by a syndicate at Lloyd's of London. It also formed a new reinsurance company called RPX Reinsurance LLC and a new underwriting, marketing and claim manager called RPX Insurance Services LLC.

The effort is being led by Rob Kingsley, who joined RPX in 2011 and previously led several insurance companies and agencies.

RPX is focusing the insurance product on the some-10,000 companies who have rarely or never been sued by an NPE and as a result don't see the value in being a full-fledged member of RPX, which can cost more than $1 million a year.

The liability insurance covers up to $10 million in infringement claims made during a policy year. The policies carry significant retentions of $25,000 and above and cost from $150,000 to $250,000 a year.

Amster said during a conference call about the company's first-quarter earnings that it has sold infringement liability insurance to 31 policyholders, including some who were already subscribers.

RPX reported net income of $9.86 million, or 18 cents a share, for the first quarter, down from $14.7 million, or 28 cents a share, in the same period a year ago. Revenue rose 1.1% to $61.9 million.

The company posted net income of $40.8 million, or 76 cents a share, for all of 2013, up from $39 million, or 74 cents a share, in 2012. Annual revenue rose 20.1% to $237.5 million.

Net acquisitions during the year totaled $126.5 million.

Shares of RPX, which trade on the Nasdaq Global Select Market under the symbol RPXC, were worth $16.08 as of Friday, giving the company a market value of $852.4 million.

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