

***On February 5, 2013, Dell announced that Michael Dell and Silverlake Partners were planning to take the company private at \$13.65 a share.<sup>1</sup> Their proposed price could undervalue the company and possibly diminish the interest of current Dell shareholders. Dell's second largest investor, Southeastern Asset Management (Southeastern), publicly opposes the transaction. It released a sum-of-the-parts analysis of Dell's share price. Southeastern came to the conclusion that a more appropriate share price would be 75% larger than Michael Dell estimated.<sup>2</sup> Unfortunately, even Southeastern did not adequately consider Dell's intellectual property (IP) optionality in its analysis.***

Until the last few years, markets did not give much consideration to the value of IP when determining enterprise value or monetization options. More recently, IP has become a hot topic due to a series of high profile transactions. A startling wake-up call occurred during the bankruptcy of Nortel Networks. Prior to Nortel's collapse, the value of its IP portfolio received little attention from market analysts. During its bankruptcy in 2011, the IP portfolio sold for \$4.5 billion dollars, which accounted for over 80% of the creditors' recovery.<sup>3</sup> In addition, Alcatel-Lucent is attempting to use its famous Bell Labs IP portfolio as collateral for \$2.1 billion in financing.<sup>4</sup> These events are not anomalies but signals which indicate a growing market realization that IP controls and protects the marginal cash flows of businesses.

The case with Dell is no different. Dell is moving out of the PC manufacturing market and into information technology (IT) service markets. Investors need to know that Dell has a strong IP portfolio in these new markets and therefore has the capacity to control marginal cash flows in these sectors. However, since Dell is not currently exercising these controls, they are missing a large opportunity to harvest value for their shareholders. Dell has the opportunity to transact using these market controls and create more value for its shareholders if it so chooses.

Dell's transition to an IT services company has not been easy and its market cap has suffered as a result. Contributing to these difficulties, Dell has failed to execute a meaningful IP monetization strategy to support this transition beyond the strategy to cross-license with industry partners. Dell's 2012 SEC 10-K filing describes a minimalist strategy: *"While we use our patented inventions and also license them to others, we are not substantially dependent on any single patent or group of related patents. We have entered into a variety of intellectual property licensing and cross-licensing agreements...We anticipate that our worldwide patent portfolio will be of value in negotiating intellectual property rights with others in the industry."*<sup>5</sup> **Dell has failed to recognize the value of its own assets which control marginal cash flows in several unexamined market segments.** These market segments are in innovation spaces where Dell wants to grow and become a bigger player. Does Dell truly not know it has strong market controls in its new business segments? Or is Michael Dell fully aware of these assets and is perhaps waiting to competitively transact in these spaces once the privatization plan is successful? Investors deserve to have clarity on these points.

This week, Carl Icahn stepped on the scene and acquired a 6% stake in Dell. On March 5, 2013, Icahn sent a letter to Dell's Board of Directors to state his opposition to the buyout and propose an alternative plan similar to the one proposed by Southeastern.<sup>6</sup> Between himself, Southeastern, Yacktman Asset Management, and T. Rowe Price, 20% of Dell's equity shareholders are openly opposing the buyout for undervaluing the company. Yet even their estimates of the full value of Dell fall short of the accretive cash flows available to harvest if they are not accounting for the IP.

<sup>1</sup> <http://www.sec.gov/Archives/edgar/data/826083/000119312513041273/d480506d8k.htm>

<sup>2</sup> [http://www.sec.gov/Archives/edgar/data/807985/000094787113000078/ss164605\\_sc13d.htm](http://www.sec.gov/Archives/edgar/data/807985/000094787113000078/ss164605_sc13d.htm)

<sup>3</sup> <http://www.guardian.co.uk/technology/2011/jul/01/nortel-patents-sold-apple-sony-microsoft>

<sup>4</sup> <http://www.m-cam.com/sites/www.m-cam.com/files/P-PO-ALU%20Financing.pdf>

<sup>5</sup> <http://www.sec.gov/Archives/edgar/data/826083/000082608312000006/dell10k020312.htm>

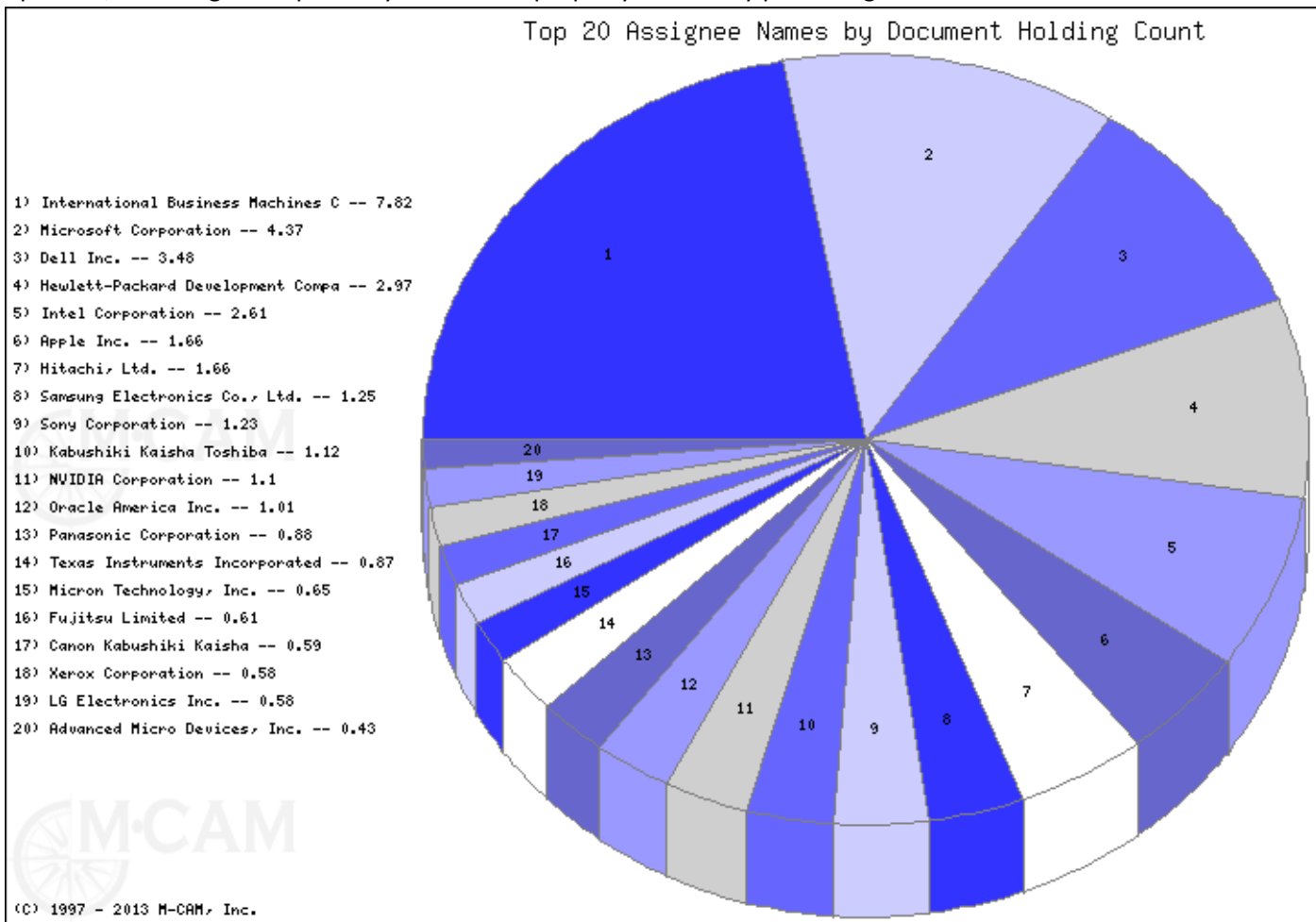
## Dell's Commercial Fitness

Dell stated in its SEC filings last year that it has 3,449 patents and an additional 1,660 patent applications pending.<sup>7</sup> To make a determination about commercial fitness, we assessed Dell's IP portfolio and commercially scored its contents using the M•CAM proprietary unstructured data mining algorithms. This assessment measured the commercial strength and transferability of each patent. Commercial patents are linked directly with cash flows and may have a basis for licensing. Non-commercial patents have little chance of being licensed, lack market relevance, or are direct liabilities to the holder due to prosecution impairments.

Overall 47% of Dell's IP portfolio scored as commercial versus 53% being non-commercial. While this may seem poor to the casual observer, in comparison to the portfolio assessments of other multinational corporations, Dell's portfolio scores better than most. Of the 47% which have commercial opportunities, we have divided the portfolio into 17 separate technical categories. Of these 17 categories, four segments were found to have higher than a 50% 'commercial' score. These categories included Graphics Processing, Data Transfer, Networks, and Switches. Since these are areas where Dell has its strongest market controls, they represent greater optionality for Dell to generate cash flows.

## Innovation Spaces

Below is an exemplary graphical display of the entities in the innovation space surrounding the Graphics Processing patents, revealing the top twenty intellectual property holders by percentage of volume.

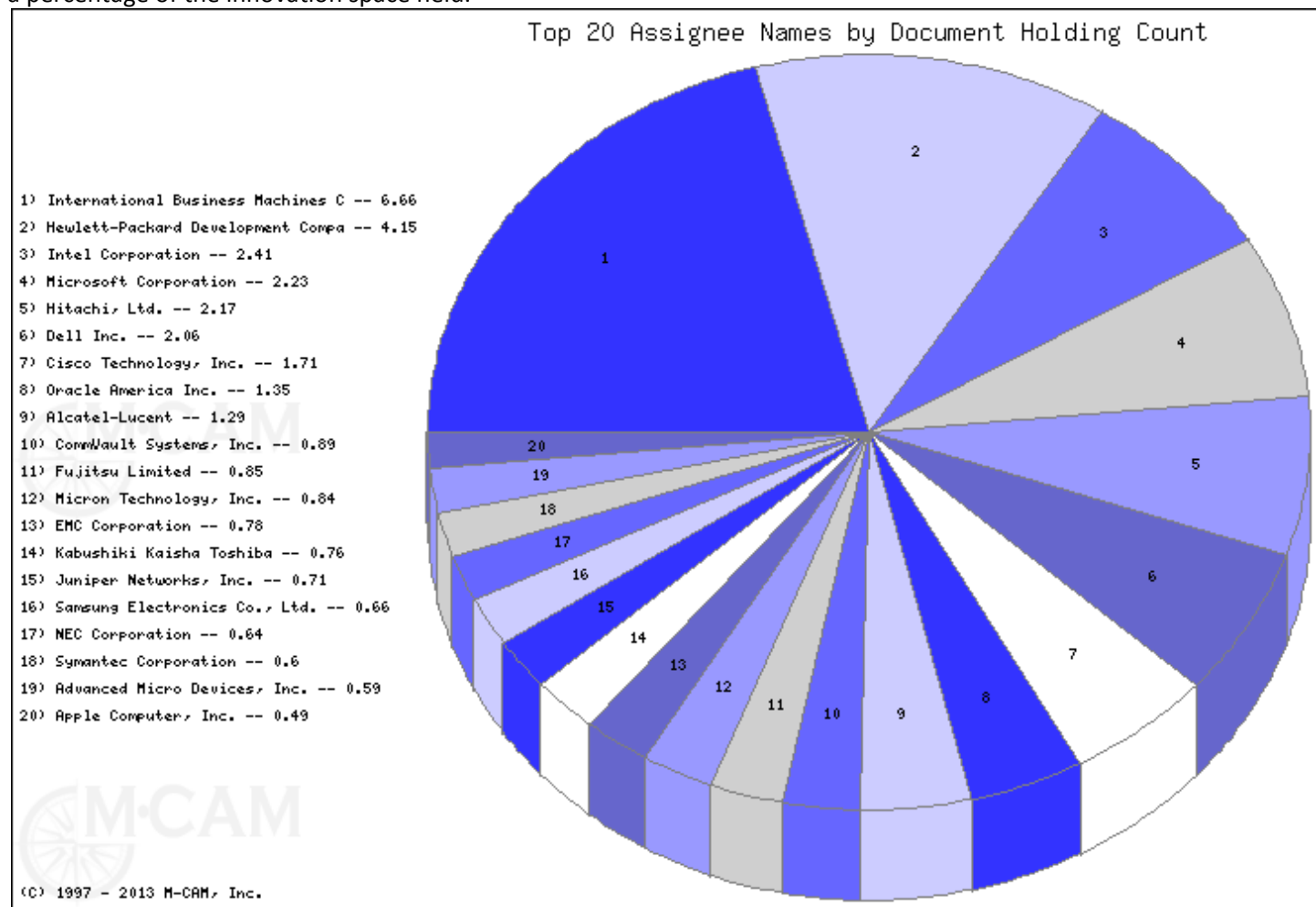


<sup>6</sup> <http://allthingsd.com/20130307/read-carl-icahns-letter-to-dells-board-about-the-buyout-plan/>

<sup>7</sup> <http://www.sec.gov/Archives/edgar/data/826083/000082608312000006/dell10k020312.htm>

Microsoft is near the top of the list. Dell has a strong patent licensing program with Microsoft and Microsoft has offered to invest up to \$2 billion in the planned buyout.<sup>8</sup> However, they are by no means alone in their interest for some of these Dell properties. Phone makers like Samsung, Apple, and LG could be interested in Dell's Graphics Processing Units and may want to acquire those assets to help block competitors. This space indicates a definite growth opportunity for Dell, but only if it gets the visibility to act on this information.

Since Data Transfer, Networking, and Switches have some similar functional characteristics, their innovation spaces overlap significantly and we have combined them for a more comprehensive look. Again, property holders are shown as a percentage of the innovation space held.



IBM, Microsoft, Hewlett-Packard, Hitachi, Intel, Micron Technology, Apple, Oracle, Advanced Micro Devices, and Fujitsu are all companies which show up consistently in these innovation spaces. Many of these companies are in-sector competitors for Dell. In addition, many of these companies have executed IP monetization strategies which have put them in a relatively better market position.

Dell's strength in the areas of Graphics Processing, Data Transfer, Networks, and Switches should be recognized for its quality and used to more completely benefit Dell's investors. Those familiar with the Nortel Networks IP auction will note the presence of Microsoft, Apple, EMC, and Sony. These companies were part of the consortium which purchased the \$4.5 billion IP portfolio.<sup>9</sup> The auction set a high price tag on the value of patents in this space and demonstrates that this is a highly coveted market. Because Dell can play here competitively, some proportion of this value must be counted.

<sup>8</sup> <http://www.sec.gov/Archives/edgar/data/826083/000119312513038969/d480650dex991.htm>

<sup>9</sup> <http://dealbook.nytimes.com/2011/07/01/apple-and-microsoft-beat-google-for-nortel-patents/>

## *Conclusion*

If the 20% of Dell's shareholders who oppose the buyout understood the full range of options available to Dell, particularly in regards to its strong IP market controls, their enterprise-driven valuation approaches would expand to include an IP-informed share price greater than the current Southeastern alternative proposal.

Southeastern, Icahn, and other key shareholders could add value to its estimate of Dell's buyout share price to include a fully-informed analysis of the IP portfolio. Icahn could possibly offer more bridge financing to the company than the \$5.5 billion he already has to assist in manifesting this latent value. This evidence could aid those shareholders' quest to convince other investors to reject the proposed Michael Dell buyout offer and act to realize Dell's true value. If Dell would like to competitively leverage its IP in market segments where it has effective proprietary controls, then it needs to know where its marginal price controls actually reside. Only then can it successfully transform itself into a business that will be relevant in the future and realize the latent value of its IP portfolio.

## M-CAM's Patent Glossary

<u>Aligned Sector:</u>	The business sector in which the product(s) resulting from the patent(s) is currently or intended to be sold.
<u>Applicant:</u>	The person or corporation that applies for a patent with the intent to use, manufacture or license the technology of the invention; under U.S. law, except in special situations, the applicant(s) must be the inventor(s).
<u>Application:</u>	Complete papers submitted to the U. S. Patent and Trademark Office seeking a patent including oath, specification, claims, and drawings. This usually does not signify a Provisional Patent Application, but only a regular patent application.
<u>Art:</u>	The established practice and public knowledge within a given field of technology. This also identifies a process or method used to produce a useful result. A term used in consideration of the problem of patentable novelty encompassing all that is known prior to the filing date of the application in the particular field of the invention.
<u>Assignee:</u>	The person(s) or corporate body to whom the law grants or vests a patent right. This refers to the person or corporate entity that is identified as the receiver of an assignment.
<u>Business Method Patent:</u>	A patent that controls the way a business process is undertaken. The issuance of these patents by the United States Patent and Trademark Office (USPTO) is new and controversial, since many allege that it is unfair to allow a patent on a way of doing business.
<u>Citation:</u>	This may include patents or journal articles that the applicant or examiner deems relevant to a current application. A reference to legal authorities or a prior art documentation are examples of a citation.
<u>Claim:</u>	The language in a patent application that defines the legal scope of the patent. Most patents have numerous claims. This is typically the single most important section in the application.
<u>Concurrent Art:</u>	Concurrent art occurs when related patent applications are being examined by the USPTO at the same time. It is difficult for any company or inventor to know, at the time they file for a patent, whether a "related" patent application exists.
<u>Filing Date:</u>	The date when a properly prepared application reaches the patent office in complete form.
<u>Innovation Cycle:</u>	A description of the commercialization timeframe for the intellectual property.
<u>Innovation Space:</u>	M-CAM's representation of the innovation(s) that occur before, during, and after the pending period of the subject patent. The innovation space is the first place to look for patents that are closely related to the subject patent and that may impact the defensibility of the subject patent or create opportunities for patent licensing.
<u>Issue Date:</u>	Not to be confused with the filing date, which is the date the patent application was physically received by the U.S. Patent and Trademark Office. This is the date on which the patent actually issues.
<u>Non-Aligned Sector:</u>	Any sector in which the patent can be used or sold, other than the sector for which the patent or resultant product was invented or intended.
<u>Pod:</u>	A group of patents owned by a company that should be treated as a single unit of innovation (e.g., a certain group of patents that comprise a single product or multiple related products).
<u>Prior Art:</u>	Any relevant patent that was issued before the patent being analyzed. If this previous patent was specifically mentioned in the new patent's application, the previous patent is referred to as "cited prior art". If it was NOT mentioned, then that previous patent is referred to as "uncited prior art".
<u>Subsequent Art:</u>	Any patent that has a filing date with the USPTO that is after the issuance date of the subject patent. This subsequent art patent may or may not have cited (see "Citation" above) the subject patent. As subsequent art represents more recent innovation than the subject patent, it has great potential to shrink the market opportunity for the subject patent.

## *A Brief Primer on the Patent System*

In recent years, the importance of patents and intellectual property rights as an important variable in the marketplace has come to the forefront of the public consciousness as world leaders declare their country's lead in the innovation race. Damaging intellectual property litigation is becoming increasingly common across all industries. This is exacerbated when patent rights are granted for non-novel ideas. A vast amount of precedent innovation is unconsidered by patent-granting authorities in the creation of new IP rights. Patent granting authorities including the United States Patent and Trademark Office (USPTO), European Patent Office (EPO), Japanese Patent Office (JPO), Chinese State Intellectual Property Office (SIPO), Korean Intellectual Property Office (KIPO) and many others are constrained by the use of patent classification systems which are routinely circumvented by patent applicants.

There is a two-way social contract underlying the patent system. In the United States, patent terms are generally limited to 20 years from the date of application. By statutory intention, once a patent has expired, the patent holder loses the right to exclude others from fully utilizing any innovation described in the patent. A large number of patents enter the public domain when they are "abandoned" – when owners discontinue paying patent maintenance fees. Patents also only provide an exclusionary right in the country for which the patent is filed. As demonstrated by the Global Innovation Commons<sup>10</sup> (G.I.C.), using intellectual property available in the public domain eliminates the need to pay licensing fees on those innovations in countries where the patent was never registered, or worldwide, if abandoned.

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<sup>10</sup> <http://www.globalinnovationcommons.org/>