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IN-DEPTH PATENT MONETIZATION COVERAGE

Finjan CEO Phil Hartstein says rigors of running a public company help him drive credibility and profits

Finjan Holdings Inc. (FNJN) CEO **Phil Hartstein** said the responsibility of being CEO of a publicly traded company has forced him to develop and execute an effective business strategy and communicate it clearly to shareholders, which is the key to credibility and profitability in the patent monetization business.

Even as other publicly traded IP companies go private such as **RPX Corp. (RPCXC)**, go without a CEO such as **Acacia Research Corp. (ACTG)** and **Immersion Corp. (IMMR),** sell themselves such as the former Unwired Planet, or are foreclosed upon, such as **Marathon Patent Group (MARA)** and **Inventergy Global (INVT)**, Finjan has avoided what Hartstein calls the pitfalls of "the pivot of 2016`-2017."

The pivot of 2016-2017 involved many publicly trade IP companies using their cash to acquire operating businesses or selling out. It was a recognition that the bottom had fallen out of the U.S. patent market.

The damage started with the U.S. Supreme Court's still controversial 2006 decision in eBay v. Mercantile Exchange, which set a higher bar for injunctions in patent cases and effectively rendered them impossible, depriving patent owners of a useful tool for forcing settlements.

Next came the high court's increasing skepticism of high damage awards and its outright hostility to non-practicing entities or patent trolls.

The piece de resistance was the America Invents Act of 2011, which made it much easier and cheaper to challenge patents through the inter partes review process overseen by the Patent Trial and Appeal process.

The IPR process and the PTAB developed into a system that cancelled some 80% of the claims of patents challenged in the years since it was passed in 2011. The numbers cancelled of late have come down as the low hanging fruit of the lowest quality patents diminished.

East Palo Alto, California based Finjan has had nearly inverse results and has successfully defended the vast majority of IPR challenges of its patents. To date, approximately 80% of petitions to challenge the validity of Finjan's patents have been denied institution. For the petitions that have been instituted, Finjan has only lost one independent method claim out of hundreds of claim challenges.

That has allowed Finjan under Hartstein to resist the siren call of going private or acquiring an operating business or reducing its patent enforcement efforts due to concerns about how difficult licensing and litigation has become over the last five years.

That's in large part thanks to its home grown foundational cybersecurity patents, which allowed Hartstein to remain focused on winning enforcement actions and managing his licensing pipeline.

The company is on pace for its best year ever for revenue, with revenue to date of more than $80 million. The company has been able to double its revenue every year for three consecutive years, and expects to do so again in 2018.

Given the Finjan's continued success and growing balance sheet, Hartstein told shareholders earlier this year the company was working with the board on considering three different strategies, which he outlined as "more of the same," "something new" and returning cash to shareholders.

He said that after talking with shareholders and hearing their views about the risks of pursuing the acquisition of an operating business, shareholders told him they would prefer for Finjan to stick with what it does best, which is patent licensing deals.

In May, Finjan also announced a $10 million share buyback program.

To be sure, other IP companies have not fared so well. San Francisco-based RPX recently sold itself to middle market private equity firm **HGGC LLC** for $555 million in cash, a year after ousting its former founder and CEO **John Amster** under pressure from activist investor **Mangrove Partners**.

Newport Beach, California-based Acacia's decision to go without a CEO since the ouster of former CEO **Matt Vella**, who was the architect of its marquee patent portfolio strategy, which focused on portfolios expected to produce at least $100 million in revenue, led to an activist investor campaign that ousted Executive Chairman **G. Louis Graziadio III.**

Under Graziadio, Acacia downsized its patent licensing business and used cash to invest in risky technology startups and also stopped articulating its corporate strategy with shareholders. The dissatisfied shareholders eventually sided with activists **Sidus Investment Management** and **BLR Partners** in a proxy battle that rested control of the company from Graziadio.

In the meantime, Acacia with Sidus' **Al Tobia Jr.** and **Clifford Press** on its board has not articulated a new strategy for Acacia.

"Acacia is already substantially downsized," Hartstein said. The company has indicated its staff now consists of 13 employees down from 57 at the time Vella ran the company in December 2015.

"That's not enough staff to effectively monetize the diversity in their patent portfolio. They have plenty of cash to do so, but they're not spending the cash on their licensing programs."

"The problem is that even though Acacia has plenty of cash there's no one at the wheel, driving the ship."

The allure of being a public company is often driven by two factors, access to capital, and liquidity for longtime shareholders.

Hartstein adds a third, transparency, which "may be the least obvious of the bunch but the results been extremely transformative for Finjan."

He emphasizes that it's his responsibility as CEO to put in place a business strategy that is effective, durable, and that will lead to creating shareholder value.

"We haven't deviated from the strategy we installed in the early days of Finjan's life as a public company, not in five years."

He also maintains constant communication with shareholders to make sure they fully understand the risks and rewards of any potential change in strategy.

In contrast, he said Acacia stopped communicating with shareholders after Vella was ousted.

After that, "shareholders were left to guess who was in charge and where the company was going, which is how they got to where they are today."

In the absence of communication with shareholders, he said it's no wonder Acacia trades at a discount to its cash position and investment in Veritone.

Institutional shareholders require certainty in their investing and sometimes the associated expenses of being a public company don't align with being an IP licensing company.

Being a public company comes along with significant fixed expenses and reporting costs, which can be 10% to 20% of a company's total operating expenses. There are also costs associated with regular reporting, operating a board, and substantial costs of interacting with shareholders.

Those costs are both real dollars and also the intangible costs of management's time.

"The reason you go public is access to capital and liquidity for shareholders, which doesn't ring true for microcap companies and especially microcap IP companies.

"The requisite discipline of running a public company and the integrity by which you adopt that rigor translates into credibility. We report good outcomes and bad outcomes equally, though we've been fortunate to not have many bad outcomes lately. We understand deeply that the shareholders own the company. If you don't communicate with them they'll make sure you don't enjoy being a public company."

Hartstein said adopting transparency across all aspects of the business is critical for success, and without the regiment of reporting requirements transparency is window dressing.

"You have to practice transparency as the CEO of a public company because you have no choice. And if you do, it becomes embedded in your process. You don't just say you're transparent. You are."

That helps establish credibility, which is the most important thing for a public company.

"Being a public company CEO is often demanding, often in ways I never expected, but it has some advantages. A good strategy and transparent communication lead to credibility and success."

Hartstein is very protective of Finjan's credibility. It's what prevents him from venturing beyond Finjan's wheelhouse into patent portfolios unrelated to its core cybersecurity patents or into acquiring an operating business.

Instead, he has turned to investments such as becoming a strategic limited partner in a venture fund called JVP which is focused on providing capital to new and upcoming cyber related technologies.

Finjan Blue — a relationship created with IBM Corp. – is another investment which also owns foundational cybersecurity patents which Hartstein indicates incrementally strengthens Finjan's overall portfolio and make its licensing offerings more comprehensive to potential licensees.

Finjan's view of blockchain technology and whether patents related to specific blockchain features such as hashing, illustrates the costs of venturing out of a patent licensing company's wheelhouse.

While Acacia, the former Vringo and other patent monetizers have touted the potential value of patents related to blockchain technology, Hartstein plays down the enforcement value of Finjan's own portfolio in that emerging sector.

"Hashing is something that Finjan's existing patents cover. We have looked at how hashing patents might intersect with cryptocurrency technology. We don't see any enforcement value, not at this time. That goes back to our credibility. If you start applying your patents to a new untried technology you're going to lose credibility in that endeavor."

In the meantime, Hartstein said Finjan isn't interested in being a consolidator in the IP monetization space, because so many of the assets that are available are so encumbered by various side agreements with the original owner, contingency lawyers, or where rigid monetization strategies have already been deployed to make it next to impossible to extract value through enforcement. He said that certainly, this translates into diminished value.

"Many have had decisions and continuing liabilities that can't be unwound. Those challenges are more of as risk for a small company like Finjan."

Big financial players such as **Fortress Investment Group,** whose IP division is run by **Eran Zur**, or **Vector Capital,** whose IP shop is run by **Rob Amen**, as well as larger established players like **InterDigital Inc. (IDCC)** and **Xperi Corp. (XPER)** are the only real consolidators because they have the requisite funds and patience to execute a revisionist strategy or find a CEO who can devise a strategy to extract the value.

"Acquisitions and the execution of them are a substantial distraction. As a CEO looking at those opportunities, I believe sometimes it's more risk to your capital investment than it's worth."

"That's a lot of the reason you're seeing a number of IP companies not being acquired and being delisted or foreclosed upon," he said.

Indeed, Fortress recently decided not to foreclose upon patents owned by **Document Security Systems (DSS)**, after previously foreclosing upon assets owned by Marathon Patent Group and Inventergy Global.

Editor and Publisher Dan Lonkevich is available for public commentary and speaking engagements. Connect with him on LinkedIn.

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