

# After six years of attacks, Qualcomm finally sees stability return to patent licensing

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Alex Rogers says he likes stress. As head of Qualcomm's maligned patent licensing division, he has seen plenty of it over the past few years.

Starting in 2014, government regulators from China to South Korea to the U.S. attacked the San Diego mobile technology firm's lucrative [business](#) model for licensing its intellectual property, claiming it coerced smartphone makers into paying sky-high patent fees that harmed

consumers.

Apple joined the fray in 2017 with a lawsuit aimed at dismantling Qualcomm's blueprint for licensing patents. A year later, chip rival Broadcom made licensing troubles the centerpiece of its hostile takeover pitch to Qualcomm shareholders. The takeover failed only after the U.S. government moved to block it over national security concerns.

"All of these matters were challenging various elements of the licensing business and creating pressure on the licensing business," said Rogers. "That created a tremendous amount of uncertainty. How would the licensing business fare? Will the licensing business, for example, be forced to license at the chip level and what will that do to the value of Qualcomm's patents?"

Fast forward to today. For the first time in years, the narrative around Qualcomm is not dominated by legal struggles in patent licensing, which helps fund about \$5 billion a year in [fundamental research](#) that has made Qualcomm the U.S. leader in developing core mobile technologies such as 5G.

Instead, the conversation has shifted to the company's emerging 5G processor opportunity, including its return as a mobile chip supplier for Apple's iPhones. Qualcomm's shares are up more than 35% so far this year.

"This is probably the least controversial the licensing business has been from a Wall Street perspective in a decade," said Mike Walkley, an analyst with Canaccord Genuity. "If you step back, there was huge pressure on these guys to cave in and sell the company to Broadcom for 50% below where the stock is today. Give them credit. They held their ground and got through this."

The licensing turnaround stems from the culmination of factors—the accelerated commercialization of 5G that nudged Apple toward mending fences; settlements with regulators in China and Taiwan that left Qualcomm's business model intact; and a big legal win last month at the U.S. 9th Circuit Court of Appeals.

But the company also made strategic moves aimed at lowering the heat surrounding its licensing division.

Key among them was a decision to offer worldwide licenses for its cellular standard-essential patents—required intellectual property that enables interoperability between devices and networks—at a lower rate.

Qualcomm also added its trove of new 5G patented inventions to its licensing program at no extra charge.

Rogers is the choreographer of this strategy to lessen the volatility around patent licensing. An English major and former high school teacher, he went back to Georgetown for his law degree and worked as a litigator before joining Qualcomm in 2001. He was named head of licensing in 2016.

"What we did not want to change is the fundamental model that we have now, which is the licensing business funds an underlying level of research that very few companies in the world do," he said. "The purpose of the licensing business is to get a return that allows us to keep doing this research years ahead of these standards actually coming into being. It allows us to drive technology in mobile five to 10 years ahead of when it actually hits the market."

Rogers and other company executives often talk about bringing "stability" to patent licensing. The strategy appears to have worked. Qualcomm has entered into more than 100 5G license agreements to

date. (It has over 300 licensees for its 2G, 3G and 4G patents.)

The company has signed multi-year licensing deals with all major smartphone brands—including Apple, Samsung, LG, Xiaomi, Oppo and Vivo. Last month, Qualcomm inked a new license with holdout Huawei, China's largest smartphone maker.

"Because we have licensed up every major handset manufacturer, not to mention scores of other device manufacturers, we have worked through all this with the licensing program not only intact but healthy," said Rogers.

Even so, patent licensing is no longer seen by Qualcomm investors as the high growth business that it once was.

During the peak of the 3G to 4G smartphone upgrade cycle, royalty revenue doubled. By 2015, patent fees brought in nearly \$8 billion and were forecast to grow to \$10 billion.

Back then, Qualcomm's base royalty rate was 5% of the wholesale device price for its full portfolio of standard essential and nonessential patents—though some high-volume customers or those with their own intellectual property paid less.

Today, it's 3.25% up to a \$400 cap for cellular standard-essential patents. While Qualcomm still offers a full portfolio license, many customers opt for the lower rate of the SEP only version.

Analysts forecast Qualcomm's annual revenue from patent licensing in fiscal 2021 at roughly \$6 billion, as Apple and Huawei resume royalty payments and the smartphone market slowly recovers from the coronavirus downturn.

"When I first started covering the company a dozen years ago, all anybody cared about was licensing," said Stacy Rasgon, an analyst with Bernstein Research. "Now people aren't looking at it to be a growth business. I think what you're hoping for is stability."

Qualcomm made other strategic moves that eased legal pressure on licensing. It championed the accelerated rollout of 5G. That contributed to Apple and Qualcomm settling lawsuits in 2019. Apple signed a multi-year patent license with Qualcomm, as well as a chip supply agreement, that is expected to bring 5G to new iPhone models later this year.

Perhaps the biggest milestone for stability was the U.S. 9th Circuit Court of Appeals ruling in August that the company's patent licensing practices are legal and do not violate anti-monopoly laws.

A three-judge panel threw out a lower court's antitrust finding against Qualcomm in a case brought by the U.S. Federal Trade Commission in 2017.

"There are a number of folks out there who looked at this licensing business and said the model was unsustainable," said Rogers. "That has been put to bed by this 9th Circuit decision."

If the lower court's ruling had been upheld, it potentially could have forced Qualcomm to renegotiate and restructure hundreds of licenses to collect royalties based on a percentage of the price of mobile chips, rather than a percentage of the price of the entire device.

Such a requirement could have gutted royalty revenue and stalled Qualcomm's R & D funding engine.

"One point the 9th Circuit made was look, when you apply antitrust law to innovation, you have to be extremely careful because applying

antitrust law to innovation can actually stifle innovation," said Rogers.

"The other thing they recognized is business model innovation is actually good," he continued. "When you bring it down to their view of Qualcomm, the fact that we license our fundamental technology separately from selling chips was an innovative business model that was organic to the way Qualcomm developed, and the 9th Circuit said there is nothing wrong with that."

The company is not completely out of the woods. The FTC is considering an appeal. While Qualcomm has settled with China and Taiwan, its legal fight in South Korea is still working through the courts.

Nonetheless, when Wall Street analysts talk about [patent](#) licensing these days, there is less hand wringing over the direction of the business.

Rogers credits Chief Executive Steve Mollenkopf, an engineer with deep roots in the company's chip division, for sticking with licensing during the turmoil.

"He understands the value of the [licensing](#) business, and he believes in the model," said Rogers. "So through a lot of challenges and a lot of criticism, he was really a stalwart in ensuring that we deal with the challenges and move the business forward. We've got it to a place of stability, particularly as the 5G era comes along."

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