Patent Utilization Strategies: Patent Funds and Key Contractual Considerations

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I. Introduction

In recent years, there has been growing recognition of the strategic importance of intellectual property ("**IP**") rights—particularly patents—in corporate business strategy. Traditionally, companies have tended to acquire patents and exercise their exclusive rights to block competitors. However, patents are now increasingly viewed not only as tools for exclusive use but as assets that can create value through monetization strategies, including the controlled opening and licensing of those rights.

In Japan, however, it is not uncommon for companies to be unable to fully leverage their patents. This may be due to factors such as the nature of their relationships with other companies or the lack of personnel within the organization who are knowledgeable about IP management. According to the Japan Patent Office, of the approximately 1.63 million patents held domestically as of 2024, only roughly half or about 850,000 are actively being utilized.

Against this backdrop, one strategy for the effective use of patent rights is through IP funds, which is the focus of this article—hereinafter referred to as "**patent funds**." This article provides an overview of the concept and structure of patent funds and outlines key considerations for companies who are thinking of contributing their patents to such funds.

II. Patent Funds in General

1. What is a Patent Fund?

A patent fund is a financial entity that invests in and manages patents by assembling them into a portfolio, operating the fund with the capital contributed by investors, and distributing the returns generated from such operations to both the original patent holder(s) and the investors.

Patent funds come in various forms, targeting specific technological fields or encompassing the full spectrum from patent issuance to commercialization. Broadly speaking, they can be classified into the following three types. However, from Section III hereof, this article will focus primarily on two of them—licensing revenue funds and litigation-based funds.

(a) Licensing Revenue Funds

In this type of fund, the patent portfolio is leveraged to negotiate licenses with companies that are believed to be practicing the patented inventions. After concluding license agreements, the fund collects royalties as its revenue. In forming the portfolio, the fund typically identifies a specific technology area and aggregates patents accordingly.

While the primary goal is to conclude agreements through negotiation, discussions can become difficult or fail entirely if, for example, the target company denies that it is practicing the invention. Therefore, patent holders must thoroughly assess the likelihood of successful negotiations based on the fund's due diligence and business plans. Should negotiations fail, the fund may consider initiating legal action against the target company for alleged infringement, shifting to the model described in subsection (b) below.

(b) Litigation-Based Funds

Litigation-based funds target companies believed to be infringing on the patents held in the portfolio. The fund initiates patent litigation to seek damages, settlement payments, or other forms of compensation. Because this strategy involves a high degree of legal confrontation, patent holders must carefully vet the potential defendants and confirm that litigation would not interfere with their own business strategies.

(c) Support-Oriented Funds

This type of fund aggregates patents deemed promising for the future or technologies with long-term potential that have not yet been patented. The fund then holds and manages these assets, aiming to generate revenue through their eventual commercialization or enforcement. Although enforcement of rights may occur (as in the licensing or litigation types of funds), support-oriented funds differ in that they do not narrowly define a target portfolio. Instead, they focus on building broad networks with external companies and institutions and emphasize long-term development and flexible portfolio management.

2. Two Typical Structures of Patent Funds in Japan

Patent funds can be structured in various ways. Two representative models that are available under Japanese law are outlined below:

(a) TK-GK Scheme (*Tokumei Kumiai-Godo Kaisha*)

Under the TK-GK scheme, a limited liability company ("**LLC**") (*gōdō kaisha*) is established. Investors enter into an anonymous partnership agreement (*tokumei kumiai*) with the LLC by contributing capital to the fund. The LLC then holds and manages the operational assets, i.e., the patent portfolio. The anonymous partnership agreement stipulates that investors will provide funds for the fund's activities and share in the profits generated by it. Although this structure is widely used in real estate investments it can be adapted to the management of patent portfolios as an alternative asset class.

(b) IP Trust Scheme

Under the IP trust scheme, an LLC is established to hold the patent portfolio. Using the legal trust system, patents are placed into the trust as trust assets. The beneficial interests in the trust are then transferred to investors as a means of raising capital. While less commonly used than the TK-GK scheme, the IP trust scheme is gaining attention partly due to recent amendments to the Trust Business Act (Act No. 154 of 2004, as amended), Trust Act (Act No. 108 of 2006, as amended), and Patent Act (Act No. 121 of 1959, as amended), which now allow entities other than financial institutions to serve as trustees. In addition, the ability to record patent trusts and changes in ownership thereof, as well as their favorable tax treatment, have contributed to the gradual rise in the adoption of this scheme.

3. Three Benefits of Patent Funds from the Perspective of Patent Providers (Companies)

The first two subsections of Section II of this article outlined the structures and schemes of patent funds. This subsection discusses the advantages and potential benefits for companies considering contributing their patents to patent funds.

(a) Leveraging the Expertise and Human Resources of Fund Managers

As noted earlier in the Introduction section, unless a company is deeply engaged in the strategic use of IP, it is often the case that internal personnel lack sufficient expertise in valuing and utilizing IP assets. Fund managers, on the other hand, typically possess extensive experience in patent valuation techniques, networks of external partners, know-how in enforcement and licensing negotiations, and global contracts. Leveraging these resources allows for more efficient and effective patent utilization.

(b) Broader Utilization of Patent Rights

Although the range of ways a single company can utilize its own patents may be limited—depending on the number of patents it holds—a patent fund typically aggregates patents from multiple companies, enabling the formation of more robust patent portfolios. This makes it possible to pursue enforcement and commercialization strategies that are otherwise unavailable to individual companies, thereby expanding the scope of patent utilization.

(c) Lower Costs of Patent Maintenance and Enforcement

Enforcing patent rights often requires significant costs, including legal and professional fees. By delegating enforcement to patent funds, companies can shift these financial burdens to such funds. Moreover, when patents are transferred to a patent fund, the fund typically assumes responsibility for maintenance fees, resulting in lower patent-related costs for the original patent holders.

(d) Bankruptcy Remoteness and Limited Liability

Patent fund structures are generally designed to isolate patent portfolios from the effects of the fund's insolvency and ensure that investors are not liable for losses exceeding their investment. From a company's standpoint, such arrangements provide practical benefits in terms of limiting exposure and risk associated with any potential insolvency of the patent fund.

III. Agreements with Patent Funds

1. Types of Patent Rights Contributions

When a company participates in a patent fund, it must consider two distinct phases: the contribution of patent rights (including the grant of licenses, hereinafter referred to collectively as the "**contribution of patent rights**") and the capital investment. As explained in subsection 2 of Section II, investment-related agreements, such as anonymous partnership agreements (*tokumei kumiai*) or trust beneficiary rights transfer agreements, must be reviewed from the investor's perspective and involve various considerations. Due to space limitations, this section will focus on agreements related to the contribution of patent rights.

Broadly, there are two common structures by which companies may contribute patent rights to a patent fund: (a) patent transfer scheme, and (b) license scheme. Under the patent transfer scheme, the company transfers ownership of the patent rights to the patent fund. Under the license scheme, the company grants a license (with sublicense rights) to the patent fund. In some cases, only one of these schemes may be adopted, while in others, a combination of both may be used.

2. Two Key Characteristics and Considerations in Patent Rights Contribution Agreements

When a company contributes patent rights to a patent fund, it must enter into either a patent assignment agreement or a patent license agreement with the patent fund. The following subsection outlines key considerations and practical points to be addressed when entering either type of agreement.

(a) Scope and Conditions of Enforcement

First and foremost, if a company is considering contributing its patent rights to a patent fund (i.e., a licensing revenue fund or litigation-based fund), it is essential to confirm whether the potential targets of enforcement would pose any commercial or strategic conflict for the company. In this regard, the company should proactively inquire with the patent fund about which entities are being contemplated as enforcement targets under the patent fund's business plan, and whether additional targets may be included in the future.

Furthermore, in determining the method of contribution—whether to transfer ownership of the patent rights or merely to grant a license—the company must carefully coordinate with its internal business departments. This is especially important where the subject patents are currently significant to ongoing operations or are expected to become strategically important under future business plans. It is therefore critical for business development and IP departments to align their understanding and strategy. If internal hurdles render an outright transfer of the patents impractical, then the company may consider granting a license with sublicensing rights instead. However, from the patent fund's perspective, whether it holds full ownership of the patents or merely a license can significantly impact both the scope of enforceable rights and its negotiating leverage with third parties. Holding title to the patents allows the patent fund to assert them without restriction, whereas a license-only structure may impose certain limitations on its enforcement authority. Accordingly, careful evaluation of the enforcement scope consistent with the patent fund's business objectives is essential when structuring the rights to be granted.

(b) Consideration and Cost Allocation

Under both the patent transfer scheme and the license scheme, it is essential to determine how consideration for the transfer or license of the patent rights will be structured. Two primary payment models are generally considered: a lump-sum cash payment based on a pre-assessed valuation of anticipated enforcement outcomes, and a profit-sharing model.

The profit-sharing model, which has become increasingly common in recent years, typically involves an initial payment at the time of the patent transfer or license grant, followed by ongoing revenue sharing based on the actual monetization results achieved by the patent fund. This approach is particularly suitable for patents whose value is difficult to quantify upfront, as it allows for the allocation of profits in proportion to the returns realized. When adopting a profit-sharing arrangement, the company must conduct a detailed review of the patent fund's business plan, including the anticipated targets and number of enforcement actions, the projected revenue from such actions, and the methodology for calculating and allocating profits. It is also important to examine how the profit split is structured among the company, the patent fund, and its investors. In particular, with respect to the projected revenues and the calculation methodology, the company must ensure a sound understanding of the underlying assumptions, taking into account the scope and conditions of enforcement discussed in subsection 2(a) of Section III of this article. Based on this understanding, the company should engage in thorough discussions and negotiations with the patent fund to agree on appropriate profit allocation terms.

(c) Coordination with Existing Use of Patents (Self-Use and Licensing by Group Companies)

Where a company has already granted licenses to third parties or entered into cross-licensing agreements within its corporate group, transferring or licensing the same patents to a patent fund requires careful coordination with these existing agreements. For example, if a patent under an existing license agreement is being transferred to a patent fund, the licensee must be assured that they can continue using the patent under the same conditions. In such cases, a tripartite agreement among the company, the patent fund and the licensee is usually required. The company should proactively provide information to licensees and begin coordination for such three-party agreement alongside the main agreement with the patent fund.

(d) Reversion of Patent Rights and Treatment upon Fund Termination

While it is ideal for the patents contributed to a patent fund to be fully utilized and generate revenue throughout their remaining term, there may be cases where, due to various circumstances, the patent fund is unable to continue monetization efforts. Additionally, the possibility that the patent fund itself may be prematurely terminated cannot be ruled out. From the company's perspective, if the patent fund is no longer pursuing monetization, it would be reasonable to seek the return of the relevant patents to explore alternative avenues for commercialization. Therefore, it is advisable for the company and the patent fund to agree in advance on the conditions under which the patents may be returned to the company. However, in the case of litigation-based funds, setting return provisions may be challenging due to concerns over standing to sue (i.e., whether the fund qualifies as the proper plaintiff). If the structure allows for patents to be easily returned to the original owner, then courts in certain jurisdictions may conclude that the transfer of ownership was not substantive enough, potentially resulting in the patent fund being denied standing in litigation.

Accordingly, any return provisions must be carefully structured with consideration of these legal implications, particularly regarding the requirements for standing in the relevant jurisdictions.

IV. Conclusion

The strategic utilization of companies' dormant patents not only contributes to effective asset management and monetization but also acts as a catalyst for industrial revitalization. Patent funds are expected to play an increasingly important role in facilitating such use.

We hope that this article provides useful insights for companies considering leveraging patent funds to unlock the value of their patent portfolios.