Who's afraid of Nathan Myhrvold?

The giants of tech, that's who. And they have a nasty name for the former Microsoft honcho: "patent troll."

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(FORTUNE Magazine) -- Nathan Myhrvold says he doesn't know what everybody is so upset about.

"Some article called me the most feared man in Silicon Valley," he says. "Good Lord! Why? My teenage boys got a kick out of it: 'Dad, how could this be true? You're not even the most feared person in this house. '"

Myhrvold, 47, is a nerd's nerd, an exuberant and charismatic polymath with a rollicking laugh, the rumpled look of a science professor, and an armload of academic credentials.

He has a master's in geophysics and space physics from UCLA, a Ph.D. in theoretical and mathematical physics, and a master's in mathematical economics from Princeton. He's also a paleontologist, a prize-winning photographer, and a gourmet chef.

Oh, yeah - and he's very rich.

Myhrvold, formerly Microsoft's chief technology officer, retired six years ago from the software giant with a fortune that, it's safe to say, runs well into nine figures.

But instead of taking early retirement as a chance to relax, travel, and maybe dash off a unified field theory or two, Myhrvold collects everything from antique slide rules to chunks of meteorite.

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Great patent fights in history

Patents have been controversial for as long as they’ve existed in the U.S. The arrival of virtually every major invention has been followed by waves of litigation, charges of abusive lawsuits - and attempts to reform the system.

19th-century patent pirates

Samuel F.B. Morse railed about "patent pirates" in the mid-19th century, complaining of hours spent in court to prove he was the inventor of the telegraph.

The patent that Ford fought

In the early 20th century, a group of financiers purchased a patent from inventor George Selden that purported to cover all gas-powered cars. Henry Ford eventually crushed the patent in court.

Flying solo

The Wright brothers were vilified because they refused to license their airplane patents. During World War I the U.S. government forced them to share.

Patents vs. the courts

Patents have at times had a reputation as evil tools to protect monopolies. As Supreme Court Justice Robert Jackson wrote in 1949, "The only valid patent is one which this Court has not been able to get its hands on."

Too much protection?

Fears of diminishing U.S. innovation in the ’70s led Congress to beef up patent protection, creating a special appeals court. Critics say patents are now granted too easily and the court protects them too strenuously.

Shutting down BlackBerry

The BlackBerry case last year made the patent issue real for millions of people, who were infuriated that their mobile e-mail might be shut down.

Myhrvold has founded a firm, based in Bellevue, Wash., that has produced almost as much rage, terror, and ominous speculation as Microsoft once did.

It's called Intellectual Ventures, or IV, and it's a combination private-equity fund and innovation hothouse. The plan, Myhrvold says, is to purchase and invent patents and then license them to manufacturers.

Others see IV as something altogether more sinister. As Shane Robison, the chief strategy and technology officer of Hewlett-Packard (Charts), puts it, "They are a very large patent troll."

Patent troll (n., derogatory): An entity that neither invents nor makes products but instead acquires patents and uses them to extort money from legitimate businesses by suing or threatening to sue.

The species became notorious last year when BlackBerry users nearly had their service cut off by a patent suit, and the manufacturer of the wireless e-mail devices, Research in Motion, was eventually forced to shell out $612 million to settle.

More recently, the U.S. Supreme Court weighed in this May on a patent case involving eBay, potentially making it harder to obtain injunctions like the one that could have halted the use of BlackBerries.

That hardly extinguishes the threat of trolls, in the view of tech companies, which have been lobbying in Washington for patent reform.

In this contentious environment, perhaps it's not surprising that suspicion surrounds Myhrvold's firm, at least in Silicon Valley. While the firm has said little about what it is up to, press accounts have estimated that Myhrvold has gathered some 3,000 to 5,000 patents, an order of magnitude greater than that of any other purported troll (few of which have more than 100).

To many tech executives, it seems only a matter of time before Myhrvold turns to the courts to try to monetize those patents.
This conclusion alternately irritates and amuses the often amused Myhrvold.

A weird concept

During a series of in-depth discussions with FORTUNE over several weeks, he cheerfully admits that "IV is a big investor in patents" (though he won't give specific numbers).

"Here's my 'secret plan,' " he explains one recent morning aboard his Gulfstream V en route to a meeting with inventors in Austin.

He reels off a list of companies that have made huge sums by licensing patents, such as Lucent (Charts), Texas Instruments (Charts), and IBM (Charts), which generates $1 billion a year on its patents.

"We want to build a portfolio just like those companies have, with licensing approaches broadly like they have ... I want to achieve what IBM has achieved. That's my financial model. This is a play where I take portfolio theory and apply it to something illiquid to deliver a return for my investors. I don't see that as evil. I don't see that as particularly threatening."

And that is where the notion of IV as a "troll" starts to get weird.

Myhrvold's firm was, in one early iteration, titled the Patent Defense Fund. Today Myhrvold's reported investors include some of the same companies that most vociferously condemn trolls: Microsoft (Charts), Intel (Charts), Sony (Charts), Apple (Charts), eBay (Charts), and Google (Charts). (Myhrvold will say only that the list "isn't fully accurate." Intel and Google declined comment. Sony, Apple, and eBay didn't respond.)

Microsoft confirms to FORTUNE that it is putting $76 million into IV: $36 million as an equity investment and $40 million for the right to use IV's inventions, with an option to invest an additional $40 million later.

Which raises the question: Can Myhrvold's firm be both scourge and benefactor of tech companies at the same time?

On a late-May evening, Myhrvold is out with his friends Tim and Nina Zagat, eating in the kitchen of Manhattan's glittery Le Cirque. Myhrvold, who loves to eat almost as much as he loves to talk, is an investor in the Zagats' restaurant-guide business and proudly flashes a business card that reads CHIEF GASTRONOMIC OFFICER.

As usual, he is holding court.

Myhrvold tells how his own cooking career began when, at age 9, he persuaded his mother to let him flambé a turkey for Thanksgiving. It may be the salutary effects of several glasses of Crozes-Hermitages, but Myhrvold soon turns the conversation to IV's new inventions, which he otherwise cloaks in secrecy.

He describes a portable device his firm is working on that, he says, can diagnose whether a stroke has been caused by a blood clot or a hemorrhage and make a huge difference in a patient's chances of survival. His audience is enthralled. (Says Bill Gates via e-mail: "I believe the inventions they have already made [at IV] will have an impact on many fields.")

At the hushed Palo Alto headquarters of HP, reactions to Myhrvold's ideas are considerably more skeptical.

Joe Beyers, who oversees HP's patents, dismisses IV's invention plans as a "smokescreen to buy time." The real game will be lawsuits, he says.

"We're very familiar with their business model," adds HP's Robison,
explaining that Intellectual Ventures approached HP as a potential investor. Robison says he can't say any more than that because he's bound by a nondisclosure agreement. But why, he suggests, would Myhrvold collect all those patents if he weren't planning to start suing eventually?

From HP's perspective, trolls have an unfair advantage. They could shut down a manufacturer. But trolls are immune to countersuits, because they make nothing themselves.

That balance of power is very important to companies like HP, which both licenses and litigates patents. In fact, Robison and Beyers aggressively market the company's 30,000 patents and other intellectual-property rights. Last year the program brought in $200 million.

Is there much difference between that and being a troll?

Robison says HP sues only to protect its rights, not to generate revenue. Ultimately, it's a moral distinction or maybe a metaphysical one.

What it seems to come down to in the minds of Robison and other troll haters is that HP makes stuff, while Myhrvold et al. do not. "We're trying to run a business," Robison says. "We're not in the business of running around the world pissing everyone off."

Myhrvold, naturally, doesn't see himself that way. He says, "I've never filed a patent lawsuit. I hope never to file a patent lawsuit. That may be unrealistic, but it would be great if I could avoid doing it.... Lawsuits are a ridiculous way to do business."

Like a cagey pol, though, he isn't about to take any no-lawsuit pledges. From his point of view, that would be like taping a PLEASE INFRINGE MY PATENTS sign on his back.

Room 226 of the U.S. Senate's Dirksen building is standing room only, but you can tell Myhrvold is present when you hear his theatrical laugh cut through the pre-hearing din. He is seated at a green-felt-covered table on this mid-May afternoon, preparing to testify before a Senate subcommittee about patent reform.

His adversaries, seated shoulder to shoulder alongside him, include general counsel Mark Chandler of Cisco, whose company is among those leading the charge to make it harder for patent holders to extract money in lawsuits.

Chandler's testimony sketches a bleak landscape.

"The patent-litigation system is broken," he begins. He explains later that a single tech product--a laptop, for example--may have thousands of patented inventions inside it. That means thousands of opportunities to be sued and pay damages or be shut down completely, because the law permits a winning patent plaintiff to prevent an infringer from using the technology.

Cisco, he later notes, faces 13 patent suits today, compared with two seven years ago. The number of patent suits filed overall, he testifies, has more than doubled over the past 15 years. Moreover, he says, those statistics don't capture the many cases that are settled before a suit is even filed.

The next speaker, though, presents a starkly different reality. Philip Johnson, the chief patent counsel for Johnson & Johnson, might seem an unlikely ally for Myhrvold.

But it turns out that J&J, along with industrial giants like DuPont (Charts), General Electric (Charts), 3M (Charts), and Procter & Gamble (Charts), not to mention numerous universities, have lined up against tech companies.
Biotech and pharmaceutical products, Johnson explains, may be encapsulated in a handful of patents or even a single one. And because those companies make huge bets on their products, they want the maximum latitude to go after anybody who might be copying them.

Myhrvold, in his turn, challenges Chandler.

**Patent battles far and wide**

"This isn't a litigation crisis," he says. The number of patent suits filed in 2005, he points out, actually fell 11% from the previous year, while the ratio of suit per patent has been dropping over the past decade. There are more suits today, he argues, simply because there are more patents.

As the corporate factions spar, the challenge of finding consensus becomes clear. Sen. Orrin Hatch (R-Utah), who is presiding, remarks to the panel, "You haven't resolved all of our problems. If anything, you've made them more complex." Listening to him, it's hard to imagine significant patent reform emerging soon. That's a victory for Myhrvold, but not one that'll end the battle.

Patent combat, as we've seen, is not limited to trolls. Myhrvold says it has long been simply a fact of life in Silicon Valley, with big companies often infringing the patents of small inventors and daring them to sue.

He adds, "This isn't some X-Files conspiracy theory. I was in the meetings at Microsoft!" The big guys certainly are not reluctant to sue to protect their own patents (witness Verizon's recent legal assault on Vonage), and they've even gone to court over patents they've bought rather than invented.

In 2004, for example, Kodak (Charts) extracted a $92 million settlement from Sun, whose Java software had been found to infringe patents that Kodak had purchased from Wang Laboratories. Intel has also filed at least one such suit. (Intel's former patent head Peter Detkin—who is now a managing director at IV—coined the phrase "patent troll.")

In one more of the Troll War's ironic twists, IV bears more than a passing resemblance to entities that tech companies themselves use to quietly buy and sell patents or to pool patents with those of competitors.

These vehicles can protect them from lawsuits and provide a discreet way to make money, including through litigation. Dozens of giant corporations such as Sony, Philips, Microsoft, Thomson, and IBM have formed or acquired entities with names like Intertrust, ContentGuard, MPEG LA, and the Open Invention network, among others.

In fact, some big tech companies don't seem bothered at all by the emergence of Myhrvold's firm.

David Kaefer, Microsoft's director of business development for intellectual-property licensing, distinguishes between what he calls "patent speculators" (bad) and "patent aggregators" (good).

"Intellectual Ventures is a perfect example of a market efficiency," he says. "If you were in our shoes ... and ten really interesting patents [were being auctioned], do you really want to go with your business card saying MICROSOFT? Or do you want a third party to act on your behalf?"

As Kaefer puts it, "It's a chess board of leverage and counter-leverage." Entities like IV provide a variety of benefits for companies, he says, including one that might surprise you: By providing a venue to buy and sell patents, he says, such firms "reduce litigation."
Invention capital' fuels passion

So what exactly is the incentive for a fabulously wealthy geek with an endless list of enthusiasms to spend his middle age becoming the patent equivalent of an ambulance chaser?

"I'm not at the stage in my economic life where I can say I'll eat a better grade of hamburger because of this," Myhrvold notes. "I don't need to work."

Indeed, to see him at one of IV's "invention sessions," trading ideas with rocket scientists and brain surgeons (really), is to see a man who is just having fun.

And the idea of creating a new business model thrills him too.

He has dubbed it "invention capital" and likes to compare the reaction against it to what he used to hear about software, which early on was dismissed as just an adjunct to hardware, the real product.

Microsoft, of course, proved how much money there is in "just" software. "I'm in this funny position where I get to repeat my career with basically the same idea all over again," Myhrvold says. "First it was that software was a business, and now I'm trying to say invention is a business."

In his mind, it's partly just the newness of the idea that the HPs of the world find so upsetting. He compares invention capital to venture capital and private equity, which he's fond of saying were also once viewed with suspicion:

"The book about RJR Nabisco is called Barbarians at the Gate. It's not Smart Capitalists at the Gate. Barbarians! Oh my God! They were horrible!" He's happy to be today's business barbarian, if he also gets to be tomorrow's business hero.

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