Update to the Investment Committee
Matt Briggs and Tim Krauter
Schedule

1. BIG and RPXC
2. Business Overview
3. Initial Thesis
4. Recent Developments
   1. Inventus Acquisition
   2. Management / Mangrove Partners
5. Legislation Risk
6. Valuation
BIG and RPXC

- BIG bought 507 RPXC shares in December 2014 at $13.91 per share
- Shares hit $16.82 per share in June of 2015 before falling to $8.71 last month (June 2016)
- As a result, BIG is currently down ≈29% on the investment and we have decided to reevaluate our thesis and the company’s positioning in the patent risk aggregation market
- BIG’s position in RPXC currently represents 4.5% of the portfolio, making it the second smallest position in the fund after VLKAY (3.5%)
Business Overview

• RPX’s offers a core subscription product that has 3 real value propositions:

  1. RPX buys up patents and licenses in the open market that would otherwise be sold to patent trolls, thus preventing their clients from being sued for potential infringement of these patents

  2. RPX helps to settle cases quickly for their clients in the event that they do get sued, thus limiting legal and transactional costs

  3. RPX will also occasionally negotiate large patent transactions for a fee (ex. Rockstar acquisition in 2015)

• RPX has also begun selling an insurance product to smaller clients that don’t get sued enough to consider the core subscription product or lack the funds to pay for the full patent portfolio

✓ Note: At this time, the insurance clients contribute minimal revenue and the future success of RPX is largely dependent upon demand for the core insurance product
### Initial Investment Thesis

<table>
<thead>
<tr>
<th>Compelling Value Proposition</th>
<th>Significant Barriers to Entry</th>
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<tbody>
<tr>
<td>• Right to use all patents in RPX’s patent portfolio</td>
<td>• Need certain size to offer meaningful patent protection to lucrative customers</td>
</tr>
<tr>
<td>• Patent trolls buying up patents and suing companies represent large costs and operating risks for companies</td>
<td>• Large portfolio of patents creates a network effect</td>
</tr>
<tr>
<td>• RPX can settle cases by buying the trolls’ patent, which then additionally benefits their subscription clients</td>
<td>• Management has deep-rooted expertise with years of experience navigating patent market</td>
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<table>
<thead>
<tr>
<th>Insurance Market Possibilities</th>
<th>Cash</th>
</tr>
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<tbody>
<tr>
<td>• Insurance market remains an opportunity (but a small one)</td>
<td>• $203 million of cash and short term investments as of Q1</td>
</tr>
<tr>
<td>• Difficult to “convince” smaller clients that they need patent insurance</td>
<td>• Ample room for stock repurchases and continued patent spend</td>
</tr>
<tr>
<td>• Much smaller rev/client and questions around actual profitability</td>
<td>• Provides downside protection (currently represent ≈40% of equity value</td>
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Inventus Acquisition

- Inventus Solutions is a discovery management practice focused on the use of technology to enhance the legal discovery process

- Main Services:
  1. Managed Services
     - Offer a suite of services that cover initial data collection to data manipulation throughout the entire discovery process
     - Effective use of technology to reduce costs and operational burden
  2. Project Management
     - Provide support and technical assistance throughout the document review process and discovery phase of the litigation life cycle
  3. M3: Multi Matter Management
     - Product that allows corporate legal departments to recycle data, coding, and valuable attorney work across multiple cases

- eDiscovery Market is expected to grow at a 10% CAGR through 2019, especially in international markets within the enterprise sector, which is the sector Inventus is particularly exposed to (2/3 of revenue)

- Potential for synergies and cross-selling, although we disregarded these in our model (also set to expand RPX’s international presence)
Mangrove Partners

- Mangrove Partners is value oriented investment manager and is currently the 5th largest shareholder in RPX.
- They recently took an activist position in RPX, nominating 3 members to the Board of Directors (7 seats total).
- Highlighted current mismanagement and areas they plan to focus on:
  1. Poor capital allocation
     - Purchased Inventus at 12.7x EBITDA while RPX was trading at only 1.6x (slight exaggeration by Mangrove)
  2. Excessive employee compensation
  3. Wasteful growth projects
     - Too much investment ($16 million annually) that produce minimal revenues
  4. Stagnant core business growth
     - Restructure sales force
  5. Cash Hoarding
     - Suggest moderately leveraging balance sheet and returning cash to shareholders
Market Perception

**Limited Competition**
- Defensive patent aggregation scheme unique
- RPX has first mover advantage in the space making threats of competitors entering the space very weak
- RPX’s expertise in the patent space is an additional value add for its clients
→ Market understands novel business model

**Capital Intensive Business**
- Patent spend is ~50% of revenue, which is significant (think of this as CapEx and maintenance CapEx)
- Inherent risk in navigating this illiquid market (uncertainty around ability to buy the right patents at the right prices)

**Industry Headwinds**
- NPE legislation a huge problem; litigation claims will decrease and RPX’s value proposition fades
- RPX has picked off the low-hanging fruit, making it incrementally harder to acquire customers; with constant churn that will decrease clients even if industry were to remain in size

**Inventus Acquisition like Burning Cash**
- RPX paid $228mm on 18.3mm of EBITDA (12.5x) for a business that some argue will create few synergies (overpaid significantly)
- Beyond financial “repercussions”, shareholders lament management’s broader incompetence
BIG Variant Perception

**Inventus Acquisition**
- Brings >$18mm of EBITDA and >1,000 clients, with potential to cross-sell
- Stock dropped >20% upon news of acquisition ($150mm of equity value slashed immediately)
- As a result, Inventus was valued at ≈$80mm, or ≈4.5x EBITDA (RPX paid 200% premium? Or lit $150mm on fire?)
- This is all assuming 0 value creation in cost synergies or cross-selling opportunities

**Mangrove Opportunity**
- Mangrove’s strategy aligns very well with our thesis and BIG’s core value strategy
  - Value-oriented long/short hedge fund
- Solid track record of investing in companies that have lost a considerable amount of market value
- In a position to have considerable influence on the company (3 board seats)

**Industry Headwinds**
- Patent litigation risk is not going away, even if patent trolls face more challenging operating environment
- Low-hanging fruit argument seems weak in wake of ≈150 subscription clients; every company that gets sued >2x per year is a potential client
- Multi-year subscriptions provide additional downside protection in the near term ($140mm in deferred revenue)

**Cash Reserves as Downside Protection**
- Share buybacks to create value even if core business does poorly (we assume -9% revenue CAGR through 2020)
- In addition to significant cash levels, significant room to lever up the business to free up room for alternative value creation methods (buybacks or dividends) if money can’t be used strategically to grow business
Legislative Risk

Innovation Act:
• Requires NPEs (patent trolls) to include the following details:
  • Specific accused instrumentalities alleged to infringe any claim
  • Name and model number
  • Where element in each claim is found
  • Authority of the party alleging infringement to assert each patent and the grounds for the court’s jurisdiction
• Requires losing party to pay for reasonable fees associated with the claim

Key Takeaway:
• NPEs need to be a lot more specific in their claims
• This will likely lead to a decrease in the number of “loose” claims going forward

What to keep in mind:
• While claims are going down, the number of patents issued in the US are growing a faster and faster pace each year
• While the rules are getting stricter, the number of opportunities to be sued continue to increase
Other Legislative Risks

- Alice Corp v. CLS Bank
  - The Supreme Court stated that patents directed towards abstract ideas were not entitled to patent protection under Title 35 of the US Code
  - Implementing claims on a computer are insufficient to transform an idea into a patentable invention

- Effects of Alice:
  - A number of computer related patents were challenged and invalidated in the Federal and District courts

- Patent Act (S.1137):
  - Intended amendment to the America Invents act
  - Addresses the disclosure of financial interests and technical detail by the patent holder
  - Bill would require the patent owners to supply specific information on the type and extent of the patent claim before filing in a district court.
Q1 Highlights

- **Revenue**
  - A decrease of $3.6 million in total revenue over Q1 2015 primarily due to a reduction in non-recurring fee related revenue
  - Subscription revenue was up ~$1 million over Q1 2015
  - Additional $10.6 million from eDiscovery services (Inventus)

- **Cost of Revenue**
  - Total COGS increased $12.9 million over Q1 2015 due to the following:
    1. $8.7 million increase in patent amortization expense related to a shorter amortization period (28 vs 42 months) for recently acquitted patents. This is a non-cash expense
    2. $5 million in additional COGS related to the Inventus acquisition

- **Selling, General, & Administrative**
  - $3 million in additional SG&A related to Inventus personnel (nearly double employee count)
  - $3.2 million in one-time expenses related to the Inventus acquisition
## Valuation

<table>
<thead>
<tr>
<th>Metrics</th>
<th>Base Case</th>
<th>Downside Case</th>
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<tbody>
<tr>
<td>Core Subscription Clients</td>
<td>No growth</td>
<td>9% decline per year</td>
</tr>
<tr>
<td>Revenue/Client</td>
<td>$1.6mm (historical avg)</td>
<td>$1.3mm</td>
</tr>
<tr>
<td>Inventus Acquisition</td>
<td>$18mm EBITDA contribution</td>
<td>$9.9mm revenue contribution</td>
</tr>
<tr>
<td>Insurance Clients</td>
<td>41 additional clients/yr</td>
<td>20 additional clients/yr</td>
</tr>
<tr>
<td>Share Repurchases</td>
<td>$80mm over next 2 years</td>
<td>$40mm over next 2 years</td>
</tr>
</tbody>
</table>

- **Value (Core Business)**: $12.43, $6.95
- **Value (Inventus)**: $2.80, $1.48
- **Combined Value**: $15.24, $8.43
## Valuation – Return Sensitivity

### Sensitivity (Base Assumptions)

<table>
<thead>
<tr>
<th>WACC</th>
<th>Inventus Multiple</th>
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<tbody>
<tr>
<td></td>
<td>6.00x</td>
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<tr>
<td>7%</td>
<td>17.56</td>
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<tr>
<td>8%</td>
<td>15.70</td>
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<tr>
<td>9%</td>
<td>14.29</td>
</tr>
<tr>
<td>11%</td>
<td>12.31</td>
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</table>

### Sensitivity (Downside Assumptions)

<table>
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<tr>
<th>WACC</th>
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</thead>
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<tr>
<td></td>
<td>6.00x</td>
</tr>
<tr>
<td>7%</td>
<td>9.46</td>
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<tr>
<td>8%</td>
<td>8.60</td>
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<tr>
<td>9%</td>
<td>7.95</td>
</tr>
<tr>
<td>10%</td>
<td>7.44</td>
</tr>
<tr>
<td>11%</td>
<td>7.03</td>
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Summary of Investment & Recommendation

- RPXC’s equity value has depreciated significantly over the past 1.5 years due to concerns around the growth prospects of the core business, issues around management’s inability and unwillingness to create shareholder value and what some consider to be an expensive and failed acquisition.

- We believe that some of these concerns are valid to a certain extent, but have a differentiated view that leads us to believe that RPXC is trading significantly below its fair value:
  - Mangrove Partners, a well-regarded value-oriented hedge fund, has gone to lengths to force management to create shareholder value to regain some of its lost ground.
  - The Inventus acquisition is being significantly undervalued by the market (4.5x EBITDA), which we believe is well below market value for a company with similar cash flows and growth prospects (and potential cross-selling opportunities).
  - RPX trades at 5.7x 2015 EBITDA and ≈4.5x 2015 Pro-Forma EBITDA including the Inventus acquisition

  ◆ We believe a company of RPX’s nature, despite facing potential legislative headwinds, does not warrant such a low multiple, especially given its robust financial health with cash alone representing >40% of the equity value.

Recommendation:

We recommend a “Hold” to the investment committee for reasons outlined above and in previous slides.
Potential Due Diligence Triggers/Stree Expectations

- **Barclays:**
  - Q2: $81-$82mm in subscription fee and discovery-related revenue
  - $0mm from fee-related revenue, although $3mm in FY16
  - FY revenue contributions of $61-$64mm from Inventus
  - Expecting EBIT margins to decrease ≈12% (seems unnecessarily bearish)

- **Cowen & Company:**
  - 2016E: $339mm rev/$0.71 EPS
  - 2017E: $375mm rev/$1.08 EPS
  - 2018E: $399mm rev/$1.37 EPS

- **Due Diligence Triggers:**
  - Regulation on patent trolls and general patent legislation dynamics (Innovation Act, America Invents Act, Patent Act)
  - Negative news about Inventus’ integration into RPX
  - Severe earnings misses
  - Client acquisition and churn of core subscription business
  - Mangrove Partners’ actions and management’s responses