

## **BUSINESS METHOD PATENTS: PROTECTING INVENTIONS OF SERVICE BUSINESS CLIENTS**

*By Michael Lasky and Peter H. Berge*

Traditionally, patents have been thought to be the province of engineers working with greasy gears and scientists with test tubes. Patentable inventions were thought to be “things” not “ways of doing business” or “marketing concepts.” The question was whether such matters were in fact “inventions” within the scope of the patent statute, 35 U.S.C. §101. While the United States Supreme Court had previously held, in *Diamond v. Chakrabarty*,<sup>1</sup> that “anything under the sun that is made by man”<sup>2</sup> was patentable, doubt remained. There is no doubt any more. Business methods are patentable and many business lawyers’ clients, particularly those with service businesses, may now be eligible to protect their business processes with patents. Under the circumstances, a good business lawyer should be advising her clients to file business method patents.

### **SCOPE OF PATENT ACT**

The language of the Patent Act that *Chakrabarty* interpreted did not seem inconclusive on its face. The Patent Act requires issuance of a patent to:

Whoever invents or discovers any *new and useful process*, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent therefore, subject to the conditions and requirements of this title.<sup>3</sup>

Two judicially created exceptions, however, cast significant doubt on

the true breadth of patentability seemingly announced in *Chakrabarty*. The first was the “business methods exception” and the second was the “mathematical algorithm exception.”

The first assault on the exceptions was in the area of software patents. In the 1970s there was a general reluctance to allow patents for software on grounds that they were mere mathematical algorithms. Since algorithms were merely abstract statements of mathematical truths, so the logic went, they were more akin to discoveries than “useful” inventions.<sup>4</sup> Therefore, they were not patentable inventions under United States law.<sup>5</sup> The commissioner of the Patent and Trademark Office (PTO) at the time, Sidney A. Diamond, vigorously argued that software programs were akin to principles of nature and thus could never be patented. On his side were a number of medium-sized software developers who were vehemently opposed to patenting of software, not because of the laws of nature argument, but because software patents would limit their freedom to adopt concepts from other companies.

In *Diamond v. Diehr*<sup>6</sup> the United States Supreme Court dismissed Commissioner Diamond’s interpretation and ordered the PTO to issue patents for software. Despite the *Diehr* case, many companies stayed on the sidelines thinking that software patents would be short-lived. The opposite has happened. Judicial and administrative changes since *Diehr* have made obtaining such patents easier and any doubt as to the viability of software patents was dismissed by the Federal Circuit in *In re Alapat*,<sup>7</sup> Now over 20,000 software patents are granted each year, comprising about 15 percent of all patents.<sup>8</sup>

The upshot of this trend was that software companies who invested in patents, such as Microsoft and Dell, found themselves owning valuable technology real estate. Those who ignored software patents — whether from lethargy, lack of knowledge, or the vain hope that Congress would overturn them — lost out on a valuable opportunity.

While it became clear that software was patentable, the general “business methods exception” remained until the PTO was presented with the application for U.S. Patent No. 5,193,056. The patent application involved software by which mutual funds pooled assets in an investment portfolio in a hub and spoke structure. Plaintiffs argued that the patent was improperly granted by the Patent Office because it was a mere method of doing business and lacked the statutory basis to be covered by a patent. In the case of *State Street Bank & Trust Co. v Signature Financial Group, Inc.*<sup>9</sup> the Federal Circuit held the patent grant to be valid. In its reasoning, the Federal Circuit reviewed its past

tests for patentability and struck down the business methods exception. It established a new liberal test holding that business methods are patentable like any other methods as long as they meet other indicia of patentability. Thus, a business method which has utility, is new or novel, and is not obvious is patentable by the inventor.<sup>10</sup>

### **METHOD PATENTS & LITIGATION**

The apparent demise of the business methods exception opened the gates, and before long, the Gold Rush was on. For example:

- After conducting an exhaustive examination process, the PTO issued Amazon.com a patent for its “one-click shopping”: U.S. Patent No. 5,960,411.
- Every time an airplane flies with an empty seat, it loses a revenue opportunity. But if an airline lowers its price to fill seats, it risks lowering total revenue. So why not pass those empty seats over to a third party who will auction them off, but not reveal the airline’s name or departure time until after the sale is complete? This is the business model of Priceline.com: U.S. Patent No. 5,897,620.

Other examples include:

- A method comparing the browsing and buying habits of customers to provide suggested purchases for a current customer received Patent Nos. 6,912,505 and 6,853,982.
- An “integrated interface for vendor/product-oriented Internet Web sites” or online “shopping cart” was awarded U.S. Patent No. 5,895,454.
- In the realm of online dating, a “method and system for identifying people who are likely to have a successful relationship” submitted by *eHarmony.com* was granted U.S. Patent No. 6,735,568
- Patent is pending for a method by which an ATM machine issues a disposable one-time password to enable customers to use public computers (*e.g.*, at an Internet cafe) to access their accounts online without risk of password theft.

Although the Supreme Court has yet to take a position on such patent grants, it has had ample opportunity to do so and has declined. That business method patents are viable and being granted by the PTO is now without serious question. The remaining question, when advising

clients, is what is the value of such a patent. The value is considerable, judging from the business practices and litigation that has arisen in the wake of the *State Street Bank* decision and the PTO's issuance of business method patents.

Within a month of the PTO's issuance of the "one-click" patent to Amazon.com, Amazon.com sued BarnesandNoble.com for infringement.<sup>11</sup> At the height of the Christmas shopping season, Amazon.com obtained a preliminary injunction shutting down BarnesandNoble.com's "Express Lane" checkout system on its Web site for nearly a year.<sup>12</sup> BarnesandNoble.com quickly changed its "Express Lane" from a one-click to a two-click system after the injunction was issued. Since each click required raises the potential of the buyer abandoning the purchase, enforcement of the "click patent" has been widely recognized as a significant business advantage for Amazon.com. The parties ultimately settled the case without disclosing the terms of the settlement.<sup>13</sup> Perhaps the one-click patent could have been invalidated as being "obvious" (though all business method patents seem obvious in retrospect), but the power of such patents to affect competitive strategies is clearly evident.

Priceline.com brought suit against Microsoft Corporation for its implementation of a reverse auction scheme in its Expedia online travel service. The case was settled. Terms of the settlement were not disclosed except that Microsoft agreed to license the business method from Priceline.com.<sup>14</sup> Here again, without the patent document, Microsoft clearly would have never taken a license.

The Priceline.com example is particularly instructive on the power and potential of business method patents. It was developed by Walker Digital Management, LLC, started by a former patent lawyer. Walker Labs' business model is to develop business methods and patent them. Its R&D department consists of patent lawyers and they have reportedly filed over 200 patents, including that for Priceline.com.<sup>15</sup>

## **PRACTICAL IMPLICATIONS**

Software patents protect a novel series of steps performed on a computer to achieve a useful result. Business method patents cover a novel series of steps that need not be performed on a machine to achieve a useful result. Thus while the intellectual leap from greasy mechanical devices to business methods is huge in defining what is a patentable "invention," with the intervening step of software patents, patents for business methods are not such an outlandish idea.

There is also good reason why Congress is loath to act against business

method patents. Over the last 30 years, the U.S. economy, for better or worse, has changed from one of making stuff (the realm of the traditional greasy gear patent) to selling other people's stuff. As our economy has changed, intellectual property has changed and so there is a real need for business method patents. Furthermore, Congress did act to create a very limited safe harbor provision for prior users of certain business methods,<sup>16</sup> so that pressure on Congress to legislate over the *State Street* decision has largely dissipated,

Most business lawyers now represent many clients that are in service industries (*i.e.*, they sell other people's stuff or provide services to others). For such clients, intellectual property has always been important, but until recently the only forms that concerned them were trademarks, trade secrets, or copyrights. With the advent of business method patents, however, the business lawyer must add these to the list of concerns when advising businesses. Those clients who are clever about *how* they market their services have a reasonable chance of owning their original marketing techniques. Those thinking about implementing the clever marketing ideas of others may run the risk of an infringement suit if a business method patent covers the idea.

Lawyers need not become experts on patent law to adequately advise their clients concerning business method patents, *but because there is a short statutory time period for filing, a minimum competency*, at least sufficient to refer the issue out, is essential. Lawyers should, however, be familiar with the following in order to guide their clients through this new legal thicket:

- A potentially patentable business method can be any novel and non-obvious series of steps which obtain a “useful, tangible, and concrete result,” even if it is simply a financial transaction or other abstract business method.
- Any business method that uses computers will almost certainly meet the test of patentability. Because e-commerce necessarily requires computers, business methods for e-commerce are almost universally patentable.
- Business method patents can deter competitors and create a valuable intellectual property resource for the company owning the patent.
- Clients must act quickly to obtain patents. The patent must be applied for within one year of certain triggering events (first public use, offering for sale, sale or publication).<sup>17</sup> The trigger date for this year is tricky to calculate so urgency is the best

policy; once the statutory date has passed, there is no recovery.

- If funding is an issue, a business may resort to filing a *provisional* patent application initially because of the lower cost and effort needed to file, but provisional applications, to have a *real and effective* filing date, must meet all requirements of the patent statute for regular patents.
- Company policy and employment contracts should make clear that all inventions are assigned to the company.

With an understanding of the basic principles about business method patents, business lawyers can more fully inform their clients of a valuable new source of intellectual property. Protecting those rights will add value and may provide a competitive edge for the client. Failing to protect them or failing to seek a patent within the one-year limitation may leave the client vulnerable to competitors in the market and in a weak position in any subsequent litigation over the idea. It behooves any reasonable business lawyer to become well-aquainted with the benefits of business method patents.

#### NOTES

1. *447 U.S. 303 (1981)*.
2. *Id. at 309 (method for genetically engineering a bacterium capable of breaking down crude oil held patentable)*.
3. *35 U.S.C. §101*.
4. *The question is one of “patentable subject matter.” The sorts of processes, machines, manufactures, compositions of matter and improvements upon them that are eligible for patents under 28 U.S.C. §101 do not include such things as music, photographs, phenomena of nature, basic mathematical and physical relationships, or mental process.*
5. See *Gottschalk v Benson, 409 U.S. 63 (1972)*. *They were not without protection; the Federal Copyright Act was amended by Congress to add protection for software. See H. Rpt. No. 94-1476 (1976) and P.L. 96-517 (94 Stat 3028)*.
6. *450 U.S. 175 (1981)*.
7. *33 F.3d 1526 (Fed. Cir. 1994)*.
8. *Lessig, Lawrence, The Future of Ideas: The Fate of the Commons in a Connected World, at 319. New York: Random House, 2001. By*

*Lessig's count, of 154,434 patents issued in 1999, approximately 21,000 were software patents.*

9. *State Street Bank & Trust Co. v Signature Financial Group, Inc.*, 149 F.3d 1368 (Fed.Cir.1998)(concerning U.S. Patent 5,193,056). See also *AT&T Corporation v. Excel Communications, Inc.*, 50 U.S.P.Q. 2d 1447 (Fed. Cir. 1999) (upholding State Street Bank).

10. *State Street Bank*, supra n. 9, at 1376.

11. *Amazon.com, Inc. v BarnesandNoble.com, Inc.*, 73 F.Supp.2d 500 (W.D. Wash. 1999).

12. *Id.* The ruling was ultimately reversed on appeal and returned to the district court for a full hearing on the merits, 239 F.3d 1343 (Fed. Cir. 2001).

13. <http://archives.cnn.com/2002/TECH/industry/03/08/amazon.bn.dispute.idg/> (last visited 08/31/05).

14. <http://www.internetnews.com/ec-news/article.php/555711> (last visited 08/31/05).

15. [http://www.walkerdigital.com/about\\_wwd.htm](http://www.walkerdigital.com/about_wwd.htm) (last visited 08/31/05).

16. American Inventors Protection Act of 1999, *Pub. L. No. 106-113*, 113 Stat. 1501 (1999) codified in scattered section of 35 U.S.C., most particularly §273.

17. 35 U.S.C. §102(b).

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