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Patent Law Pending

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The U.S. Court of Appeals for the Federal Circuit redefined the margins of patent eligibility in *State Street Bank & Trust Co. v. Signature Financial Group Inc.* in 1998. The effect was to boost patent protection for business methods, such as financial models, contract provisions, insurance policy features, computer-related inventions and Internet startups.

There were unintended effects, too. The U.S. Patent and Trademark Office was deluged with new patent applications and had few examiners with the expertise to handle them. Four Supreme Court justices have bemoaned the precedent, calling it vague and contrary. And several financial-services companies, frequent targets of the business-method-patent holder, have run up millions and in some cases billions of dollars in royalties and damages.

After a decade of disagreement over the precedent's bearing on American innovation, the Federal Circuit decided Feb. 15 to revisit *State Street* through the lens of another case, *In re Bilski*, which lifts *State Street's* holding on business methods and attempts to carry it further.

In a rare move, the court scheduled an en banc hearing without prompting by the parties in the case. The hearing is set for May 8.

"Every court has a responsibility to try to clarify, and when necessary, modify its own precedent," says Chief Judge Paul Michel of the Federal Circuit. "In the 10 years since the *State Street* Bank decision, there hasn't been much clarification by our court, and the rationale given was so terse as to be not very illuminating."

'ANYTHING UNDER THE SUN'

Until 1998, patent lawyers had lived by the words of Chief Justice Warren Burger, who, borrowing a phrase uttered by a legislative aide in the 1950s, famously wrote that Congress intended the patent's reach to "include anything under the sun that is made by man."

State Street, then, reached for the stars. The opinion, authored by Judge Giles Rich, one of the architects of the Patent Act of 1952, was based on the thinking that the patent system should be as much an incubator for business innovation as for technological innovation.

Critics say the precedent worked to the opposite effect by overburdening the Patent Office. Applications for business method patents have increased by an average of 1,000 a year since 2005, according to the Patent Office. In 2007, the office received 11,378 application filings and issued 1,330 business method patents.

Wynn Coggins, the director of the business methods area in the U.S. Patent and Trademark Office, says the number of examiners working on financial-services-related filings doubled from 30 to 60 last year, and the staff is expected to double again this year. Patent examiners are required to hold science or engineering degrees, not MBAs. The

business method section is conspicuously short on examiners with financial backgrounds. Coggins says the Patent Office has a proposal pending in the Office of Management and Budget that would allow her to hire candidates with advanced degrees in business to vet business method applications.

James Myers, a partner in the D.C. office of Ropes & Gray, the firm that represented *State Street* Bank, says *State Street* created steep costs to financial-services companies. “Business method patents are disproportionately important because of the high-dollar stakes that come with their enforcement and licensing,” Myers says. “Patent damages and patent royalties sought often exceed \$100 million — and even sometimes over \$1 billion.”

Supporters say business method patents protect American innovation, especially on the Internet, where ideas are poached almost inevitably. “A big part of the American economy is that we’re innovative on the Internet, and we have patents to protect it,” says Charles Macedo, a partner at Amster Rothstein & Ebenstein in New York.

Macedo says that Rich, who in the 1950s co-authored the first full revision to U.S. patent law in more than 100 years, recognized in 1998 that the Internet would require new protections for inventors.

“That’s why *State Street* was such an amazing thing in patent law,” Macedo says. “You have the leading patent lawyer of many generations saying business methods are patentable.”

In the *State Street* decision, the court held that patent eligibility turned on whether an invention “produces a useful, concrete and tangible result.” That meant that Signature Financial Group’s data-processing system, which makes a daily calculation of assets of two or more mutual funds invested in a partnership portfolio, was indeed patentable, even though it constituted a method of doing business and not an invention in the mode of Alexander Graham Bell (or perhaps Elisha Gray?). A key feature of the method, the court noted, was the use of a machine to calculate the figures.

In re Bilski, patent lawyers say, is far more brazen, eschewing the link between method and machine. Bernard Bilski and Rand Warsaw filed their patent application in April 1997 for “a method for managing the consumption risk costs of a commodity sold by a commodity provider.” Put simply, it’s a novel hedging method. The Patent Office rejected the application on the grounds that the method lacked an apparatus to perform the functions described and failed to show the transformation of physical subject matter. Thus, the Patent Office board ruled, it flunked *State Street*’s “useful, concrete and tangible result” test.

Bilski appealed, setting up oral arguments before Judges William Bryson and Kimberly Moore and Senior Judge Raymond Clevenger III last October. His lawyer, David Hanson of the Webb Law Firm in Pittsburgh, argued that the method involved a series of physical steps requiring communication and negotiation. Rather than issue a ruling, the court voted to hear the case en banc.

In a telephone interview, Hanson says the en banc hearing “is probably a good step for my client” because it will allow the court to give the case a full airing.

Lawyers and patent officials predict that the court will use the opportunity to carve out boundaries in business method patents, rather than repeal them. “Either way it goes, it’s not going to mean the end of business method patents,” says John Love, deputy commissioner for patent examination policy in the Patent Office.

HEAT FROM ABOVE

Michel of the Federal Circuit declined to discuss what prompted the vote for a full-court hearing. It was discussed during the court’s monthly executive meeting, he says, and at least seven of the 12 judges on the court favored a hearing en banc.

Several patent lawyers said the decision was a response to recent rulings in the court that lacked definition on the issue of whether business methods require technology for patent eligibility.

But James Lampert, a partner in Wilmer Cutler Pickering Hale and Dorr's Boston office, says the Supreme Court's messages to the Federal Circuit have been unambiguous.

"The Federal Circuit is listening to the Supreme Court," Lampert says. "They are listening."

Justice Anthony Kennedy has called into question "the potential vagueness and suspect validity" of business method patents. Justice Stephen Breyer, joined in a 2006 dissent by Justices David Souter and John Paul Stevens, was more cutting: "[*State Street*] does say that a process is patentable if it produces a 'useful, concrete and tangible result.' . . . But this Court has never made such a statement and, if taken literally, the statement would cover instances where this court has held the contrary."

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