An Introduction to Business Method Patents

Puja Karki

Wipro Infotech, Thapar House
124, Janpath, New Delhi 110 001

The case of State Street Bank vs Signature Financial Group, Inc kicked up fresh debates on business method patents and their desirability. For some the definition of these patents is vague and open to interpretation, and the patents are impracticable. For others these patents are royalty and share price earning assets and a necessity to survive in the competitive market place. The article provides an introduction to the issue and the debate.

Not many know what is a business process patent or what it can do, but the general reaction is to procure as many as possible (see Tables 1 and 2). In the history of Internet there is an equivalent to this mass activity, in the race to register all possible portal or site names. This might have yielded rewards for some, in the absence of clear-cut cyber laws, but many cyber squatters are now being dragged to the court. Expecting a similar turn of the events, organizations and people are rushing to obtain patents before competitors do. And the general idea is that a business patent is one that covers any method of using existing technology, such as the Internet, in some unique manner.1

Business method patent for bookkeeping was denied in 1908 case of Hotel Security Checking Co vs Lorraine Co2. From 1908 until now methods of doing business were not considered patentable. But on 23 July 1998, a three judge panel of the USA Court of Appeals for the Federal Circuit, definitively ruled that there is no business method exception to the patent laws, and that the business methods are subject to the same legal standards as any other process or method.2 The growth in the use of computer technology in business decided that business methods should enjoy patent protection, even if they do not involve computers.3 This case established the precedent that even "abstract ideas constituting disembod-

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ied concepts or truths” could be patented. The case is considered a landmark because business method patents are not even sketchable, like the inventions of the phonograph or the telephone.

Case Study

State Street Bank vs Signature Financial Group, Inc.

State Street Bank and Signature Financial are companies that act as administrators and accounting agents of mutual funds. Signature Financial owns US Patent No. 5,193,056 entitled “Data processing system for hub and spoke financial services configuration.” The invention in question is related to a financial investment vehicle, which Signature Financial called a “Hub and Spoke” configuration. A Hub and Spoke arrangement is an investment structure whereby mutual funds (the “spokes” in the configuration) pool their assets in an investment portfolio (the “hub”) organized as a partnership. Enabling mutual funds to pool their assets in this manner provides for economies of scale with regard to the costs of fund administration and has beneficial tax consequences.

This complex financial structure, however, creates its own set of administrative challenges. Administering this structure requires a daily allocation of income, capital gains, and expenses or investment losses. The daily allocations are made on the basis of the Spoke funds’ percentage share in the total assets of the Hub portfolio.

Signature’s invention was directed to a data processing system for administering this Hub and Spoke configuration. The system is operated by means of a personal computer, software capable of performing the various functions described in the claims and detailed in the preferred embodiment and flowcharts, data storage means such as a floppy disk, and display means such as printed output and a computer screen.

Signature informed State Street that any data processing system designed to perform book accounting for a multi-tiered fund arranged in a Hub and Spoke configuration was likely to infringe the patent. State Street subsequently negotiated with Signature for a licence for its patented data processing system. When negotiations broke down, State Street brought an action in district court seeking to invalidate Signature’s patent on the basis that it covered subject matter that should not be capable of being

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of applications (approximate)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>900</td>
</tr>
<tr>
<td>1998</td>
<td>1300</td>
</tr>
<tr>
<td>1999</td>
<td>2700</td>
</tr>
<tr>
<td>2000 (estimate based on first quarter)</td>
<td>6000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of patents granted (approximate)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>110</td>
</tr>
<tr>
<td>1996</td>
<td>160</td>
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<td>1997</td>
<td>240</td>
</tr>
<tr>
<td>1998</td>
<td>490</td>
</tr>
<tr>
<td>1999</td>
<td>705</td>
</tr>
</tbody>
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patented. The district court held that the patent was invalid because it was directed to a business method. But the story is not over yet: The appeals court later held that a “business method” exception was not a reason that could be used to invalidate a patent.

Benefits of Business Method Patents

The frenzied pace of technological innovation and an extremely competitive Internet marketplace are behind this surge in applications for business method patents which range from miscellaneous finance patents and patents on accounting and management system to patents on method of funding college tuition.

Dozens of software developers and dot.com executives could be developing similar business methods simultaneously, so securing a patent can be the key to survival. Business method patents provide a competitive advantage in today’s over-crowded marketplace. They also act as differentiating factors where services are easy to copy.

Not only do patents act as assets on a company’s balance sheet but also result in shoot­ing up of the company’s stock prices, thus appearing to be more desirable to investors. Geoworks more than doubled its stock price after it announced it held a patent on a core wireless application protocol (WAP) technology. As Greg Maier, a patent lawyer and chairman of the American Bar Association’s Intellectual Property Section, says, start-ups that are looking to fund themselves need proof that they have assets or they have something that will endure. At the same
time, every big industry is moving to use the Web. They all realized that they have to use patents as a defense mechanism and to boost their portfolio.

Patents can be a steady source of income as patent ownership affords a 20-year sanctioned monopoly, granting the right to market a technology or charge royalty for its use. In exchange, the patent owner must fully disclose how the invention was made. In 1998, revenues in the United States for patent licences generated more than $100 billion. IBM holds more patents than any other company and it alone took in more than $1 billion from licensing. IBM holds more patents than any other company and it alone took in more than $1 billion from licensing.

Organizations should opt for business method patents, to avoid being slapped with infringement suits from others, who might have discovered the process later but were quicker at patenting it. In such cases the companies have to pay licensing fees or go to court. Both of these are expensive propositions (see Table 3 for information on litigation history). Litigation costs can soar past $1 million for each side when a relatively simple patent is in dispute, legal experts say. The more complex the patent, the higher the price tag.

The Debate

On one hand, according to the article 52 (2) European Patent Convention, methods of doing business mathematical methods, presentations of information and programs for computer shall not be regarded as inventions, while European patent is to be
granted to inventions (though a product or a method which has a technical character may be patentable)\(^\text{11}\). On the other hand, examiners at the U.S. Patent and Trademark Office are swamped with applications for business method patents, which doubled last year to nearly 2,700\(^\text{4}\) (see Table 4 depicting the spate of articles on the issue). This year’s total could reach 6,000.

This debate over the desirability of business method patents has been complicated by misconceptions about these, like these being easily identified as a group thus requiring special handling. In reality these are indistinguishable from many other types of inventions and hence pass the same test of patentability.

What is doubtful is the actual need for a patent protection in all the cases. Most of the patents cover an impractical large area. Consider U.S. Patent 6,085,231, filed in January 1998 and granted to AT&T Communications: “A method and system of delivering a voice mail message via an e-mail address.” The telecommunications giant now has the patent for a system that appears to cover a core concept for a number of Internet companies. In another case Massachusetts-based Open Market has been granted several patents that, some claim, could potentially allow it to demand royalties from almost any company engaged in e-commerce. These include a patent on a secure, real-time payment method using debit and credit cards, one covering electronic shopping carts, and another on a technique for analysing how users browse Web content. In a similar context Sightsound.com, which claims to have been granted a patent that covers the sale of any digital audio or video recording over the Internet, is currently suing N2K, a company that retails music on the Web. The Mt. Lebanon, Pa., company has also written to a number of other prominent music sites demanding royalties on every sale that involves downloading music to a customer\(^7\).

Any one who applies for the patent first, gets it. According to Greg Aharonian\(^4\), a consultant who runs a patent news service and revels in researching and busting up software patents, there is a cold war going on in the software world. Thus competition forces a cloud of secrecy on development of business methods, this and the lack of documentation in most cases prevents the ascertainment of the method being a work of ‘prior art’. For example, BT has a U.S. patent on hyperlinks, which allow users to click from one Web page to another. But hyperlinks, the technology behind the World Wide Web, was already in use when BT applied for the patent in 1989. Peter Menell, a law professor at the University of California at Berkeley and the author of Intellectual Property in the New Technology Age agrees that there are serious questions about whether business methods should be patentable and questions of the ability of the Patent and Trademark Office to review these patents given the lack of prior art databases\(^3\).

The grant of business monopoly for 20 years to the holder of the patent is another area of concern. In a field like medicine, where a large investment over a large frame of time is required, such a monopoly rewards the patent holder. A comparable investment and subsequently reward is uncalled for in business method patents. Thus a patent for a shorter duration could be the solution\(^1\). Some people are in favour of doing away with
## Table 3—Selection of broad e-commerce patents issued by the US Patent and Trademark Office\textsuperscript{10}

<table>
<thead>
<tr>
<th>Company</th>
<th>US Patent Number</th>
<th>Subject</th>
<th>Update</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amazon.com</td>
<td>5,960,411</td>
<td>One-click purchasing</td>
<td>Amazon.com has used its patent to force changes to Barnes &amp; noble’s web site.</td>
</tr>
<tr>
<td>CyberGold</td>
<td>5,794,210</td>
<td>Attention brokerage</td>
<td>Patent covers rewarding web surfers for paying attention to online advertisements.</td>
</tr>
<tr>
<td>Netcentives</td>
<td>5,774,870</td>
<td>Online incentives</td>
<td>One of several recently issued patents covering reward systems for internet purchasing.</td>
</tr>
<tr>
<td>Open Market</td>
<td>5,715,314</td>
<td>Electronic shopping carts</td>
<td>This patent may be infringed by many e-commerce sites on the internet.</td>
</tr>
<tr>
<td>Priceline.com</td>
<td>5,794,207</td>
<td>Buyer driven sales</td>
<td>Priceline has sued Microsoft and its Expedia travel site for copying its patented business method.</td>
</tr>
<tr>
<td>Sightsound.com</td>
<td>5,191,573</td>
<td>Music downloads</td>
<td>Sightsound is demanding a 1% royalty from all online music sellers</td>
</tr>
<tr>
<td>E-data</td>
<td>4,528,643</td>
<td>Download based sale</td>
<td>A judge blocked E-data’s attempts to enforce this pre-Internet era patent.</td>
</tr>
</tbody>
</table>

These patents altogether as these seem to be contrary to the idea of a free net-society, where the source codes are public for all to enhance and enrich.

## Conclusion

The granting of the business method patents has been accepted to be essential. The debate is on its definition, demand and duration. Thus the need is to define through business method patent laws, framed under the purview of patent laws, the methods which can be patented. The demand defines need for the business process patents in a field which has already advanced by decades into the Internet age, and its ability to financially sustain it. This would obviously include the introduction of complex systems for tracking the claims on issues like ‘prior art’. Patent and trademark office can be provided with the right resources and technology to work in this direction.
Table 4 — Business method patents in the news

- January 12, 1999, Bloomberg News, in NYT, ‘Court declines to review ruling seen as software boon’
- February 1998, ‘Patents for banks and financiers’. From Banking Law, February 1998 Number 105. This is an Australian publication. “Patents are relevant not just to high technology companies. Banks and financial institutions, as developers and users of technology, are discovering that patents apply to their businesses too.”

The duration for which the patent is valid settles many issues of the debate. Though this element could be the most complex as the effect of duration of a patent is guided by the content of the payment and also by the speed of changes on the Internet. With concrete laws and information dissemination in this field, the debate over the issue will conclude but it is unwise to be passive spectators, waiting for the dust to settle on the issue.

References

1 Malhotra Deepak, Software patents, Siliconindia, July 2000, 74-76
5 Wong May, Internet boom boosts rush for high-tech, Popular Science, 12 July