

Federal Circuit Raises The Bar For Business Method Patents

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The United States Court of Appeals for the Federal Circuit issued a decision on October 30, 2008 in a closely watched case on the patentability of processes under Section 101 of the Patent Act.¹ Chief Judge Michel's en banc majority opinion in the *Bilski* case adopted a more stringent test for the patentability of processes and affirmed the Patent Office's rejection of patent claims on a method of hedging risks for trading commodities. Relying on a series of 1972-1981 Supreme Court cases, the court defined the proper test as requiring that a process either be "tied to a particular machine" or "transform[] a particular article into a different state or thing." Processes that do not meet this test will no longer be patentable under Section 101.

Because *Bilski* impacts the patentability of many kinds of processes, including business methods, it generated interest from a wide spectrum of companies, trade groups, and professional associations. Almost 40 groups filed *amicus* briefs, ranging from the American Civil Liberties Union and the Electronic Frontier Foundation to IBM, Yahoo!, and Eli Lilly.

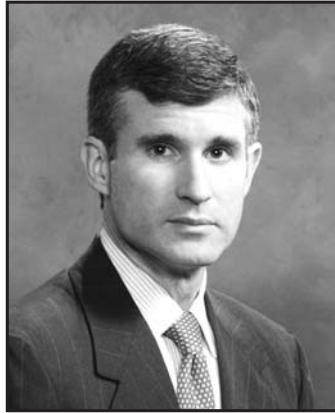
Background

The Federal Circuit's decision in *State Street* a decade ago clarified that business methods are "subject to the same legal requirements for patentability as applied to any other process or method."² That decision released a flood of patent applications for methods of doing business. *State Street* concerned a data processing system with an investment structure for mutual funds to pool their assets within a portfolio. The Federal Circuit upheld the patentability of the financial method, holding that the "useful, concrete and tangible result" produced by the method "renders it statutory subject matter...."³ Over the past decade, *State Street*'s "useful, concrete and tangible result" test has proved to be a low bar for business methods.

Bilski

The dispute in *Bilski* stemmed from Bilski's patent application for a method of hedging risk in the field of commodities trading. The Patent Office rejected Bilski's patent claims because they (1) did not involve the transformation of a physical subject matter, (2) did not

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describe an apparatus to perform the claimed functions, (3) were directed to an "abstract idea," and (4) failed to recite a "'practical application' or produce a 'concrete and tangible result'" under the *State Street* test.⁴

Majority Opinion

In the majority opinion, the court held that Bilski's hedging method was not eligible for patent protection because it was not "tied to a specific machine" and did not "transform a particular article to a different state or thing." This test is referred to as the "machine-or-transformation" test.

The court started its analysis with the statute, 35 U.S.C. § 101:

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 therefor, subject to the conditions and requirements of this title.⁵

The first question in *Bilski* was how to determine what is a "new and useful process" under Section 101. The court focused on a 1981 Supreme Court decision, *Diamond v. Diehr*, that held that a claim is not patentable if it claims "laws of nature, natural phenomena, [or] abstract ideas."⁶ The *Bilski* court explained that these "fundamental principles" are "part of the storehouse of knowledge of all men . . . free to all men and reserved exclusively to none."⁷

The second question was whether Bilski's claim "recites a fundamental principle and, if so, whether it would [impermissibly] pre-empt substantially all uses of that fundamental principle if allowed."⁸ To answer that question, the court found that the Supreme Court has outlined a test to determine whether a process claim preempts a fundamental principle or covers only a particular application of the principle. The court held that the Supreme Court's machine-or-transformation test is the "only applicable test" to determine whether a process is patentable.⁹

Importantly, the court explained that merely reciting some machine or some transformation in a patent claim is insufficient. Instead, "the use of a specific machine or transformation of an article must impose meaningful limits on the

claim's scope" and "not merely be insignificant extra-solution activity."¹⁰ The court left to another day "whether or when recitation of a computer suffices to tie a process claim to a particular machine."¹¹ However, the Supreme Court rejected a claim on a process of converting data to binary format using "an algorithm programmed onto a digital computer."¹² Reciting a digital computer was not enough to save the claim because "the claim's tie to a digital computer did not reduce the pre-emptive footprint of the claim since all uses of the algorithm were still covered by the claim."¹³ Thus, it appears that reciting generic computer hardware will not satisfy the requirement for a "specific machine" that imposes "meaningful limits" on the scope of the patent claim.

On the transformation part of the test, the court explained that the transformation of an article into a different state or thing "must be central to the purpose of the claimed process."¹⁴ The "article" that is being transformed is also key to patentability. The court acknowledged that "articles" such as "electronic signals and electronically-manipulated data" are "raw materials of many information-age processes" and may be patent-eligible.¹⁵ For example, processes involving a "visual depiction that represents specific physical objects or substances" or the "electronic transformation of the data itself into a visual depiction" may be patent-eligible.¹⁶ By contrast, legal obligations, legal relationships, and business risks are examples of abstractions that "cannot meet the test because they are not physical objects or substances."¹⁷

The court specifically overruled *State Street*'s "useful, concrete and tangible result" test for patentability as "inadequate" and "insufficient."¹⁸ The court also declined to adopt the "technical arts test" urged by some *amici* that would limit patentable processes to only those that involve the "application of science or mathematics."¹⁹

The majority opinion by Chief Judge Michel was joined by eight of the twelve members of the court. Judge Dyk filed a concurring opinion (joined by Judge Linn). Judges Mayer, Newman, and Rader filed separate dissenting opinions.

Concurring And Dissenting Opinions

Judge Dyk's concurring opinion rejects the notion that "processes for organizing human activity were or ever had been patentable."²⁰ He reports that English practice circa 1793 (when the first U.S. patent act was adopted) and Supreme Court precedent are consistent with the concept that patentable processes are only those "processes for using or creating manufactures, machines, and compositions of matter," i.e., processes "involving other types of patentable subject matter."²¹

Judge Mayer dissented because the majority decision did not go far enough in doing away with business method patents. Signaling that he would have adopted the "technical arts" test, he declared that "[t]he patent system is intended to protect and promote advances in science and technology, not ideas about how to structure commercial

transactions."²²

Judge Newman dissented, stating that the majority's machine-or-transformation test "excludes many of the kinds of inventions that apply today's electronic and photonic technologies, as well as other processes that handle data and information in novel ways."²³ Judge Newman warned that the decision's "impact on the future, as well as on the thousands of patents already granted, is unknown."²⁴ Judge Rader said a new standard was not needed because current law makes it clear that Bilski was not entitled to a patent. Sharing Judge Newman's concern, he also faulted the majority for relying on "Supreme Court opinions dealing with the technology of the past" and lamented that the machine-or-transformation test risks "precluding patent protection for tomorrow's technologies."²⁵

Implications

Applying the *Bilski* test will make it more difficult, but not impossible, to patent business methods. That result will likely be mitigated because the Patent Office already tests for a physical transformation when examining process applications, and patent practitioners will in some cases be able to tailor patent claims to satisfy *Bilski*'s machine-or-transformation test.

Bilski also might lead to more litigation by exposing issued business method patents to more validity attacks. In the past, comparatively few defendants based validity attacks on Section 101. Those attacks will likely increase in the wake of *Bilski*.

Bilski is not the last word on the patentability of business method. The court left the door open for "future developments in technology and the sciences," recognizing that "the Supreme Court may ultimately decide to alter or perhaps even set aside this test to accommodate emerging technologies, [a]nd we certainly do not rule out the possibility that this court may in the future refine or augment the test or how it is applied."²⁶

¹ In re *Bilski*, 545 F.3d 943 (Fed. Cir. 2008).

² *State Street Bank & Trust Co. v. Signature Fin. Group, Inc.*, 149 F.3d 1368, 1375 (Fed. Cir. 1998).

³ Id. at 1375.

⁴ In re *Bilski*, 545 F.3d at 950.

⁵ Id. at 951.

⁶ *Diamond v. Diehr*, 450 U.S. 175, 185 (1981).

⁷ In re *Bilski*, 545 F.3d at 952 (quoting *Funk Bros. Seed Co. v. Kalo Inoculant Co.*, 333 U.S. 127, 130 (1948)).

⁸ Id. at 954.

⁹ Id. at 964.

¹⁰ Id. at 961-62.

¹¹ Id. at 962.

¹² Id. at 953 (discussing *Gottschalk v. Benson*, 409 U.S. 63, 65, 71-72 (1972)).

¹³ Id. at 955.

¹⁴ Id. at 962.

¹⁵ Id. at 962-63.

¹⁶ Id. at 963.

¹⁷ Id. at 962.

¹⁸ Id. at 959-60.

¹⁹ Id. at 960.

²⁰ Id. at 972 (Dyk, J., concurring).

²¹ Id. at 972, 974 (Dyk, J., concurring).

²² Id. at 998 (Mayer, J., dissenting).

²³ Id. at 976 (Newman, J., dissenting).

²⁴ Id.

²⁵ Id. at 1011, 1015 (Rader, J., dissenting).

²⁶ Id. at 956.