Client Alert.

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Business Method Patents Survive *Bilski*

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This morning, the U.S. Supreme Court issued its eagerly awaited decision in *Bilski v. Kappos*. The Court affirmed the Federal Circuit's judgment that Bilski's particular business method for hedging consumption risk was not eligible for a patent. The Court, however, rejected the machine-or-transformation test as the "sole test" for patent eligibility. And the Court expressly stated that the Patent Act does not categorically exclude business methods from patent eligibility. Instead, the Court relied on its previous precedent to reject petitioners' patent as "an unpatentable abstract idea."

By requiring a more flexible approach, the Court's decision may benefit those seeking – or trying to enforce – not just business method patents, but also method patents in a broad range of technologies.

LEGAL BACKGROUND

In recent years, patents have been sought in a wide variety of fields once thought beyond the reach of patent laws, including tax strategies, executive compensation schemes, and dispute resolution. The question of whether methods or processes in these and other areas are eligible for patent protection – especially when not tethered to a physical machine – has become a hotly contested one. Until today's decision in *Bilski*, the Supreme Court had not spoken directly on the issue of patent eligibility in almost 30 years.

The question is one of statutory interpretation. Section 101 of the Patent Act provides that "any new and useful process, machine, manufacture, or composition of matter" may be patentable subject matter. In a trilogy of cases decided decades ago, the Court explained that abstract ideas, laws of nature, and natural phenomena are excluded. For example, in *Gottschalk v. Benson*, 409 U.S. 63 (1972), the Court rejected a method claim on an algorithm, reasoning that "[t]he mathematical formula involved here has no substantial practical application except in connection with a digital computer, which means that if the judgment below is affirmed, the patent would wholly pre-empt the mathematical formula and in practical effect would be a patent on the algorithm itself." *Id.* at 71-72; *see also Parker v. Flook*, 437 U.S. 584, 589-90 (1978). By contrast, in *Diamond v. Diehr*, 450 U.S. 175 (1981), the Court found that a method for "curing" synthetic rubber into molded rubber products using a well-known mathematical formula was not merely an attempt to patent a mathematical formula, and thus was patent eligible. *Id.* at 191-92.

Today's *Bilski* decision represents a return by the Supreme Court to the question of how to interpret and apply Section 101, but this time in a context the Court has not previously addressed: business methods. Lower courts for much of the 20th century rejected business method claims on various grounds, even calling into question whether business methods were ineligible per se. But the Court of Appeals for the Federal Circuit, in its 1998 decision in *State Street Bank v. Signature Financial Group*, "la[id] this ill-conceived [business method] exception to rest," holding that business method claims were instead subject to the same requirements as any other process. 149 F.3d 1368, 1375. *State Street* suggested that a process, including a business method, satisfied Section 101 as long as it produced a "useful, concrete, and tangible result." *Id.*

THE UNDERLYING FACTS AND THE DECISIONS BELOW

In this case, petitioners Bernard Bilski and Rand Warsaw claimed a method that enabled commodities dealers to minimize risk through hedging contracts. But they did not claim a computer or other means for implementing this method. After the Patent Office rejected the claims as patent-ineligible subject matter, they appealed to the Federal Circuit.

In February 2008, before the three-judge panel issued its opinion, the Federal Circuit took the unusual step of sua sponte ordering the case reheard en banc to reconsider the appropriate Section 101 standard for method claims. In its en banc opinion, the Federal Circuit held that a process that is "tied to a particular machine" or that "transforms a particular article into a different state or thing" is patent eligible under Section 101. *In re Bilski*, 545 F.3d 943, 954 (2008) (en banc). In so doing, the Federal Circuit suggested that the "machine-or-transformation test" was the sole test for determining patent eligibility of a process, at least until the Supreme Court or the Federal Circuit "decide[s] to alter or perhaps even set aside this test to accommodate emerging technologies." *Id.* at 956.

The Supreme Court granted certiorari review on June 1, 2009, and heard oral arguments on November 9, 2009.

THE SUPREME COURT'S DECISION

In its June 28, 2010 opinion, the Supreme Court affirmed the Federal Circuit's judgment that petitioners' business method for hedging consumption risk was not eligible for a patent. The Court, however, rejected the Federal Circuit's suggestion that the "machine-or-transformation test" is the only measure of patentability for a process. The Court stated that, while "the machine-or-transformation test is a useful and important clue, an investigative tool, for determining whether some claimed inventions are processes under §101," the Patent Act must not be read so narrowly, especially in the "Information Age."

The Court also stated that the correct interpretation of Section 101 "similarly precludes the broad contention that the term 'process' categorically excludes business methods." The Court reasoned that the use of the term "method" within Section 100(b)'s definition of "process" indicates the inclusion of at least some methods of doing business.

But the Court cautioned against an overly broad reading of its opinion. It stated that its precedents on the unpatentability of abstract ideas provide a useful limiting principle. And it held that petitioners' patent failed for that reason: "[t]he concept of hedging . . . is an unpatentable abstract idea."

Finally, the Court noted that "nothing in today's opinion should be read as endorsing interpretations of §101 that the Court of Appeals for the Federal Circuit has used in the past," citing the *State Street* decision. On the other hand, the Court stated that "we by no means foreclose the Federal Circuit's development of other limiting criteria that further the purposes of the Patent Act and are not inconsistent with its text."

Although the Justices unanimously agreed that petitioners' patent was not eligible to be patented, four Justices would have held all business methods categorically unpatentable. In a long concurrence in the judgment, retiring Justice Stevens reasoned that the "textual, historical, and functional clues" all point to the conclusion that "petitioners' claim is not a 'process' within the meaning of §101 because methods of doing business are not, in themselves, covered by the statute."

IMPLICATIONS OF THE DECISION

The Supreme Court's decision in *Bilski* gives ammunition against invalidity challenges under Section 101 back to patent applicants and holders. This may be particularly the case in prosecutions and litigations concerning new and emerging technologies such as software, e-commerce, information technology, and medical diagnostics. In rejecting the Federal Circuit's machine-or-transformation test as "the sole criterion" for patent eligibility, the Court emphasized the need for a more dynamic approach that could accommodate the "previously unforeseen inventions" of the "Information Age."

Patent Prosecution

While it remains to be seen precisely how *Bilski* will be implemented at the Patent Office, the decision will likely benefit patent applicants because it does not categorically preclude the patenting of business methods. Further, applicants will no longer be limited to showing that their method claims are tied to a particular machine or transformative of a particular article. By leaving open for future development the standards by which an invention may qualify as a patentable "process," the Court has made it more difficult for the Patent Office to rely on bright-line rules for rejecting claims on Section 101 grounds.

Justice Kennedy's opinion also refers twice to the Patent Act's other requirements, *i.e.*, that an invention be "novel," "nonobvious," and "fully and particularly described" under Sections 102, 103, and 112. These references by the Court could be interpreted as a directive to the Patent Office not to rely excessively on Section 101 rejections.

Nonetheless, applicants will want to ensure that their claims are not so abstract as to violate the Court's long-standing prohibition against patenting an abstract idea, law of nature, or mathematical formula. Moreover, as the machine-or-transformation test remains a "useful and important clue" to patent eligibility, applicants may still find it prudent to write claims with an eye toward meeting the test, especially if it does not affect their overall claim-drafting strategies.

Litigation

The Supreme Court's ruling will also impact U.S. patent litigation. The rejection of the Federal Circuit's machine-or-transformation test as the sole test for patent eligibility will make it more difficult for accused infringers to mount Section 101 challenges to method claims. Since the Federal Circuit's en banc decision in 2008, this has become a prevalent defense, and there have been several cases in which district courts invalidated patent claims by relying on the Federal Circuit test. Many of those rulings may now be challenged on appeal or at the district court level.

That said, while the Section 101 standard for patentees will no longer be so restrictive, the exact parameters for when claims run afoul of the prohibition on claiming "laws of nature, physical phenomena, and abstract ideas" remain unclear. Patent owners seeking to enforce their patents in court will undoubtedly want to emphasize that their claims are concrete, specific, and limited in scope, and that they do not preempt any abstract ideas or fundamental principles.

Today's decision may also impact summary judgment decisions. The Federal Circuit has stated that patent eligibility under Section 101 is a question of law, *Bilski*, 545 F.3d at 951, and several recent district court decisions have invalidated patent claims on summary judgment for failure to satisfy the machine-or-transformation test. But the Federal Circuit has also suggested that underlying factual issues can render summary judgment on Section 101 grounds inappropriate. *See, e.g.*, *In re Comiskey*, 554 F.3d 967, 975 (Fed. Cir. 2009). The Supreme Court's *Bilski* decision is silent on the issue of summary judgment. However, by emphasizing that Section 101 calls for a more nuanced approach, the Court's ruling may ultimately aid those litigants seeking to avoid summary judgment.

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