

# INTELLECTUAL PROPERTY

Court issues key business-method patent ruling

To infringe, a single entity must perform all elements of a claim.

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January 21, 2008

Since the 1998 decision by the U.S. Court of Appeals for the Federal Circuit in *State Street Bank & Trust Co. v. Signature Financial Group Inc.*, 149 F.3d 1368 (Fed. Cir. 1998), which legitimized business-method patents, intense debate has taken place between those for and against patents directed to methods of doing business. As that debate raged on, as Congress threatened to take action and as the U.S. Supreme Court justices openly questioned the soundness of the State Street decision, the Federal Circuit addressed the issue from a different perspective. On Sept. 20, 2007, the Federal Circuit issued a decision in *BMC Resources Inc. v. Paymentech L.P.*, 498 F.3d 1373 (Fed. Cir. 2007), that raised important practical questions on how patents can really be used. This one decision dramatically affects who can be liable for patent infringement. The Federal Circuit relieved pressure on the desire to overturn *State Street* and provided additional life to business-method patents. Going forward, business-method patents will have a new emphasis on obtaining and enforcing "proper" claims. *BMC* is a decision that is especially important for those companies that obtain business-method patents.

Business methods, especially those that involve electronic commerce, usually involve more than one person or entity in addition to a customer, who owns or controls the various resources needed to carry out a transaction, such as Web servers and credit clearance houses. Prior to *BMC*, it was not necessary for the acts that constitute infringement of a business-method patent to be performed by only one entity. Multiple entities could be joined together and sued. In *BMC*, the court gutted this practice and held that, in general, a single entity must perform all elements of a patent claim. Although the decision applies to all patents, its effect will be felt the most by those attempting to enforce business-method patents.

The business-method patent, which is nothing more than an ordinary method patent, whose subject matter happens to be business, rose in popularity after the 1998 *State Street* decision. As business-method patents began to proliferate, new segments of the economy that had previously felt immune from the patent system found themselves inundated with patent infringement lawsuits.

In the Supreme Court's June 22, 2006, decision in *Laboratory Corp. v. Metabolite*, 126 S. Ct. 2921 (2006), there were signs that the liberal scope of the business-method patent was being called into question. Justice Stephen G. Breyer

explicitly singled out the Federal Circuit's statement in *State Street* that "a process is patentable if it produces a 'useful, concrete, and tangible result,' " noting that the Supreme Court "never made such a statement and, if taken literally, the statement would cover instances where this Court has held the contrary." *Id.* at 2928. Justice Anthony M. Kennedy, in his concurring opinion in *eBay Inc. v. MercExchange LLC*, 126 S. Ct. 1837 (2006), addressed the business-method patent issue from the viewpoint of when injunctive relief is appropriate. Before waiting for the Supreme Court to take action, the Federal Circuit changed the rules of the game in *BMC* and took the sting out of many business-method patents for potential defendants.

### **Three types of infringement**

To understand how the rules changed, we need to first explain the basics of patent infringement. There are multiple types of patent infringement, but the basic three are direct infringement, contributory infringement and inducement to infringe. Direct infringement requires that the accused infringer make, use, sell or offer to sell all the elements listed in a patent claim. For example, if a claim lists a chair comprising a first leg, a second leg, a third leg and horizontal bracing connected to the first, second and third legs, a company that makes a stool with three legs would be a direct infringer. Contributory infringement would occur when a company knowingly offers to sell, sells or imports a component of an item; when the component constitutes a material part of the invention; and when the component is not a staple article of commerce suitable for substantial non-infringing uses. In this example, a company that supplies special bracing for the patented three-leg stool would be a contributory infringer. Although the legal subtleties can be complex, for the purpose of this discussion, what matters is that contributory infringement still requires there to be a direct infringer.

Inducement to infringe occurs when a party actively induces another entity to directly infringe the patent. Like contributory infringement, inducement to infringe needs a direct infringer. Contributory infringement and inducement to infringe are indirect forms of infringement that require at least two parties: an indirect infringer and a direct infringer.

The indirect and direct infringer are jointly and severally liable among the infringers. A patent holder will want to pick the largest target, or perhaps the patent holder's direct competitor, and sue accordingly.

Let's look at a second example that attempts to use multiple parties to satisfy the role of the direct infringer. Assume that a claim recites a method of selling insurance by applying numerical inputs to a telephone, processing the numerical inputs, connecting the telephone to a second telephone and playing a recorded notice when the second telephone has been answered. Can the telephone company that connects telephones (i.e. processing said numerical inputs, connecting said telephone to a second telephone) be liable for infringement of that claim? Prior to *BMC*, the answer was probably yes. In the 2006 decision in

*On Demand Machine Corp. v. Ingram Industries Inc.*, 442 F.3d 1331, 1344-45 (2006), the Federal Circuit stated that "[w]e discern no flaw" in a jury instruction that stated, "It is not necessary for the acts that constitute infringement to be performed by one person or entity. When infringement results from the participation and combined action(s) of more than one person or entity, they are all joint infringers and jointly liable for patent infringement."

### **Changing direct infringement**

*BMC* was the assignee of two patents that were directed to a method for processing debit transactions without a personal identification number. An interface was provided between a telephone and a debit card network. The method required the combined action of several parties, including the payee's agent, a remote payment network and the card-issuing financial institution. Paymentech, the accused infringer, supplied information to the debit network but not instructions on how to process the information. The Federal Circuit put to rest the concept that the act of direct infringement could be met by multiple parties and reaffirmed that direct infringement occurs only "when a party performs all of the steps of the process." *BMC*, 498 F.3d at 1379. Without a single entity performing all the activity that a patent claim requires, the normal course of action has been to apply the laws of indirect infringement — contributory infringement and inducement to infringe. But the Federal Circuit explained that indirect infringement still requires a finding that some entity has committed "the entire act of direct infringement."

The Federal Circuit did provide for one exception when it stated that a "party cannot avoid infringement, however, simply by contracting out steps of a patented process to another entity." *BMC*, 498 F.3d at 1381. The scope of this exception has been dealt with in two recent cases leading to opposite results. In *Gammino v. Cellico Partnership*, No. 04-4303, 2007 U.S. Dist. Lexis 74201 (E.D. Pa. Oct. 4, 2007), the patent was directed to a method of blocking international calls. The U.S. District Court for the Eastern District of Pennsylvania held that merely purchasing "international call blocking" from local providers did not control how the call blocking was implemented. *Id.* at \*3. The court found that the defendant was not liable for infringement.

In *TGIP Inc. v. AT&T*, No. 2:06-CV-105, 2007 U.S. Dist. Lexis 79919 (E.D. Texas Oct. 29, 2007), the accused infringer, AT&T Inc., was not so lucky. The patent claim required data terminals that were operated by retailers. AT&T countered that it cannot be liable because it did not carry out all the acts the claim requires; others were involved. The evidence, however, showed that the activation work was performed on AT&T's behalf, that AT&T provided the specifications and AT&T defined the "requirements" necessary for AT&T to provide its service to the retailers. Hence, AT&T infringed. *Id.* at \*34.

By changing (or clarifying) the rules of how a patent is infringed, the Federal Circuit has gutted many business-method patents that require multiple parties to

directly infringe. In so doing, the Federal Circuit has provided relief for critics of business-method patents without needing to reverse course on *State Street*.

Business-method patents by definition apply to business settings. This means that they usually involve multiple parties who, together, perform all of the elements of a patent claim. In *BMC*, the claims required four different parties to perform different acts per claim. The Federal Circuit explained what a proper claim is and what it is not. The court noted that the concerns about "arms-length cooperation" as a means to avoid a finding of infringement "can usually be offset by proper claim drafting." *BMC*, 498 F.3d at 1381. The court went on to surmise that a "patentee usually can structure a claim to capture infringement by a single party." *Id.* A "proper" claim thus was seen as one as being performed entirely by a "single party." The court was able to classify these types of claims as "proper" because the court in effect vaporized the possibility of enforcement for multiparty claims — which are now "improper."

### **Some claims must be redrafted**

So what is a "proper claim" in the post-*BMC* era? Here is a simple example of a patent claim on a hypothetical e-commerce business method that might have been written prior to *BMC*: "A method of processing an order for an item comprising: from a server system, sending product information to a customer's terminal; at the customer's terminal, displaying information on the product and sending an order including a payment to the server system; at a transaction processing center, processing the payment by accessing customer account data stored at a financial institution and transmitting an order approval to the customer terminal and server system."

One can see what is wrong with this claim, post-*BMC*. It involves three entities — the server system, the transaction processing center and the financial institution — in addition to the customer (whom the patent owner certainly will not want to sue). Under the *BMC* decision, no single entity directly infringes, since no single entity controls all activity.

A "proper claim" will be written as: "A method of processing an order for an item comprising, at a server system: sending, to a customer terminal, product information to be displayed to the customer; receiving, from the customer terminal, an order including a payment; and thereafter receiving, from a transaction processing center, an order approval obtained from customer account data at a financial institution."

This claim is "proper" because it involves only one entity doing all the infringing activity — the owner of the server system, which likely is also the direct competitor of the patent owner.

On some level, *BMC* gutted the patent portfolios of companies that invested in business-method patents. On the other hand, the change provided relief for

many companies that were faced with lawsuits involving business-method patent with claims that were not "proper." By relieving pressure on the desire to overturn State Street, the Federal Circuit has provided additional life to business-method patents. Going forward, business-method patents will continue and a new emphasis will be placed on obtaining "proper" claims. These new business-method patents will issue and will be enforced. Direct infringers will be easier to identify and the companies on the periphery will be spared.

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