
BUSINESS METHOD PATENTS

HEARING

BEFORE THE
SUBCOMMITTEE ON COURTS, THE INTERNET,
AND INTELLECTUAL PROPERTY
OF THE
COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES
ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

APRIL 4, 2001

Serial No. 5

Printed for the use of the Committee on the Judiciary



Available via the World Wide Web: <http://www.house.gov/judiciary>

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 2001

72-299 DTP

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: (202) 512-1800 Fax: (202) 512-2550
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H521-55

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BUSINESS METHOD PATENTS

Wednesday, April 4, 2001

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COURTS, THE INTERNET,
AND INTELLECTUAL PROPERTY
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2 p.m., in Room 2141, Rayburn House Office Building, Hon. Howard Coble (Chairman of the Subcommittee) presiding.

Mr. COBLE. Good afternoon. The Subcommittee will come to order. Let me tell you folks what we are up against. We are going to have a vote, presumably in about 30 or 45 minutes. The last vote is scheduled to end at 3:30. Now, oftentimes when that final bell rings, we inevitably lose Members. I had hoped to hear from only Howard Berman and me. The gentleman from Virginia, I think, is going to pout if I do not recognize him. I do not want Rick pouting, so I am going to give my opening statement, and then if Mr. Berman is not here, I will recognize the gentleman from Virginia. I would appreciate it if we could keep it brief because I do not want to lose people. I know from past record once that final bell rings, we assume the risk of losing people.

I want to share with you all a conversation that occurred when the Congress was fiercely debating patent reform some recent years ago. A reporter called me from San Francisco and he said, "I have been covering the law of patents for 13 years." He said, "It is the most dull, boring, esoteric area of the law until now." He said that because we were fighting every day on the floor, Republicans fighting Republicans, Democrats fighting Democrats. This reporter could smell blood.

Well, I think the law of patents and trademark and copyright is no longer dull. It has become exciting. Now, sometimes, excitement may exceed reality, and in some areas, I think that is where we come into play, to examine it very carefully and hopefully to avert that if that is the problem.

Today, the Subcommittee reviews the ever-newsworthy subject of business method patents for the second time. Last year, we heard testimony on this subject from both the former director of the Patent and Trademark Office and academia. Dare I say, there was considerable hype over this subject a year ago, which has to some extent died down, but not completely. Last rites have not been pronounced. In my opinion, the anxiety over this subject passed when businesses saw that these patents were merely another valuable

form of intellectual property which can be managed not unlike copyrights and trademarks.

Whether you are an Alan Greenspan, a practicing inventor tinkering in a garage, or a school teacher, it is well known that patents have played a central role in our industrial and economic history since the founding of our nation when Thomas Jefferson served as the first patent commissioner. The work of this Subcommittee has proven again and again that intellectual property and the Internet are compatible. In fact, there is a long history of method patents and software-enabled inventions.

It is important for everyone within earshot to be clear that I am aware of and sensitive to the press reports of questionable patents in this area. The press has cited examples of questionable patents, including those for peanut butter and jelly sandwiches, golf swings, and gene-related inventions. Certainly, Congress should not legislate in a way that throws the baby out with the bath water.

I am pleased to hear about all the developments in this area in the past year, including the steps that the PTO has taken to tighten its review process to improve the examination of these applications and thus increase the quality of issued patents, especially in the area of business patents.

Our number one priority in Congress, it seems to me, is to work to ensure that the PTO can retain all of its fees to improve the quality of examination to be as high as humanly possible. While some have maintained that there was a crisis at hand, it is always important to look at the facts, which do not bear out this proposition. We have no evidence, or strike that, I have no evidence of crisis in the courtrooms regarding litigation concerning business method patents. As you all know, Congress was careful to address the public interest in this area when we adopted the special protections of the American Inventors Protection Act.

This afternoon, we are fortunate to hear from a range of witnesses who will bring to the Subcommittee both a lifetime of experience with patents as well as a perspective from the cutting edge of innovation.

Rest assured, we all take a genuine interest in this subject. Our door is open to anyone who feels that there is mischief by any of the parties in this area. It is my hope that the witnesses will be able to educate the Members of the Subcommittee about the latest developments in this field, as well as what may be necessary in the future to maintain an effective balance in the patent system between the rights of inventors and the public.

I look forward to hearing from you all subsequently, and I will now recognize the gentleman from Virginia for 5 minutes.

Mr. BOUCHER. Thank you very much, Mr. Chairman. I want to applaud you for examining today the many questions that surround the award of business method patents. In my view, something is fundamentally wrong with a system that enables individuals to get patents for doing the seemingly obvious.

Some examples: Priceline today is utilizing a business method patent on a reverse auction name-your-own-price system on the Internet. This patent was awarded even though the market economy of the Western world and the entire theory of micro economics

is predicated on individuals setting a price at which they are willing to purchase something.

As another example, a patent was awarded for a business method for interactive fundraising across a data packet transferring computer network. The holder of this patent is now suing the Red Cross for soliciting charitable contributions on the Internet, claiming that his patent covers this entire field.

As another example, a patent was very nearly awarded for conducting commercial transactions across international boundaries using the Internet. I understand that the PTO had made a tentative allowance of this patent and that tentative allowance has now been withdrawn, but the patent application itself is still being reviewed.

It would appear that methods of doing business that are well known and long established in the physical world of bricks and mortar are now being deemed novel and new simply because they are being carried out on the Internet. The result is the restriction of competition and the lessening of innovation, precisely the opposite of the result that the patent laws are designed to achieve. Under these patents, entire markets are foreclosed to competition and it is difficult to perceive how the continued award of patents along this line advances the greater public good.

It should be said that in these instances, the patent covers the basic concept of the business method, such as using computers to solicit donations or to conclude commercial transactions across international borders. The creator of the intellectual property can always obtain a copyright on the software that implements a particular method of doing these things and no one would complain. What is new and what is disturbing is obtaining ownership of the entire concept of performing seemingly obvious acts, whatever individual method of implementation is used, and in doing so, foreclosing the opportunity for competitors to develop new and different means of entering that business.

Mr. Berman and I have drafted legislation which would, if enacted, provide a much needed reform of the business method patent process. We would not go as far as Europe has gone. We would not go as far as the United Kingdom has gone. We would not go as far as Japan has gone and prohibit altogether business method patents. Our legislation would leave the United States distinct among the industrialized world in allowing patents for business methods. But by making one major substantive change and two major procedural changes, our measure strikes at the very heart of the problems that I have described.

First, we would create the presumption that the computer-assisted implementation of an analog world business method is obvious and is, therefore, not patentable. Using the Internet to do such obvious things as set a price for an item, solicit money, or conduct business across international boundaries would no longer be patentable.

We would also create an opportunity for the public to submit evidence of prior art while the patent application is being reviewed, and after a patent is awarded, an opposition procedure with a preponderance of the evidence standard of proof would give the gen-

eral public a chance to challenge a patent without having to resort to litigation.

I want to commend the Patent and Trademark Office for the greater care it has recently shown in reviewing business method patent applications. The legislation that Mr. Berman and I have put forward would further enhance the PTO's ability to assure that patents are awarded only for the truly novel and that the PTO will not award any more monopoly power to people who are doing the patently obvious.

Thank you very much, Mr. Chairman, and I look forward to the witnesses' testimony.

Mr. COBLE. I thank the gentleman.

I am now pleased to recognize the Ranking Member, the distinguished gentleman from California, Mr. Berman.

Mr. BERMAN. Thank you, Mr. Chairman, first, for holding the hearing, and secondly, for indulging me in my tardiness. I was at another committee and could not get away.

The gentleman from Virginia made a number of the points that I wanted to make, so I am going to try and shorten my opening statement. I would ask unanimous consent that it be made part of the record in its entirety.

Mr. COBLE. Without objection.

Mr. BERMAN. I want to do a couple of things. First, I want to thank the witnesses, but particularly Mr. Steinberg, who detoured here on his way between New York and Texas, for agreeing to share his experiences, both as a businessman and an attorney affected by business method patents.

I have two related concerns about business method patents. They both arise out of my deep respect for the role of patents in spurring innovation. When weak patents are granted, innovation is dissuaded. The patent system is meant to encourage and enable inventors to push the boundary of knowledge and possibility, not simply reward them for putting old wine in new bottles.

My first concern relates to the very propriety of patenting methods for doing business. Should an abstract idea for conducting or organizing business operations receive patent protection? Opponents of patenting of business methods believe the patenting of business methods extends patent protection far beyond its appropriate and historical scope. They believe such patents will harm innovation and could effectively preclude competition in businesses for which one party has a business method patent. They argue that patents are supposed to give an innovative business an advantage over its competitors, not the ability to prevent any competition in that business.

I am going to cut short some of the illustrations of this—I will try and patent my concepts here—my second concern is the quality of some business method patents issued by the PTO in recent years. There have been a number of those examples. Mr. Boucher mentioned a few of them. There are patents covering the method of allowing automobile purchasers to select options for cars ordered over the Internet, a method of operating a fantasy football league over the Internet, international commerce over the Internet, the use of targeted banner advertising over the Internet, the sale of audio and visual works over the Internet.

I do not purport to be a patent expert, nor do I pretend to know whether any of these patents and others like them are valid or invalid. There are a variety of good reasons to harbor substantial doubt about their validity. Many of these patents appear to simply cover age-old business practices conducted over the Internet. Many respectable parties have expressed serious concerns about the quality of such patents and several courts have held against the owners of various business method patents.

The very existence of significant doubts about the validity of many business method patents is a problem, as these doubts dissuade investment in companies holding such patents. Furthermore, there is reason to believe that such doubts will only build as time passes.

I know that the PTO has moved to address these concerns by creating a business method patent initiative. I commend the PTO for undertaking that initiative and I look forward to hearing from the Acting Director about the success that they have. I am not completely convinced that the initiative will be sufficient to address patent quality concerns, and for these reasons, I have introduced legislation with my friend and colleague, Mr. Boucher, to raise some new processes and new ways of dealing with the quality of these patents. Mr. Boucher has described this to some extent and I will not take the committee's time to go any further.

I once again want to thank the Chairman for holding a hearing on this. I think it is not an issue that people are marching in the streets about. This does not give you music for free, but it is an important question and I appreciate the Chairman holding a hearing.

Mr. COBLE. I thank the gentleman.

[The prepared statement of Mr. Berman follows:]

PREPARED STATEMENT OF HON. HOWARD L. BERMAN, A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF CALIFORNIA

Mr. Chairman,

I thank you for calling this hearing on business method patents. It provides a welcome opportunity to explore a very complicated area of law that profoundly affects the growth and health of our information economy.

I want to thank all our witnesses for appearing today. In particular, I want to thank Mr. Steinberg, who has detoured here on his way between New York and Texas, for agreeing to share his experiences as a businessman and lawyer affected by business method patents. Mr. Steinberg, I hope you have time to take in the cherry blossoms before you hop back on a plane.

I have two related concerns about business method patents, and I am in good company harboring these concerns. I understand they are shared by many others, including academics, many members of the patent bar, and companies in the technology, Internet, software, financial services, and insurance industries.

At the outset, I want to note that my concerns arise out of the deepest respect for the role that patents play in spurring innovation. I believe that the patent system is strongest, and incentives for innovation greatest, when only truly deserving inventions receive patent protection. Conversely, when "weak" patents are granted—when artful claim drafting rather than technical breakthroughs become the road to a patent—innovation is dissuaded. The patent system should encourage and enable inventors to push the boundaries of knowledge and possibility, not simply reward them for putting old wine in new bottles.

My first concern relates to the very propriety of patenting methods of doing business. Should patent protection should be granted to processes for achieving a business objective when such processes involve no physical transformation, physical element, technological innovation, or industrial application? Put another way, should an abstract idea for conducting or organizing business operations receive patent protection? Doesn't the language of our U.S. Constitution, which gives Congress the

ability to provide patents for inventions in the "Useful Arts," require some technological aspect in a patented invention?

Opponents of patenting of business methods believe the patenting of business methods extends patent protection far beyond its appropriate and historical scope, and verges on allowing patents for abstract ideas. They believe such patents will harm innovation, and could effectively preclude competition in businesses for which one party has a business method patent. For example, what if American Airlines had thought to patent the "hub and spokes" method of organizing an airline's flight operations? People are concerned about competition in the airline industry today, but what would have happened to competition in the airline industry if such a patent existed? Would American Airlines be the only airline left today?

Opponents to business methods patents believe that their effect on innovation and competition will be particularly severe with regard to Internet businesses. Because new Internet business models are created every day, the first to patent a new business model may be able to preclude any competition in a new business. They argue that patents are supposed to give an innovative business an advantage over its competitors, not the ability to prevent any competition in that business.

My second set of concerns involves the quality of some business method patents issued by the PTO in recent years. Many examples of potentially troublesome business method patents have been brought to my attention. A patent has been granted for a method of allowing automobile purchasers to select options for cars ordered over the Internet, even though automobile showrooms appear to have employed these methods in the physical world for decades. Another patent purportedly covers the selling of music and movies in electronic form over the Internet. There are patents covering a method of operating a fantasy football league over the Internet, incentive programs using the Internet, the use of targeted banner advertising over the Internet, and a system for previewing music samples over the Internet.

Again, I do not purport to be a patent expert, nor do I pretend to know whether any of these patents, and others like them, are valid or invalid. However, there are a variety of good reasons to harbor substantial doubt about their validity. Many of these patents appear to simply cover age-old business practices conducted over the Internet. Many respectable parties, including patent lawyers, companies with enormous patent portfolios, and academics, have expressed serious concerns about the quality of such patents. Several courts have held against the owners of various business method patents. And BountyQuest has awarded bounties for prior art unearthed in relation to some of these patents.

The very existence of significant doubts about the validity of many business method patents is a problem, as these doubts dissuade investment in companies holding such patents. Furthermore, there is reason to believe that such doubts will only build as time passes. The pace of business method patenting has picked up dramatically. While in FY 1999 the PTO received approximately 2650 business method patent applications, in FY 2000 it received 7800 such applications. The PTO reports that the first quarter of FY 2001 has seen business method applications running 18-20% higher than in Q1 of FY 2000.

We will not know what business methods are claimed in these applications for at least eighteen months after filing. In fact, since most foreign countries do not grant patents for business methods, it is likely that U.S. applications for business method patents will not be published until they are issued approximately twenty-six months after filing. Some consider this another grave problem, as technology businesses attempting to move at Internet speed may invest enormous sums of ever-dwindling venture capital only to find important elements of their business plan covered by a patent.

I know that the PTO has moved to address these concerns by creating a Business Method Patent Initiative. I commend the PTO for undertaking this action, and I look forward to hearing from the Acting Director about the success they have had. However, I am not convinced that this action will be sufficient to address patent quality concerns. Instead, I believe legislation may be necessary, and to that end I introduced three related bills yesterday with my colleague, Congressman Boucher.

Though this is an oversight hearing, I want to briefly discuss these bills.

First and foremost, I want to make clear that my primary motivation in introducing these bills is to bolster strong protection of intellectual property, which I believe is critical both to innovation and to the economy. I believe such protection is advanced by assuring the highest level of quality for U.S. patents.

The Business Method Patent Improvement Act of 2001 is very similar to last year's version, but includes several significant changes in response to legitimate criticisms of last year's bill. The Patent Improvement Act of 2001 responds to suggestions by many parties that certain provisions in last year's bill should apply

broadly to all patentable inventions. Finally, the PTO funding Resolution ensures that all PTO fees will be used to fund the PTO and the vital services it provides.

These bills represent a starting point, not an end point, for discussion of legislative solutions to patent quality concerns. The multitude of comments received on last year's bill demonstrate that these problems are difficult and, as yet, present no clear-cut answers. Indeed, reactions to last year's bill exhibited few consistent patterns, with members of the same industries often expressing diametrically opposed viewpoints. What was clear, however, was that introduction of specific legislation proved invaluable at focusing the discussion. Thus, I introduce these bills to initiate that discussion anew in the 107th Congress.

I would like to see a patent system that subjects these patents to more rigorous review, and thus provide greater assurance that they are valid when issued. If there may be ways to improve the prior art available to patent examiners before they issue a patent, we should explore them. If there are ways to decrease the costs of challenging bad patents, we should create them. And if retention of fees will result in better trained, more experienced examiners with access to better resources, we should free the fees.

The bottom line is this: there should be no question that the U.S. patent system produces high quality patents.

[The prepared statement of Mr. Conyers follows:]

PREPARED STATEMENT OF HON. JOHN CONYERS, JR., A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF MICHIGAN

We've all been hearing about the "bad" patents the PTO has been granting: Amazon's one-click shopping method and Priceline's reverse auction system are the usual examples. Some of these patents grant monopolies on methods of doing business that were already being used or simply do not seem worthy of patent protection. That is why there is a lot of criticism that these patents are going to limit the rapid growth in technology that led to the longest period of economic expansion in the 20th century.

Many are blaming the PTO, saying it should just do a better job, but we should get to the root of the problem before we do that. Is it true that the examiners are not being careful enough? Or does the PTO not have adequate resources to review the thousands of patent applications it gets every year? After all, it's no secret appropriators have taken about \$554 million dollars from the PTO over the past ten years, making it impossible for the PTO to modernize. Whatever the reason is for these patents' approvals, though, we need to figure it out before someone tries to patent a method of getting a bill through the House.

As a final note, the situation is improving. Despite the money it's been losing, the PTO is trying to alleviate the problem. It is reaching out to businesses to get their ideas on what to do, enhancing its training programs for examiners, and expanding its patent search procedures to find out if new applications really are innovative. Also, the 1999 patent reform law made it possible for people to defend themselves against infringement claims if they used the invention before it was patented.

Mr. COBLE. We are blessed with a very talented panel this afternoon and we are pleased to welcome each of you. Our first witness is the Honorable Nicholas P. Godici, who serves as the Acting Under Secretary of Commerce for Intellectual Property and Acting Director of the U.S. Patent and Trademark Office.

Mr. Godici, you have two titles. Do you prefer the Director over Under Secretary, or does it make any difference?

Mr. GODICI. Whatever you prefer, Mr. Chairman.

Mr. COBLE. Very well. Prior to his present position, Mr. Godici served a long and distinguished career at the PTO, including in several management capacities and last as the Assistant Commissioner for Patents and Trademarks. Mr. Godici has had excellence in public service acknowledged by numerous awards, including a bronze medal by the PTO and two silver medals by the Department of Commerce.

Mr. Godici received a Bachelor of Science in mechanical engineering in 1972 from the Pennsylvania State University and

earned a graduate level Certificate of Advanced Public Management from the Maxwell School of Citizenship and Public Affairs from Syracuse University. We often have political people come and testify, but Mr. Godici has had a distinguished career of more than 28 years of experience in patents and the intellectual property rights protection arena. I am told that he started his career as a patent examiner in the mechanical arts section, specializing in sporting goods, including hunting, fishing, and vermin destruction devices. Welcome to the Hill, Mr. Godici. He can write a book on those experiences, I am sure. [Laughter.]

Mr. COBLE. Our second witness, seated next to Mr. Godici, is Mr. Mike Kirk, unknown to none of us on this Subcommittee. Mr. Kirk serves as the Executive Director of the American Intellectual Property Law Association. Prior to AIPLA, he served as the Deputy Assistant Secretary of Commerce and Deputy Commissioner of Patents and Trademarks from May 1994 through March 1995. In 1993, Mr. Kirk also served as the Acting Assistant Secretary of Commerce and Acting Commissioner of Patents and Trademarks.

Mr. Kirk earned his Bachelor of Science degree in electrical engineering at the Citadel in South Carolina, his Juris Doctorate in 1965 from Georgetown University Law Center, and his Master of Public Administration in 1969 from Indiana University.

Our third witness is Mr. Ronald E. Myrick, who is the President of the Intellectual Property Owners Association, properly known as IPO, and serves as Chief Intellectual Property Counsel for the General Electric Company. GE's many businesses include one of the world's largest financial entities, the GE Capital Services. GE, I may stand corrected, but I think it is one of the largest companies in America and can trace its origin to Thomas Edison and his many patents, such as the light bulb, am I right, Mr. Myrick?

Mr. Myrick holds a Juris Doctorate cum laude from Loyola University of Chicago Law School. Prior to assuming his present position, he was an attorney in private practice. He has been nominated by the United States to the World Trade Organization dispute settlement roster and has served as a delegate for IPO at meetings of the committees of experts for the Byrd Protocol and the Patent Harmonization Treaty. He is also a member of the U.S. PTO's Patent Public Advisory Committee.

Mr. Myrick has also published a multi-volume treatise and several papers relating to the subject of international litigation. He has lectured at meetings and seminars organized by such organizations as the WIPO, the World Intellectual Property Organization, the ABA, and the State Bar of Texas.

Our fourth and final witness this afternoon is Mr. Andrew B. Steinberg, Executive Vice President, Administration General Counsel, and Corporate Secretary for Travelocity.com. Mr. Steinberg received his Bachelor's degree from Princeton University, magna cum laude, and received his J.D. cum laude from the Harvard School of Law. After law school, Mr. Steinberg served as a law clerk for the Honorable Richard A. Gadbois of the U.S. Central District Court in California. He has served in various positions in private practice, specializing in antitrust, commercial litigation, and aviation matters before his current post at Travelocity.com. Travelocity is a

leading travel website and the world's third largest e-commerce retailer.

Mr. Under Secretary, I presume in the order of introduction we will start with you. And gentlemen, if you will, as we have previously requested, if you could confine your oral testimony to 5 minutes, I assure you your written testimony has been read and will be reread. You will not be buggy-whipped if the red light comes on, but that is at least your warning that your 5 minutes have expired.

Mr. Godici, good to have you with us.

STATEMENT OF NICHOLAS GODICI, ACTING UNDER SECRETARY OF COMMERCE FOR INTELLECTUAL PROPERTY AND ACTING DIRECTOR OF THE U.S. PATENT AND TRADE-MARK OFFICE

Mr. GODICI. Thank you very much, Mr. Chairman. It is an honor for me to be here today, and I appreciate this opportunity to discuss the U.S. PTO's operations concerning business method patents.

Mr. Chairman, as you have indicated, the patenting of business method inventions is not without its share of controversy. The U.S. PTO takes the concerns expressed seriously and we are working to address them.

In administering our nation's patent laws, the U.S. PTO takes its direction on what subject matter is eligible for patenting from Congress and from our reviewing courts. Over the course of the last few years, the courts have made it clear that inventions directed to business methods are eligible for patenting. In the most well-known business method case, the *State Street Bank and Trust v. Signature Financial* case, the Court of Appeals for the Federal Circuit found in 1998 that the financial management system in question constituted a patentable invention because it produced a useful, concrete, and tangible result. In so doing, the Federal Circuit explicitly rejected the notion that a business method exception exists in the United States patent law.

Not surprisingly, we have experienced a significant increase in business method filings in the wake of the *State Street Bank* decision, from 1,300 filings in fiscal year 1998 to 7,800 filings in fiscal year 2000. From those applications, we issued 900 patents last year. That is one-half of 1 percent of all the patents granted that year.

As with any emerging technology, business method applications have posed some challenges for our office and we have taken steps to address those challenges. Our Business Method Patent Initiative, launched just over a year ago, is helping us provide a high-quality examination of patents in this area. Let me briefly highlight some of the key features of this initiative.

First, we have enhanced our partnerships with the affected industries to help identify more databases for our examiners to search and to take advantage of the private sector's expertise in this particular field. Just last month, we held our inaugural business methods partnership meeting in Crystal City, which was attended by over 40 representatives from the private sector.

We have also defined a mandatory search for all applications in the computer implemented business method area, including a classified search of U.S. patent documents and a full text search of U.S. patent documents, foreign patent documents with English language abstracts, and non-patent literature.

We have also established electronic information centers that provide our examiners with access to over 900 databases, over one-third of which contain business and financial information.

We have implemented a new rule, Rule 105, which confirms that examiners have explicit authority to ask for information that may be necessary to properly examine an application.

At the same time, we continue to enhance the technical training of our examiners. Our examination guidelines and training materials have all been well received. Moreover, these materials make clear that merely automating a known business process using well-known computer techniques is not patentable.

Another key feature of our initiative is what we call our second pair of eyes, requiring a second-level review of all allowed applications in Class 705 by an additional experienced examiner.

And lastly, to handle the growth in the number of business method filings, we have increased the number of examiners in Class 705 from 17 at the end of 1997 to 77 today.

We believe our Business Method Patent Initiative is on the right track and we are pleased with the results we are beginning to see. For example, our allowance rate in the business method area has decreased since the time our initiative was launched over a year ago. It is interesting to note that some of our customers are now saying that we are being too restrictive in our examination of these applications, while others still maintain we are not being strict enough. To me, Mr. Chairman, that suggests that maybe we have got it just about right.

With that said, I want to assure the Members of the Subcommittee that the U.S. PTO will continue to closely monitor the situation. If further administrative action is warranted or needed, we will not hesitate to implement the appropriate reforms.

Mr. Chairman, the 211-year history of our patent system makes it clear that robust intellectual property protection fosters innovation. Thanks to the incentives built into the system, advanced technologies have been nurtured and developed in our nation to a degree that is unmatched anywhere else on the globe. I know the U.S. PTO and the Administration look forward to working with you, with Ranking Member Berman, and the other Members of the Subcommittee to ensure that the U.S. patent system continues to be the model for other nations to strive towards. Thank you very much.

Mr. COBLE. Thank you, Mr. Godici.

[The prepared statement of Mr. Godici follows:]

PREPARED STATEMENT OF NICHOLAS P. GODICI

Mr. Chairman and Members of the Subcommittee:

Thank you very much for inviting me to testify today on the patenting of business method inventions. As you know, patents in this emerging area of innovation are a topic of considerable interest and debate in many circles. As has often been the case in the past with other emerging technologies, legitimate concerns have been raised about which business methods should be patentable and whether business

method patents will inhibit innovation and commerce. Given the importance of these issues, particularly in light of our increasingly knowledge- and information-based economy, I commend the Subcommittee for holding this hearing.

U.S. PATENT SYSTEM

In order to understand the patentability of business method inventions, I believe it is necessary to first review the underpinnings of the U.S. patent system itself and the role of the United States Patent and Trademark Office (USPTO) in administering this system. The basis for our patent system is found in Article 1, Section 8, Clause 8 of the Constitution, which provides that Congress shall have the power:

To promote the progress of science and useful arts by securing for limited times to . . . inventors the exclusive right to their . . . discoveries.

In order to implement this Constitutional directive, our Founding Fathers designed an extremely flexible patent system based on principles that have proven remarkably suitable to 210 years of technological advancement. The uniformity and flexibility of the patenting standards of novelty, non-obviousness, adequacy of disclosure, and utility—coupled with the incentives patents provide to invent, invest in, and disclose new technology—have allowed millions of new inventions to be developed and commercialized. This has enhanced the quality of life for all Americans and helped fuel our country's transformation from a small, struggling nation to the most powerful economy in the world. Equally as impressive, the patent system has withstood the test of time. This is powerful evidence of the system's effectiveness in simultaneously promoting the innovation and dissemination of new technologies and the creation of new industries and jobs.

PATENTABILITY CRITERIA

In administering the U.S. patent laws, the USPTO takes its direction on what subject matter is patentable from Congress and our reviewing courts. The current Act that details the standards of patentability, the Patent Act of 1952, specifies four basic statutory requirements that must be met to obtain a patent: (1) the claimed invention must define eligible subject matter and have utility; (2) it must be novel; (3) it must not have been obvious to a person having ordinary skill in the art at the time the invention was made; and (4) it must be fully and unambiguously disclosed in the text of the patent application, so that the skilled practitioner would be able to practice the claimed invention without undue experimentation.

Prior to granting a patent, the USPTO examines each patent application to determine whether it meets these four criteria, as set forth in Title 35 of the U.S. Code. With respect to the first statutory requirement, 35 U.S.C. § 101 states that any person who "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 . . ." subject to the conditions and requirements of the law. Thus, the threshold inquiry as to whether subject matter is eligible to receive patent protection is whether an invention is "new and useful" and whether it fits into one of the enumerated categories.

The courts have recognized the breadth of this statute. In the landmark case of *Diamond v. Chakrabarty*, 447 U.S. 303 (1980), the U.S. Supreme Court acknowledged that Congress intended the statutory subject matter under 35 U.S.C. 101 to include "anything under the sun that is made by man." The Supreme Court also noted that there are limits to patentability. Indeed, in *Diamond v. Diehr*, 450 U.S. 175 (1981), the Court explicitly identified three specific areas of subject matter that are excluded from patent protection. These three areas are: (1) laws of nature, (2) natural phenomena and (3) abstract ideas. Thus, an invention directed toward a pure algorithm or manipulation of abstract ideas with no practical application is not patentable.

The growth and importance of computers and the Internet have led to a significant increase in investment and development in computer-related processes, particularly with regard to electronic commerce. This has inevitably led to more individuals seeking patent protection in these areas. In response to this increased patent activity, a number of cases arose in the 1990's involving issues of defining the boundaries of patent eligibility. Accordingly, the Court of Appeals for the Federal Circuit (CAFC) rendered a series of decisions following the Supreme Court in *Diehr* and *Chakrabarty* that further defined what subject matter can and cannot be patented. I would like to discuss two of these cases, which very clearly set forth the standards for patentability according to our patent law.

In the case of *In re Alappat*, 33 F.3d 1526 (Fed. Cir. 1994), the CAFC, sitting en banc, found that inventions that include mathematical formulas or algorithms are

not unpatentable if they are practically applied. Thus, the mere presence of an algorithm within an invention does not exclude the entire invention from patentability. The key question to be answered is whether the claimed invention, when looked at "as a whole," is an abstract idea, such as a disembodied mathematical concept, or whether the invention produces a practical application which achieves a "useful, concrete and tangible result."

Four years after *In re Alappat* came the most well-known case with regard to business methods: *State Street Bank and Trust Co. v. Signature Financial, Inc.*, 149 F.3d 1368 (Fed. Cir. 1998). The *State Street* case involved a patented data processing system that transformed data representing discrete dollar amounts into a final share price momentarily fixed for recording and reporting purposes. The Federal Circuit found that the financial management system in question constituted a patentable invention because it produced a "useful, concrete and tangible result."

It is important to note that the significance of *State Street* goes beyond its immediate holding. The Federal Circuit in *State Street* explicitly rejected the notion that a "business method" exception exists in United States patent law, thereby ending any notion that inventions deemed to be business methods, by whatever criteria, would be excluded from patentability on that basis alone. Thus, the *State Street* decision clarifies that an invention deemed to be a "business method" will be treated in the same manner as any other method or process invention. In other words, there shall be no disparate treatment for different categories of inventions.

While *State Street* did not change United States law and practice, it did create a new awareness that business method claims could be patented. For example, in fiscal year 1998 there were about 1,300 filings in the U.S. classification area 705, which includes much of what is commonly known as computer-implemented "business method" inventions. By contrast, there were 2,820 filings in fiscal year 1999 and 7,800 filings in fiscal year 2000. It should be noted, however, that despite these increases, Class 705 filings represented only a small fraction (2.6%) of our total patent filings in fiscal year 2000. Moreover, the 899 patents that were granted in Class 705 last year constituted a mere one-half of one percent of all patents grants for the year.

RESPONDING TO CONCERNS

While the courts have made it clear that inventions directed to business method inventions are patentable subject matter, some have suggested that an increase in the issuance of business method patents may stifle innovation and investment generally. Others are concerned that patents that have been awarded in these areas, while generally appropriate, may in certain cases be overly broad or not truly novel. These fears raise legitimate issues, and the USPTO has taken a number of steps to address these concerns.

In March of last year, the USPTO announced a new Business Methods Patent Initiative. This program established a solid framework that provides the techniques necessary to cope with the challenges presented by the emerging area of business method patents. Accordingly, we have established enhanced partnerships with affected industries in order to have them educate our examiners so that we can take advantage of their knowledge and expertise in their fields. As part of this partnership, we hosted a Business Method Patents Roundtable on July 27, 2000, with members of industry and other interested parties, during which myriad issues regarding these patents were discussed. In addition, we recently convened our first meeting of the Business Methods Partnership on March 1, 2001. This partnership meeting involved a fruitful exchange of ideas, and it is just the first of many to come. I am also pleased to report that the USPTO is working to facilitate industry feedback on our examiners' prior art resources.

The USPTO's Business Methods Patent Initiative also includes specific features to bolster the quality of our patent searches. For example, we have defined a mandatory search for all applications in the computer-implemented business methods area, including a classified U.S. patent document search and a full text search of U.S. patent documents, foreign patent documents with English language abstracts, and non-patent literature. To assist our examiners in finding pertinent prior art, we also have established "Electronic Information Centers" which provide examiners with access to over 900 databases, over one-third of which contain business and financial information. As 18-month publication of patent applications takes effect and as we identify with our industry partners more databases to search, the amount of published prior art available to examiners will also increase.

With respect to prior art, the USPTO implemented a new Rule 105 (37 C.F.R. § 1.105), effective November 27, 2000, which confirms that examiners and other office employees have explicit authority to ask for information that may be reasonably

necessary to properly examine an application or treat a matter with regard to the examination of a patent application filed under 35 U.S.C. § 111 and 35 U.S.C. § 371. We are hopeful that Rule 105 will further enable our examiners to perform the best examination possible, with applicants' assistance. In addition,

37 CFR 1.99 permits third parties to submit for examiners' benefit prior art in published applications without an attribution of how that art affects patentability.

As part of our Business Methods Patent Initiative we also instituted a second-level review of all allowed applications in Class 705 by an additional experienced examiner beyond the examiner who would normally review the application before it could be granted. We also are continually enhancing the technical training for our examiners. For example, we revised our Examination Guidelines for Computer-Related Inventions and training examples for these inventions. These revisions were made in order to update patentability standards in light of the *State Street* and *AT&T* cases, which clarify that business methods should be treated like any other process claims.

Our examination guidelines and training materials specifically address the fact that merely automating a known human transaction process using well known automation techniques is not patentable. Lastly, to handle the growing number of Class 705 filings, we also increased the number of examiners in this area from 17 in late 1997 to 77 today.

We believe that our Business Methods Patent Initiative and other concerted efforts in this regard will ensure the issuance of high quality business method and software patents. In fact, we are now beginning to see significant results in this regard. For example, our allowance rate in the affected areas of business method inventions has decreased since the time our Initiative was launched a year ago. It is worth noting from recent press reports that some of our customers believe we are being too restrictive in our examination, as evidenced by this reduced allowance rate.

Before closing, I would also like to point out that the USPTO has been issuing method patents for over a century and a half. We have been issuing patents on methods of teaching since the mid-1800's, including a patent issued in 1864 for a method of teaching penmanship. Moreover, there have been a number of patents regarding innovations in the business and financial fields throughout the history of the USPTO. For example, in 1799, only nine years after the first U.S. patent, the first financial patent was issued regarding "Detecting Counterfeit Notes." Unfortunately, the details of this invention were forever lost in the great Patent Office fire of 1836. In addition, in 1889, Herman Hollerith received a patent on a method for tabulating and compiling statistical information for a business. The patent he received helped his fledgling company to survive. Later, the company's name was changed to International Business Machine Corporation (IBM). Mr. Hollerith's patented method was probably the first patent issued regarding the automation of business or financial data, and it and the related punch cards were used until the birth of the personal computer.

CONCLUSION

Mr. Chairman, the USPTO is very pleased with the results thus far of our Business Methods Patent Initiative, and we will continue to closely monitor the situation in order to ensure the issuance of high quality business method patents. In addition, if further administrative action is needed or warranted by modifications by the Courts, the USPTO will take appropriate action.

Let me assure the Members of the Subcommittee that we are committed to ensuring that our practices and policies promote the innovation and dissemination of new technologies. We are confident that the patenting of business method inventions is consistent with our law and with our practice, and we believe that any arbitrary restriction of patentability in this or other technologies may cause deserving innovations to go unprotected and deserving investments to go unrewarded.

The overwhelming preponderance of evidence throughout the history of the U.S. patent system suggests that robust intellectual property protection supports, rather than impedes, innovation. Indeed, for over two hundred years our patent system has enabled American industry to flourish, creating countless jobs for our citizens. Advanced technologies have been—and continue to be—nurtured and developed in our nation to a degree that is unmatched in the rest of the world. In many instances, the availability of patent protection has been integral to these advancements. In this regard, the USPTO and the Administration look forward to continuing to work with you and the members of the Subcommittee to ensure that U.S. patent system remains the envy of the world.

Thank you, Mr. Chairman.

Mr. COBLE. Mr. Kirk.

**STATEMENT OF MICHAEL K. KIRK, EXECUTIVE DIRECTOR,
AMERICAN INTELLECTUAL PROPERTY LAW ASSOCIATION**

Mr. KIRK. Thank you, Mr. Chairman, Members of the Subcommittee. Following the spate of criticism of the *State Street* decision and the various proposals to address the problems that allegedly exist with business method patents, the AIPLA Board of Directors initiated a thorough review of the patenting of computer-implemented business methods last year.

The AIPLA found no basis for discriminating against inventions related to business methods. We do not believe that a case has been made for amending the patent laws and procedures to provide a special regime for inventions related to business methods. Moreover, we believe that it could possibly be inconsistent with the obligations of the United States under the TRIPs agreement to single out business method patents and patent applications for special treatment. We do, however, believe that the overall functioning of the patent system could be enhanced through certain changes in U.S. patent law and USPTO procedures.

Many of the concerns regarding patent protection for business methods relate to the effectiveness of the examination process. It is fair to ask, we believe, whether the USPTO is doing the best possible job in ensuring that it carefully examines such inventions and does not issue unwarranted patents, but this is a fair question to ask in relation to any of the technologies examined by the U.S. PTO, such as inventions arising from the mapping of the human genome.

We believe that many of these concerns can be addressed through proper determinations of patentability made in the first instance by the USPTO, determinations that trained examiners with adequate search tools can and do make every day. The important things here are to find and properly apply the most relevant prior art.

Challenges in examining business methods often stem from the examiner's lack of access to pertinent prior art. At the present time, the patent literature relative to business method patents is very sparse. AIPLA therefore commends the USPTO in its ongoing efforts to identify and collect additional prior art and to examine these applications. We also endorse the hiring by the Office of examiners with both business experience, business education, and technical qualifications. We understand they now have seven examiners that have MBAs in addition to their technical qualifications that handle business method patents.

Even the most qualified individuals, however, must also be trained to become effective examiners, a task that is very difficult even in the best of times, trying to replace all of the examiners that the PTO loses annually, but a task made even more daunting in light of the President's budget, which we now understand will divert perhaps as much as \$200 million in USPTO fees for the coming year.

This leads us to the painfully obvious point that the recommendations for improving the handling of patent applications relating to business methods is going to require resources. Even in

this time of economic retrenchment nationally, the amount of money that it would require to make the USPTO the envy of other nations around the globe, as it used to be, is infinitesimal when contrasted with the magnitude of the surpluses the nation continues to enjoy. We especially appreciate the efforts of you, Mr. Chairman, in introducing H.R. 740, and also you, Congressman Berman, in introducing just yesterday H.Res. 110, both of which seek to allow the USPTO to retain and use all of its fee income.

I would like to comment about one legislative change we strongly recommend. It was largely through the efforts of this Subcommittee in the 106th Congress that Congress provided for optional *inter partes* post-grant reexamination in the AIPA. The original concept would have provided an excellent means for the public to bring new information to the attention of examiners, thus improving the quality and reliability of patents. Unfortunately, compromises were made—no third party appeal to the CAFC and additional and unwarranted estoppels—both of which, in our opinion will discourage the public from ever using this procedure. This leaves expensive, protracted litigation as the only effective alternative, an alternative which those of limited resources simply cannot afford.

To address these concerns, we propose an early *inter partes* opposition proceeding. It will allow a third party to initiate opposition proceeding within the first year after patent grant on the basis of Sections 102, 103, and 112 of the patent statute. The opposer would be able to participate in generally the same manner as *inter partes* reexamination, but with the added benefit of being able to appeal to the CAFC and without the estoppels of the existing law.

In this regard, we were pleased again, Mr. Berman, to see your bill yesterday, H.R. 1333, that would provide post-grant opposition procedures applicable to all patents.

In conclusion, we do not deny that there have been and continue to be growing pains as the USPTO and the public adjust to the growing number of applications filed for various methods of conducting businesses. Like the difficulties faced in the 1980s, however, when the USPTO faced a flood of biotech applications, we are confident that the USPTO can meet this challenge. The patent law was not changed in the 1980s to respond to the strains placed upon it by the flood of biotech applications and we do not believe that special technology-specific amendments need to be made to address this transition we are now in with business method patents. Thank you very much.

Mr. COBLE. Thank you, Mr. Kirk.

[The prepared statement of Mr. Kirk follows:]

PREPARED STATEMENT OF MICHAEL K. KIRK

Mr. Chairman:

The American Intellectual Property Law Association (AIPLA) appreciates the opportunity to present its views on the examination and grant of applications and patents for business method inventions, to offer some suggestions for improving the procedures for efficiently improving the quality of all patents, and finally to comment on a few suggestions that have been made in connection with business methods patents.

The AIPLA is a national bar association whose more than 12,000 members are primarily lawyers in private and corporate practice, in government service, and in the academic community. The AIPLA represents a wide and diverse spectrum of individuals, companies and institutions involved directly or indirectly in the practice

of patent, trademark, copyright, and unfair competition law, as well as other fields of law affecting intellectual property. Our members represent both owners and users of intellectual property.

INTRODUCTION

The Federal Circuit decisions in the *State Street Bank & Trust Co. v. Signature Financial Group*, 149 F.3d 1368 (Fed. Cir. 1998) and *AT&T v. Excel Communications*, 172 F.3d 1352 (Fed. Cir. 1999) clearly brought to the attention of the public the types of inventions for which patents can be granted. Subsequent decisions involving so-called "business method patents" (a term in desperate need of definition) have drawn further attention and criticism toward business method patents, as well as toward software-related patents. Last year, in response to popular calls for Amazon.com to stop asserting the "one-click" patent involved in its suit against BarnesandNoble.com, Jeff Bezos, CEO of Amazon.com, proposed that business method and software patents be treated differently than patents on other technologies. Observing these cries for various actions to address the alleged problems of "business method patents", the AIPLA Board of Directors concluded that a thorough review of the patenting of computer-implemented methods was called for. Thus, in March, 2000, the Board commissioned a special working group to prepare a White Paper on the patenting of methods of doing business. After extensively discussing and revising earlier versions of this White Paper in meetings in May, July, and September, the Board directed that a draft White Paper be published for comment by the AIPLA membership. Comments were accepted through October 31, 2000, and the White Paper was adopted by the Board on November 27, 2000. It is published on our website: <http://www.aipla.org>.

The White Paper contains a number of recommendations that respond to criticisms that have been made against the patenting of business methods. In summary, we recommended that business methods with useful, concrete or tangible results, including Internet- and software-implemented business methods, should receive the same treatment under the patent laws as other technologies. Where implemented in software, business method patent applications should be examined the same as software-related applications are examined today for compliance with the requirements of 35 U.S.C. §§ 101, 102, 103, etc.

The AIPLA found no basis or need for discriminating against inventions related to business methods. We do not believe a case has been made for amending the patent laws and procedures to provide a special regime for inventions related to business methods. Moreover, we believe it would possibly be inconsistent with the obligations of the United States under the Agreement on the Trade Related Aspects of Intellectual Property Rights (TRIPs) to single out business method patent applications and patents for special treatment or to engraft any notion of "technological contribution" onto the existing criteria for patentability.

The AIPLA believes that the overall functioning of the patent system could be enhanced through certain changes in the U.S. patent law and in USPTO procedures. In addition to strengthening the U.S. patent system, these changes would also address the concerns which have been raised regarding the grant of certain business method patents. These changes include:

1. improving USPTO non-patent prior art collections, including improved classification of, and access to, prior art references submitted by applicants;
2. enhancing USPTO examiner skills and training;
3. funding the USPTO adequately to allow it to fulfill its statutory obligations to effectively search and examine patent applications and promptly grant valid patents;
4. creating an early inter partes post-grant opposition procedure without estoppel unless appealed to the Federal Circuit;
5. subject to national security considerations, publishing all pending patent applications after eighteen months.

In addition to setting forth the reasons for our recommendations which follow, I will also provide the views of the AIPLA on certain aspects of H.R. 5464, the "Business Method Patent Improvement Act of 2000" introduced by Ranking Member Berman in the 106th Congress as well as on some suggestions that have recently been offered to address perceived problems created by business method patents.

Business method inventions should be protected under the same framework of laws under which other inventions are protected.

State Street did not make business methods patentable. Rather, it eliminated the "business method" exception as a basis for excluding consideration of the potential

eligibility of certain subject matter. *State Street* held that the claims in that case were directed to a "machine" (e.g., a computer programmed to determine allocation of profit and expense in a certain type of investment entity) and that those claims should be subject to the same type of analysis applied to subject matter in other areas of technology. As noted by the 1992 Advisory Commission on Patent Law Reform, "The patent laws have successfully adapted to new technologies for over two hundred years, and in each instance have fulfilled their role in promoting the technological innovation and commercial application of such technologies. Furthermore, any statutory change in either the levels or nature of available protection will cause more difficulties than benefits, and will risk the effectiveness of protection of U.S. technological innovations abroad."

A related problem arising from the misunderstanding that *State Street* made "business methods" patentable is the unfortunate reference to the term itself, e.g., "business methods." *State Street* said nothing at all about making "business methods," in the broadest sense of that term, "patentable." The court was simply considering in *State Street*, as it has in numerous other cases, the question of whether the particular type of computer-implemented invention before it was eligible for patent protection, using the same standards and principles ("useful, concrete, and tangible result") that were previously enunciated in *In re Alappat*, 33 F.3d 1526 (Fed. Cir. 1994).

A shortened term of three to five years as was originally suggested by Mr. Bezos should not be adopted. Not only is there no empirical data to justify singling out such inventions for shortened terms, but we believe it would run afoul of the obligation of the United States under Article 33 of TRIPs to provide a patent term of at least twenty years from filing.

No special test or interpretation of the patent laws should be applied to business method inventions.

There is no basis for excluding new and nonobvious business method innovations from protection under existing patent laws. Congress intended statutory subject matter to include "anything under the sun that is made by man." *Diamond v. Chakrabarty*, 447 U.S. 303 (1980). Thus, the protection acknowledged in *State Street Bank and AT&T v. Excel* for business method innovations should continue to be available for such innovations. As noted by the Advisory Commission, "Any continued fine tuning of the interpretation of statutory subject matter can be and has been undertaken by the courts."

The AIPLA believes many of the concerns that have been expressed can be addressed through appropriate application of the patent laws. Computerization of a particular, known method of doing business may, or may not, be patentable when examined under the tests of 35 U.S.C. §§ 102 and 103 currently applied to other software-related patent applications. We would generally agree with those who say that a patent should not issue on a known business process where the only contribution by the applicant is in implementing the known business method by a computer. However, to elevate this common sense observation regarding the operation of section 103 to a statutory presumption would, we believe, create more problems than it would solve. In the final analysis, this is a determination that properly trained examiners with adequate search tools should make in the course of a complete examination. Thus, an amendment of Section 103 of title 35 to provide that "a business method which differs from what is claimed only in that the claim requires a computer technology to implement the practice of the business method invention" as called for in H.R. 5364 is unnecessary and problematic. The important thing here is to find and properly apply the most relevant prior art.

As previously noted, some have suggested that section 112, paragraph 6, of title 35 should be amended to import some notion of "technical contribution" as a criteria of patentability. Perhaps because no one has yet been able to provide an adequate definition of what is meant by the term "technical contribution", other suggestions presumably intended to curtail the patenting of business method inventions have surfaced. One such suggestion would amend section 112, paragraph 6 to state that claims reciting limitations directed merely to function are not patentable, a suggestion that would introduce confusion into "means plus function" claiming and set aside decades of judicial interpretation of this section of the law. Again, both for suggestions to modify section 112 as well as for suggestions to amend section 103, one should not lose sight of the fact that TRIPs obligates member countries to make patents available for any inventions, whether products or processes, in all fields of technology without discrimination, subject only to the normal tests of novelty, non-obviousness and utility (Article 27.1).

The PTO should collect non-patent business methods prior art, including that describing business methods not implemented on a computer.

Many of the concerns regarding patent protection for business methods relate to the effectiveness of the examination process. It is fair to ask whether the USPTC is doing the best possible job in ensuring that it carefully examines such inventions and does not issue unwarranted patents. But it must be kept in mind that this is a fair question to ask in relation to any of the technologies examined by the PTO, such as inventions resulting from the mapping of the human genome.

Challenges in examining business methods often stem from the examiner's lack of access to pertinent prior art. At the present time, the patent literature relative to business method patents is very sparse. AIPPLA commends the USPTO's ongoing efforts to collaborate with the private sector to identify and develop additional sources of prior art relevant to proper examination of these applications. We encourage the USPTO to intensify its categorization and cataloging of prior art documents submitted in patent applications filed on business method inventions.

The non-patent prior art useful for examining inventions relating to methods of doing business covers a broader swath than that of most non-patent computer-related inventions. It encompasses, for example, (1) programmed e-commerce website applications; (2) literature and websites suggesting specific sales techniques for the web; and (3) the entire field of business practices (non-software implemented) themselves. In this regard, while the AIPPLA encourages the USPTO repeatedly to remind patent applicants of their duty to disclose to the USPTO all material prior art (including all forms of such prior art whether implemented manually, via computer or otherwise), we question a provision such as that in H.R. 5364 requiring an applicant for a patent for a business method invention to disclose in the application the extent to which the applicant searched for prior art. The fact that an applicant searched for prior art, by itself, would do little to assist an examiner to examine an application, but could lead to costly discovery in any litigation and possible allegations of inequitable conduct on the ground that the applicant should not have sought a patent of a given scope in light of any search conducted.

The USPTO should continue to hire more examiners with business backgrounds, such as MBAs, and should continue to aggressively improve the skills and training of new examiners.

An increase in the non-patent, business methods prior art base could pose a challenge for examiners who have software backgrounds but no business backgrounds. The non-patent software art, which presents access and retrieval challenges, may nonetheless be the most fruitful source of relevant prior art to examine business method inventions. Accordingly, business experts should be included as examiners.

Examiners must be effectively trained to respond to the increasing number of new patent applications for business inventions. Such training would be difficult enough in the context of hiring additional examiners to respond to the flood of new patent applications and the loss of trained examiners, but this task will be all the more daunting in light of the President's budget which, we have reason to believe will divert approximately \$ 200 million in FY 2002.

The one most commonly leveled complaint in the entire business method patenting debate has centered on the quality of the examination. High quality examination of business method patent applications is critical. While the Office has made significant strides in developing programs to address this criticism, especially including the "second pair of eyes" review, this has come at a cost—the cost of ever longer pendency of business methods patent applications. This lengthened pendency is now forcing some very difficult choices on applicants in this field. The United States, as is usual in these matters, is more advanced in the issuance of patents on business methods. Until our major trading partners catch up with the United States, applicants for such patents in this country are, by and large, not filing applications on business method inventions in other countries. With the growing delays in obtaining even a first opinion on the patentability from the USPTO, American firms and inventors are facing a very difficult question: do they gamble that they will get a patent in the United States and allow their applications to be published at 18 months (knowing they will get no protection abroad since they have not even filed there), or do they abandon their business method patent applications and practice the invention as a trade secret?

Congress should adequately fund the USPTO to allow it fulfill its statutory obligations to search and examine patent applications and promptly grant valid patents.

The preceding discussion leads to the painfully obvious point that the recommendations above for improving the USPTO's handling of patent applications relating to business methods require resources. Unfortunately, it appears that neither political party—whether controlling the Congress or occupying the White House—

regard the health and vitality of our nation's patent system as a sufficiently important national priority to provide the needed funding. Even in this time of economic retrenchment, the amount of money that it would require to make the USPTO the envy of other nations around the globe—as it used to be—is infinitesimal when contrasted with the magnitude of the surpluses that the nation continues to enjoy.

There should be an effective early opposition proceeding with a third party right to appeal to the Federal Circuit and with no estoppel attaching to USPTO decisions not reviewed by the Federal Circuit.

Largely through the efforts of this Subcommittee, Congress provided for optional inter partes, post-grant reexamination, in addition to the previously existing ex parte post-grant reexamination. This new procedure was intended to improve the quality of U.S. patents by offering an effective and less expensive option to protracted litigation for testing patent validity. It was to accomplish this goal by permitting limited participation in reexamination proceedings by third-party requesters. As originally conceived, the new procedure reflected a delicate balance between the interests of third-party requesters in having limited participation in reexamination proceedings, and the interests of patentees in not being subjected to undue harassment by third parties. The original concept would have provided an excellent means for a member of the public, with information not available to the examiner, to bring the information to the attention of the examiner and improve the quality and reliability of such patents. While desirable for all fields of technology, this would be particularly desirable with respect to business method patents where the relevant information may not be readily accessible to examiners.

Although the new optional inter partes reexamination procedure was a step in the right direction, compromises were made in the legislative process that we believe will discourage the public from using the procedure. The most significant of these limitations prevents third-party requesters from appealing a decision of the Board of Patent Appeals and Interferences to the Court of Appeals for the Federal Circuit. This inability of third-party requesters to appeal a decision of the Board to the Federal Circuit, or to participate in an appeal by the patentee, chills public interest in participating in inter partes reexamination. This makes expensive, protracted litigation a preferable avenue for many third parties. The increased costs in terms of time, money, and resources associated with litigation in most cases, however, leave others with no real alternative.

Moreover, in an effort to provide added safeguards against harassment, additional estoppel effects were accorded to fact determinations made by the USPTO during inter partes reexaminations and to reexamination decisions made by the USPTO. Thus, not only are the decisions of the Board not appealable, but many issues determined by the USPTO will be dispositive in any subsequent court proceedings. In addition, the estoppel effect of a USPTO decision extends to issues that could have been raised, as well as those that were actually raised. This brings the risk of initiating reexamination to an unacceptably high level for many of those who might otherwise consider it as an economically viable alternative to litigation.

To address these concerns, the AIPLA proposes instituting an early, truly inter partes opposition proceeding. The proposed proceeding would be in addition to those presently available under 35 U.S.C. §§301-307 (ex parte reexamination) and §§311-318 (optional inter partes reexamination). It would require a third party to initiate an opposition proceeding within a very short time period after patent grant, for example, one year, and would permit the third party to challenge the patent on the basis of sections 102, 103, and 112. The third party opposer would be permitted to participate before the USPTO in generally the same manner as a third party requester is now permitted to participate in optional inter partes reexamination, with one very important difference: the third party opposer would be permitted to appeal, and to participate in an appeal of, a decision of the Board to the Federal Circuit.

We believe that the proposed opposition procedure would provide a balanced approach between the interests of patentees and the public to remedy the possible issuance by the USPTO of overly broad, and therefore invalid, patents because it did not have access to the most relevant prior art. By requiring such oppositions to be filed early, third parties would have to come forward before the patentee has invested large sums of money in commercialization. Also, this would allow the patentee to seek new claims at an early stage that avoided the prior art. Thus, both the quality and reliability of patents would be improved.

We note with approval that H.R. 5364 would also have provided for a post-grant opposition procedure during the first nine months following patent grant. This opposition procedure, however, would have been limited to patents for business method inventions. The AIPLA strongly recommends that any post-grant opposition procedure be made available for patents in all technological areas. In addition to the po-

tential TRIPs consistency issues, we believe that it would be all but impossible to precisely determine which inventions are and which are not "business method inventions" which would make this and other procedures that would depend upon a clear delineation as to what is and is not a "business method" an impossible burden for the USPTO.

Finally, we would equally strongly recommend that there be no pre-grant protest or other type of public initiated administrative proceeding to prevent the issuance of a patent. The United States advocated for years that other nations should abolish such proceedings because they were subject to abuse by competitors of patent applicants to improperly delay the issuance of patents for deserving inventions. It would clearly send the wrong signal if the United States were to now embrace such a procedure.

There should be eighteen month publication for all applications.

On March 15th, the USPTO announced the first publication of pending patent applications, with provisional rights accruing to the applicants. Such publication was one of the improvements brought about by the American Inventors Protection Act of 1999 (AIPA). The AIPLA has long supported pre-grant publication of patent applications and we were pleased to learn at the Patent Public Advisory Committee meeting on February 28 that approximately 93% of all applications eligible for publication are being published.

In general, publication of applications contributes to rapid dissemination of technological advances to the public and provides early notice of potentially exclusive rights to such advances. That is why we were pleased to see the provision in H.R. 5364 requiring publication of patent applications irrespective of whether they were only filed in the United States. Unfortunately, in our opinion, this improvement in the publication provisions of the AIPA was again limited to applications for business method inventions. While publication of applications for business method inventions will address concerns expressed about the patent system not being suited for the pace of technical and business development in this field, these benefits are equally applicable to inventions in every fast-paced technological field. With earlier knowledge of such applications, industry participants may have the opportunity to design around where feasible or otherwise have a fully-informed business plan before they begin using or making significant investments to use inventions subject to pending applications. Early publication will also help reduce disruptions to the marketplace that occur when patents issue long after they are filed by limiting the time between the filing and the public's first knowledge of it to eighteen months.

The prior use defense was not adopted as a response to "overbroad" business method patents and it should be expanded, not cut back

The American Inventors Protection Act of 1999 provides a defense to patent infringement for methods of doing or conducting business for those who commercialized such methods before the effective filing date of a patent application (provided they reduced the subject matter to practice at least a year before that date). The legislative history directed to this Act explains that the use of the word "method" in the statute is not a reference to method claims, and that the scope of protection extends to any subject matter that is in fact a method of doing or conducting business, *whether or not claimed as such*.

The prior use defense was initially drafted to apply to any invention which was commercialized prior to the filing date of an application by another covering such invention. Contrary to what some now allege, the prior use defense was not inserted to address concerns regarding overbroad business method patents. Rather, it was the result of a compromise between those who opposed any form of prior use defense and those, like AIPLA, who favored such a defense to permit the continued use of any earlier commercialized invention that satisfied the criteria set forth in section 273 of title 35. Congress was faced with the difficult choice between two totally opposite positions. It was because the opponents of any prior use defense had absolutely no response to the problems created for all of the thousands of companies that had been practicing methods of doing or conducting business as trade secrets for years prior to the *State Street* decision that Congress chose to provide a prior use defense coextensive with the reach of that decision. *State Street* made it clear that all early commercializations of methods of doing or conducting business were at risk of a later inventor obtaining a patent and disrupting their business operations. The adoption of the prior use defense had nothing to do with the breadth (or lack of breadth) of any patents that had issued. The concern was the patents that might issue in the future and disrupt ongoing business operations.

In this regard, we note that H.R. 5364 would narrow this already restricted prior use defense even more. H.R. 5364 would delete the definition that "the term 'meth-

od' means a method of doing or conducting business." Thus, the defense would presumably no longer be available to methods of "conducting" business even though such methods would be patentable under the rationale of *State Street*. This would place prior users of such methods at risk, while those who had commercialized "business methods" would be protected.

CONCLUSION

In conclusion, AIPLA does not deny that there have been and continue to be "growing pains" as the USPTO and the public adjust to growing numbers of patent applications being filed for various methods of running businesses. Like the difficulties faced in the 1980's following the decision of the U.S. Supreme Court in *Diamond v. Chakrabarty* when the USPTO faced a flood of patent applications in the biotechnology field, we are confident that the USPTO will meet this challenge. The patent law was not changed in the 1980's to respond to the strains placed upon it by the flood of biotechnology applications and we do not believe that special, technology specific amendments should be made to address the transition in the filing of business method patent applications that we are seeing today.

Mr. COBLE. Mr. Myrick.

STATEMENT OF RONALD E. MYRICK, CHIEF INTELLECTUAL PROPERTY COUNSEL, GENERAL ELECTRIC, GENERAL ELECTRIC CAPITAL SERVICES, AND PRESIDENT, INTELLECTUAL PROPERTY OWNERS ASSOCIATION (IPO)

Mr. MYRICK. Thank you, Mr. Chairman, Mr. Berman, and other Members of the Subcommittee. I appreciate the opportunity to represent Intellectual Property Owners Association before you today on this important topic. It is incumbent upon me as a member of the Patent Public Advisory Committee to tell you that I am not here in that capacity. I am also not here representing General Electric. I am here only in my capacity as President of IPO.

Again, I want to congratulate you, Mr. Chairman, and Mr. Berman and the other Members of the Subcommittee for working so very hard to try to obtain adequate funding for the PTO. As Mr. Kirk has just said, the President's budget will be coming to Congress this month, and once again withholding many millions of dollars more in fees that the patent and trademark applicants and owners pay for services that they expect to receive. This continuing practice of withholding user fees is having an adverse effect on the quality of the PTO's work or its timeliness, and is also causing huge backlogs of unexamined patent and trademark applications which extend pendency. This is a subject that is relevant to business method patents as well as all other patents.

Dealing specifically with business method patents, at IPO, we formed a special task force to study this issue, and if I may, I will read the names of the companies on that task force to show you the breadth of the consideration that was given. The task force included 3M, AT&T, BASF, Bell South, Eli Lilly, FMC, General Electric, Henkel, Hewlett-Packard, IBM, J.P. Morgan Chase, Mars Incorporated, Microsoft, Rohm and Haas, and Sun Microsystems.

The task force studied the subject of business method patents over many months and recommended a statement that was unanimously adopted by the IPO board last year in June. We brought that statement back up to the board in February to ensure that we were still consistent with that and that our board still agreed with that statement, and that statement was again completely and totally, unanimously affirmed by the board in February of this year. A copy of that statement is appended to my testimony.

The central point of the unanimous IPO board statement is that the Congress should not legislate in the area of business method patents at this time. Recent developments demonstrate, as you have already heard from the previous two witnesses, that the PTO is dealing with the issues, and I would like to mention, too, that I think the courts are dealing with the issues.

We believe patent legislation can be developed to bring more certainty to legal rights in the business methods area, but also with regard to all inventions. Any legislation that is developed, however, should treat all industries equally. Special legislation for business method patents would lead to endless litigation over whether the invention is a business method patent or not.

The integrity of the patent system depends upon the ability of the PTO to carefully examine patent applications and ensure rigorous compliance with the statutory requirements, including the requirements for novelty and non-obviousness. These requirements, properly applied, will screen out all the inventions that you have been hearing about this morning in earlier comments, those that are not deserving of an exclusive patent right.

Recently, the *Wall Street Journal* cited a PTO official as saying that, for the quarter ending December 31, 2000, the PTO granted patents in only 36 percent of the business method applications it examined, down from 56 percent for the quarter ending on March 31, 2000. This dramatic increase in the percentage of business method applications in which patents are actually granted probably comes from a more careful application of the novelty and non-obviousness requirements of the statute, along with the other changes in the PTO practice.

Another recent development that we believe demonstrates that the PTO and the courts are dealing with the business method patent issues is the Federal Circuit's recent decision in the Amazon.com case. The court examined prior art that apparently was not considered by the PTO and concluded that substantial questions were raised about the novelty and non-obviousness of the Amazon.com one-click invention, making a preliminary injunction inappropriate. Now, of course, we are not making any judgment as to whether it is valid or invalid. The point was, the court decided that a preliminary injunction was not appropriate in that case.

While we believe the issues with respect to business method patents are being addressed by the PTO and the courts, we do support development of general patent legislation to address concerns about the quality and timeliness of patents generally. Such legislation could include improvement of the PTO inter partes reexamination procedure, a requirement to publish all patent applications after 18 months, and broadening of the applicability of the earlier user defense.

I appreciate the opportunity to present these comments on behalf of IPO and will be pleased to answer questions.

Mr. COBLE. Thank you, Mr. Myrick.

[The prepared statement of Mr. Myrick follows.]

PREPARED STATEMENT OF RONALD E. MYRICK

Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to speak here today on behalf of Intellectual Property Owners Association (IPO). I am the current President of IPO, and also Chief Intel-

lectual Property Counsel for General Electric Co. in Fairfield, Connecticut, and a member of the U.S. Patent and Trademark Office's Patent Public Advisory Committee, but the views I am expressing today are those of IPO.

IPO is a trade association that represents owners of patents, trade secrets, trademarks, and copyrights. We have about 100 corporate members in industries ranging from computers and software to pharmaceuticals and biotechnology. Our members obtain about 30 percent of the 85,000 U.S. patents a year that are being granted to U.S. nationals, and they also are defendants in suits brought to enforce patents.

IPO members file for at least several hundred business method patents a year. Although patents for business methods have been granted for a long time, many more business method applications have been filed since the Federal Circuit's *State Street Bank & Trust Co.* opinion in 1998, which drew attention to business methods. Last year IPO formed a Business Method Patents Task Force to study the subject. Our task force is a subcommittee of the 50-member IPO Board of Directors and currently includes the following companies:

3M Co., AT&T Corp., BASF Corp., BellSouth Corp., Eli Lilly and Co., FMC Corp., General Electric Co., Henkel Corp., Hewlett-Packard Co., IBM Corp., JP Morgan Chase and Co., Mars Incorporated, Microsoft Corp., Rohm and Haas Co., and Sun Microsystems, Inc.

The task force studied the subject over some months and recommended a statement that was approved unanimously by the IPO Board of Directors in June 2000. The task force continued to study business method patents and watched developments in the Patent and Trademark Office (PTO), the courts and the Congress. The task force recommended reaffirmation of the statement this year, and it was reaffirmed unanimously by the IPO on February 6, 2001. A copy of the statement is attached as an Appendix to my testimony.

The central point of the unanimous IPO Board statement is that Congress should not legislate in the area of business method patents at the present time. Recent developments demonstrate that the PTO and the courts are dealing with the issues.

PATENT LAW PRINCIPLES

For the patent system to operate effectively, of course, legal principles under which patents are examined by the PTO must be clear and capable of application with a reasonable degree of certainty. Similarly, the courts must be able to determine whether a patent has been properly granted using unambiguous statutes and legal precedents. As the same time, arbitrary limitations on the scope of patent law in the name of certainty should be avoided.

Patent legislation can be developed to bring more certainty to legal rights in business methods along with legal rights in all other inventions. Any legislation that is developed, however, should treat all industries equally. Special rules of patent law for particular fields of technologies add to uncertainty and complexity. Article 27 of the Trade-Related Aspects of Intellectual Property Rights (TRIPS) agreement prohibits discrimination based on the field of technology, and also requires patents to be available for inventions that are new, useful, and not obvious. Special legislation for business method patents would lead to endless litigation over whether inventions were inside or outside the law.

Years ago people advocated limitations on patent protection for computer software, but no special patent legislation for software was passed. Patents have helped software inventors prevent pirates from taking a free ride on their R&D investments and the industry has prospered. The American software industry in 1999 had revenues of \$81 billion, according to the U.S. Census Bureau. A group of CEO's predicted last year that revenues will be \$148 billion by 2005.

IPO also believes any new patent legislation that might be developed should not impose requirements for patenting beyond those already in the current statute. The existing statutory requirements, properly interpreted, will screen out subject matter that should not be patented.

A much-cited article in the New York Times last year claimed patents are now "spread across a crucial boundary, into the realm of thought and abstraction." Such claims are wildly incorrect. It is well settled that abstract ideas are not patentable. All patents must be for methods (also called processes), machines, articles of manufacture, or compositions of matter, in the "useful arts." Methods have been accepted as proper subjects for patenting since the founding of the country. The very first U.S. patent, granted to Samuel Hopkins in 1790, was for a method for making potash.

Patents for business methods should have the same scope of protection as patents granted for other inventions. The length of term for business method patents should

be the same as for patents in other fields, and the remedies for infringement of such patents, such as damages and injunctions, should be the same as for patents in other fields. Proposals for special rules for business methods, including the bill H.R. 5364 proposed by Representatives Berman and Boucher last year, have stimulated discussion and drawn attention to improvements that might be made in general patent law, but IPO is not aware of any proposal that should be enacted specially for business methods. In fact, IPO studied numerous provisions in H.R. 5364. Various provisions were referred to our committees for detailed consideration. The conclusions of all of those investigations are consistent with our position here—that is, there should be no special legislation for business methods.

THE PATENT AND TRADEMARK OFFICE

The integrity of the patent system depends on the ability of the PTO to carefully and completely examine patent applications to ensure rigorous compliance with patentability requirements, including the requirements for novelty and nonobviousness. The law defining what is obvious has been refined through a large number of judicial interpretations beginning, in the modern era, with the U.S. Supreme Court's opinion in *Graham v. John Deere Co.* in 1966. In that opinion, a unanimous Supreme Court observed:

It must be remembered that the primary responsibility for sifting out unpatentable material lies in the Patent Office. To await litigation is—for all practical purposes—to debilitate the patent system.

A key responsibility of the PTO is to locate prior art and determine its scope and content. The PTO's burden to search for prior art and make determinations concerning novelty and non-obviousness is particularly acute in emerging fields of technology, or in technology areas in which explosive growth is occurring. The law for determining obviousness, for example, is well developed and should be applied meticulously. A recent court opinion summed up the inquiries that must be made:

In order to determine obviousness as a legal matter, four factual inquiries must be made concerning: 1) the scope and content of the prior art; 2) the level of ordinary skill in the art; 3) the differences between the claimed invention and the prior art; and 4) secondary considerations of non-obviousness, which in case law is often said to include commercial success, long-felt but unresolved need, failure of others, copying, and unexpected results.

... the relevant inquiry for determining the scope and content of the prior art is whether there is a reason, suggestion, or motivation in the prior art or elsewhere that would have led one of ordinary skill in the art to combine the references.

Richard Ruiz v. A.B. Chance Co. (Fed. Cir. 99-1557, -1563, decided Dec. 6, 2000.) The obviousness standard properly applied screens out trivial inventions not deserving of an exclusive patent right.

To respond to the difficulties of rigorously examining patent applications in emerging or expanding technology areas, the PTO historically has made exceptional efforts, as when software inventions and genetic engineering inventions first emerged. We believe the PTO now is making headway with its special efforts to examine business method patents.

Last year the Office published an "Action Plan for Business Method Patents" that called for reasonable and appropriate steps to ensure proper examination of business method patent applications. Recently the *Wall Street Journal* cited a PTO official as saying that for the quarter ended December 31, 2000, the PTO granted patents in 36 percent of the business method applications it examined, down from 56 percent from the quarter ended March 31, 2000. This dramatic decrease in the percentage of business method applications in which patents are granted likely comes from a more careful application of the novelty and nonobviousness requirements of the patent statute and from the PTO program for obtaining more prior art documents relating to business method patents.

This Subcommittee should encourage the PTO to explore other constructive proposals that would address issues related to patenting business methods, particularly as they relate to the ability of the PTO to examine patent applications, as long as the proposals are not in conflict with U.S. law or U.S. treaty obligations. For example, the PTO should catalog and make available for searching prior art documents that are submitted and placed in the file of an individual application.

IPO supports the PTO's initiatives and encourages Congress to ensure the Office has sufficient funding to undertake these efforts without sacrificing its standards for examining applications in other technology sectors. Subcommittee members are well aware that the Appropriations Committees have withheld more than \$600 million in user fees paid to the PTO since 1992. Limited information available to the public so far on the President's 2002 PTO budget, which is scheduled to be sent to Con-

gress in a few days, suggests the Administration will propose to withhold from the PTO well in excess of \$100 million in user fees that are paid by patent and trademark applicants and owners. This practice of fee withholding has had and continues to have a damaging impact on the quality and timeliness of patent examination and PTO plans for adopting the latest information technology. We commend Chairman Coble, Ranking Member Berman and other members of this Subcommittee for their valiant efforts to obtain adequate funding for the PTO. Congressional appropriators must understand that adequate resources have to be made available to ensure a first class Patent and Trademark Office. This is a problem that affects all patent owners, but the controversy over business method patents highlights the necessity for the PTO to have the tools to allow it to issue only patents that comply with the statutory requirements.

COURT REVIEW OF BUSINESS METHOD PATENTS

If the PTO does not apply patent law properly, of course, legal recourse is available to competitors through suits in U.S. district courts, reviewable by the U.S. Court of Appeals for the Federal Circuit. Recent developments suggest the system of high quality PTO examination for business method patents combined with court review is working.

In 1998, in the first case that brought widespread attention to so-called business methods, *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*, the Federal Circuit decided Signature's data processing system is a type of subject matter that can be patented. Identified by the registered trademark "Hub and Spoke," the system facilitates a structure in which mutual funds pool their assets in an investment portfolio organized as a partnership. The system calculates totals including the true asset value of each mutual fund. The Federal Circuit said the system is not a mathematical algorithm that is a mere abstract idea, because it produces "a useful, concrete and tangible result"—a share price fixed for recording and reporting purposes. The U.S. Supreme Court declined to review that decision.

In 1999, in another widely cited opinion, *AT&T Corp. v. Excel Communications, Inc.*, the Federal Circuit ruled that a long distance telephone call billing method was not an abstract, unpatentable mathematical formula. The method allows billing of long distance callers according to whether they call someone with the same or a different long distance carrier. The patent claims the steps of (1) generating a message record and (2) including in the record an indicator with a value that is a function of which long distance carrier is used by the party that was called. The Federal Circuit concluded AT&T's process produces a useful, concrete and tangible result, and again the Supreme Court declined review.

Very recently, on February 14, 2001, the Federal Circuit decided a case involving perhaps the most-publicized business method patent, in *Amazon.com, Inc. v. Barnesandnoble.com, Inc.* The PTO granted a patent to Amazon.com, Inc. in 1999 for a "One-Click" or "single action" online ordering system, in which an item is ordered without using the "shopping cart" ordering model. The patent was severely criticized after Amazon.com obtained a preliminary injunction to prevent Barnesandnoble.com from using a similar online ordering system. In its February 14 opinion, however, the Federal Circuit vacated the injunction. The issue was whether Amazon.com had demonstrated the reasonable likelihood of success on the merits necessary for a preliminary injunction. The court examined five prior art items cited by Barnesandnoble.com that apparently were not considered by the PTO and concluded substantial questions were raised as to the novelty and nonobviousness of the patent, making a preliminary injunction inappropriate. We have no opinion on whether the Amazon.com "One-Click" patent is valid or invalid, but the Federal Circuit decision serves as a reminder that PTO and lower court errors with respect to business method patents, as with other patents, can be corrected.

GENERAL PATENT LEGISLATION

Congress could take a number of steps to improve the patent statute in general that would address concerns about the quality and timeliness of business method patents along with all other patents.

First, as noted, it is imperative for the PTO to be given adequate resources to do its job. PTO funding first and foremost is an issue affecting the quality of patents granted by the PTO. IPO supports Chairman Coble's bill H.R.740 and any similar legislation that would assure full funding for the PTO, and also supports efforts to persuade appropriators to provide adequate funding without legislation. PTO funding should be the single highest priority for patent system improvement.

IPO also would support legislation to adopt reforms in patent law that were only partially adopted in the American Inventors Protection Act (AIPA). First, we sup-

port amendment of the AIPA's inter partes reexamination procedure to permit third party reexamination requesters to appeal to the Court of Appeals of the Federal Circuit. Without an opportunity for appeal to court, inter partes reexamination will be seldom used because the third party requester will not have a level playing field. Requesters are subject to severe estoppel provisions if they elect to enter an inter partes reexamination proceeding, and yet they are denied a court appeal. Without amendment of the AIPA, most parties wishing to challenge a patent will continue to do so in U.S. district courts despite the greater expense and delay.

Second, we urge expansion of the AIPA's publication procedure to require publication of all patent applications after 18 months—not just those for which counterpart applications are filed in a foreign county that publishes applications. Publication of all applications will give competitors early notice of patent claims.

Finally, the earlier user defense established by the AIPA should include all types of earlier inventions. The enactment of the earlier user defense was not a response to concerns about business method patents. Business method patents were hardly mentioned during the several years the earlier user defense was debated. The phrase "method of doing or conducting business" was inserted as a last minute compromise between those who favored the earlier user defense and those who opposed it. The defense is important for all methods and products commercialized in the U.S. that can be protected most effectively against piracy by relying on trade secret rights.

Our association is studying a number of other possible refinements that Congress might want to consider for streamlining and simplifying the patent system and adapting it to modern communications methods. We will submit these suggestions to the Subcommittee at a later date.

Again, I appreciate the opportunity to present these comments on behalf of IPO and will be pleased to answer any questions.

Mr. COBLE. Mr. Steinberg?

**STATEMENT OF ANDREW B. STEINBERG, EXECUTIVE VICE
PRESIDENT AND GENERAL COUNSEL, TRAVELOCITY.COM**

Mr. STEINBERG. Thank you, Chairman Coble, Congressman Ber- man, and Members of the Subcommittee for the opportunity to share Travelocity.com's views on this important topic of business method patents. I do not want to be overly dramatic, but we do believe that the proliferation of these patents is a serious threat to the growth of electronic commerce, and if left unchecked, could mean that some businesses will not be able to adapt to the Internet because somebody else owns the right to conduct their business on- line. We urge Congress to take prompt action to prevent this from occurring.

Yesterday, my company celebrated its fifth anniversary, dating from the introduction of our website in 1996. We have 1,600 employees, including more than 1,000 customer service agents. We have sold more than 13 million airline tickets, millions of vacations and hotel rooms and car rentals and we have more than 25 million members. As you noted, we are the third largest e-commerce retailer, behind Amazon.com and eBay.

Now, how did we get there and why is it relevant to this? Well, our business depends on new technology and our success depends on constant innovation, providing consumers with what they want. And really, if there is one thing that distinguishes the Internet business today, it is the need to continually reinvent methods of doing business. In my written testimony, I have given the committee several examples of innovations: Calendar-based pricing system, alternate airports, dream maps which tell you where you can go for a specific price, and so on, that we think have been important to our success, but more importantly, illustrate our inventiveness.

The important point here is that Travelocity has done all these things notwithstanding the potential ability to patent them. We are doing them because they benefit our customers and give us a competitive advantage, and that is true for all companies. That is why the patent office of the United Kingdom concluded that patents on methods of doing business should not be issued, and they said, and I quote, "Many business methods are, of course, as old as business itself. The traditional arguments against patenting them are that innovations in ways of doing business are not like new drugs or pesticides, which require much costly R&D. The advantages of stealing a march on competitors, albeit temporarily, are incentive enough to seek to develop them." And I am here today to tell you that that is true from the point of view of a business that has succeeded online.

The purpose of the patent system is to encourage innovation, of course, but taking a business method that has existed in the brick-and-mortar world and allowing it to be patented because it can be improved upon or accomplished online does not serve the purpose of the patent laws, and the ease with which these patents have been obtained has spawned thousands of such applications.

Now, I want to be clear, Travelocity has some business method patents and many more in the works. That is a defensive mechanism on our part, but this has a price for us and our country, because in addition to the substantial legal costs that go with pursuing a patent application, there is also enormous programming time that you have to devote from your technical staff to getting a patent application drawn and defending office actions and so on. And, of course, as already noted, there is an effect ultimately on competition when these patents issue.

Many of us in the online travel world ran up against Priceline's business method patent on reverse auctions, and I hope if we have the opportunity to answer any of your questions, I can share with you our experience with that. But one shudders to think what might have happened if business method patents had been so liberally granted in the last half-century.

If Signature Financial Group can have a patent on the hub-and-spoke system for mutual fund investments, why not give similar protection to the original hub-and-spoke system in the airline industry pioneered by American Airlines? Indeed, if Sabre, our largest shareholder, had simply patented a method for direct sales of airline tickets through electronic means when it launched Easy Sabre, which is the predecessor to Travelocity on CompuServe and Prodigy in the 1980's, there would only be one retailer today online for travel, and that is a bad result.

Our Patent and Trademark Office is, in our judgment, overburdened by the number of these patent applications and simply does not have the resources to do the kind of review of prior art that would be necessary. We supported the American Inventor's Protection Act and believe it has improved the patent system and we congratulate the Chairman and other Members of the Subcommittee in getting this bill enacted, but we do not think it went far enough. Significant reforms are still necessary.

We are particularly concerned that business method patent claims based on Internet applications of well-known brick-and-mor-

tar business techniques be given greater scrutiny and that the patent system permit a more efficient way for those of us in the business community to challenge the validity of a patent grant without excessive cost. The Business Method Patent Improvement Act, introduced by Congressmen Berman and Boucher in the last Congress and reintroduced yesterday, we think would be yet another significant advance in addressing this problem, and with a few minor suggestions, we would urge the Subcommittee's favorable review of this bill.

We believe in particular that the requirement that business method patent applications be published after 18 months is the right approach. Because of the difficulties in producing tangible evidence of prior art of a business practice, we also think that the preponderance of evidence standard in the bill is a reasonable burden to place on patent challengers. We also endorse the bill's inclusion of a rebuttable presumption of obviousness for any patent claim that merely takes an existing practice and uses a computer technology. We do think the bill should apply retroactively, and I have a couple other suggestions I would be happy to make during our question and answer session.

Mr. Chairman, the Internet and electronic commerce are still in their formative years and if significant areas of commerce can be occupied by dubious patent claims, the growth and utility of the Internet will be harmed. Ultimately, I do think it might be necessary for Congress to look at the United Kingdom's solution and simply prohibit patents on methods of doing business. But in any event, we believe urgent action is necessary now and we endorse the bill that was reintroduced yesterday. Thank you for the opportunity to speak here this afternoon.

Mr. COBLE. Thank you, Mr. Steinberg.

[The prepared statement of Mr. Steinberg follows:]

PREPARED STATEMENT OF ANDREW B. STEINBERG

Chairman Coble, Congressman Berman, and Members of the Subcommittee, my name is Andrew B. Steinberg and I am Executive Vice President and General Counsel of Travelocity.com, which operates the world's largest on-line travel web site. I appreciate the opportunity to share the views of my company with you this afternoon regarding the important subject of so-called business method patents. We believe that the proliferation of these patents represents a serious threat to the growth of electronic commerce and, if left unchecked, could impede the ability of many businesses to adapt to the Internet. We urge Congress to take prompt action to prevent this from occurring.

To establish the right context for my testimony, I think it may be helpful to provide a bit of background about our business and a glimpse of what we are doing today to change the way our customers shop for and purchase travel services.

Travelocity yesterday celebrated its fifth anniversary, dating from the introduction of our web site in March 1996. Travelocity today employs nearly 1600 persons, including more than 1,000 customer service professionals. We have sold more than 13 million airline tickets and registered more than 25 million members. Earlier this year we announced that our operations will be at or close to cash profitability by the end of this fiscal quarter and will thereafter be profitable for the full year 2001. As measured by the number of unique visitors arriving at our web site each month, we rank as the third largest e-commerce retailer on the Internet, behind Amazon.com and eBay.

Five years of operations gives us a long history when compared to many Internet companies but, in fact, Travelocity was not "invented" in 1996. The introduction of a consumer-direct travel reservation service on the Internet was a natural outgrowth of the computerized reservation systems business, originally pioneered by Sabre Inc. and other companies over more than two decades. The Travelocity busi-

ness unit grew from within Sabre, and was originally referred to as "Sabre Interactive." SI, as it was then known, had operated easySabre since the 1980s, when it was introduced as a service on several dial-up networks, such as Prodigy and Compuserve. (Travelocity is now a separate, publicly traded company, with Sabre as our majority shareholder having approximately a 70% interest in the business.)

Today, Travelocity.com is as much a database-driven travel marketing and transaction company as an online travel agency. Like many travel agencies we offer consumers a wide array of services—in our case from more than 700 airlines, 50,000 hotels and 50 car rental companies. We also offer several thousand vacation packages, tour and cruise departures. But unlike a traditional travel agency, our customers can book directly on the Internet (using devices ranging from personal computers, to wireless web phones, to PDA's like the Palm VII). They don't see static brochures but rather a vast library of interactive destination and related content, which we continually update. We have a national brand. We offer a comprehensive shopping experience. We provide travel suppliers with the opportunity to place point-of-sale advertising and context-sensitive promotions. And within our vast membership, we can target customized offers to millions of users and reach them instantaneously via email.

As you can see, our business at its core relies on technology and our success depends on constant innovation and information that consumers want. Indeed, if there is one thing that distinguishes the business environment today from that which preceded the commercial use of the Internet, it is the need continually to reinvent methods of competing and doing business. I outline for the record below several innovations that we believe have been important to our success. And although we do have several patents, and of necessity many more in the works, my firm view is that Travelocity has offered these innovations *notwithstanding* the potential ability to patent them—we're doing these things because they benefit our customers and give us a competitive advantage. Certainly in our case, business method patents have been neither a prerequisite to nor even a catalyst for innovation.

I'd like to outline briefly some of these exciting innovations, all of which we introduced as a way of convincing our customers of the benefits of planning and booking their travel online rather than relying on the telephone.

BEST FARE FINDER

Best fare finder is a revolutionary new tool that has turned the airline-developed pricing and yield management system on its head. Let me explain. I'm sure every Member of this Committee has had experience with the traditional way of searching for airline flights. A customer sees an advertisement in the newspaper for a \$199 roundtrip fare, and calls the airline and asks for the fare. The agents then tell the customer that it is not possible to search by fare, only by flight and date of travel. And once the customer picks a flight, the \$199 fare may or may not be available. Travelocity technology lets its customers search for the lowest fare in a market, and then choose travel dates from a calendar that is highlighted to show when a seat at that fare is actually available for purchase.

ALTERNATE AIRPORTS

Since many Members of Congress fly every week, I suspect you are aware that fares from some airports may be inexplicably higher than fares from others. Recognizing that our customers are looking for the lowest fare, we inform our customers when they can save money by traveling to an alternate airport. For example, if you searched for a flight between Reagan National and Los Angeles, you might at the top of the flight results screen on your computer a notice that by driving the 40 miles to BWI, you could save \$200. We do this by automatically comparing fares from alternate cities to ones in the cities that the customer has requested. Most leisure travelers would be happy to drive to Baltimore to save \$800 for their family of four.

DREAM MAPS

Recognizing that the price of an airline ticket has no correlation to the distance traveled, we've developed a product called Dream Maps. If you have \$300 to spend on a ticket, Travelocity will show you on a map everywhere you could go for \$300 or less. We now customize our maps to focus on particular interests (such as ski areas, national parks, or Caribbean beach destinations in the appropriate time of year).

If there is one lesson we have learned, it's that our customers aspire to control their travel decisions from start to finish. If we are to persuade them to book online, we must provide them with tools they cannot have offline. That's really what Travelocity is all about. One of the ways we do this is by giving our customers the tools to choose their own seat on an airplane. We bring up a seating diagram, and let the customer choose the exact seat he or she wants. We do the same thing with cabins on a cruise ship, providing pictures of what an actual cabin looks like before a customer makes a purchase decision.

I provide these examples, again, to illustrate that the innovation underlying our success was critical to our business and one can reasonably expect that we would have done exactly what we did—as part of our transformation into an on-line travel agency and then a database-driven marketing and transactions company—regardless of our ability to patent each of these advancements.

Mr. Chairman, the purpose of a patent is to encourage innovation. Rather than keeping secret a new invention that will benefit consumers, a patent allows an inventor to share that invention so that others can exploit it while still maintaining proprietary rights in the invention and the appropriate benefits that come with that. I question, however, whether many of the business method patents that have been issued for activity on the Internet accomplish this goal. Certainly, a mechanical process in the offline world can be patented. But taking a commercial process or business method that has existed in the brick-and-mortar world and allowing it to be patented because it can now be accomplished or even improved online does not serve the purpose of the patent laws.

To demonstrate that point, and to show the perverse results of the current permissive policy toward business method patents, I would like to discuss the subject of auctions. Public auctions took place as early as ancient Greece, and have been used for products ranging from tobacco leaves to fine art. This traditional concept of an auction has been applied to the Internet arena with great success. Founded in September 1995, eBay today is the world's largest online trading community with 18.9 million registered users, and is among the most popular shopping sites on the Internet according to the Media Matrix September 2000 web report. eBay continues to grow rapidly. To my knowledge, eBay does not have an overarching business method patent on online auctions, and plenty of other Internet sites, including Yahoo!, CNet, Amazon, ZDNet, and Excite have established online auctions. The result is ferocious competition among the various industry participants to see who can provide the best auction service. Today, millions of people participate in and benefit from online auctions, taking advantage of the breadth of the Internet.

I believe this could never have happened if one of the players had a business method patent on the online auction. Why? Compare the success of the traditional online auction to so-called "reverse auctions." In a reverse auction, the buyer announces his or her preferred price, and sellers are allowed to bid in response. Of course, like the traditional auction, reverse auctions have existed in various forms in the offline world, including the Dutch auction. But when Walker Asset Management was issued U.S. Patent No. 5,794,207 on August 11, 1998, it was clear that there would be no widespread implementation of or technology competition as to reverse auctions over the Internet.

The Walker Asset Management patent, which is used by Priceline.com, is described as "method and apparatus for a cryptographically assisted commercial network system designed to facilitate buyer-driven conditional purchase offers." Let me translate: a customer says he is willing to pay \$250 for an airline ticket between Greensboro-High Point, North Carolina and Las Vegas, Nevada departing on April 14 and returning on April 17. If that price offer is acceptable to one of Priceline's participating carriers, the customer's credit card is charged and the ticket is issued. If it's not acceptable, the customer's offer is declined.

The airline inventory that Priceline is selling is not necessarily unique. But because Priceline.com has enjoyed a well-publicized patent on "name your own price on-line," few companies have entered the field of reverse auctions via the Internet, lessening the amount of technical innovation. Moreover, the patent has effectively limited the methods by which discounted or last-minute travel inventory can be presented to consumers.

At Travelocity, we had two choices. Although we doubted the validity of the Walker Asset Management patent, we would have risked being sued. That's what one of our competitors, Expedia, chose to do, setting up a hotel reservation system that Priceline then alleged violated its "name your own price" patent. Priceline filed a patent infringement suit against Expedia, and after presumably significant expense to both sides, the case was recently settled.

We chose a second path. We reached a marketing referral agreement with Priceline, in which Travelocity customers who wished to name their own price for an airline ticket could follow a link to Priceline. Priceline customers whose offers were not accepted and who wished to search for fares and flights in the usual way were provided a link to Travelocity. This agreement was not a license. We did not concede the validity of the patent. However, by reaching a marketing referral agreement with Priceline, we avoided the costs that might have been involved in contesting the "name your own price" patent. Of course, there were several factors behind our agreement with Priceline but certainly an important factor was our reluctance to deploy a reverse-auction capability ourselves and possibly become involved in a protracted and expensive lawsuit.

The relative ease with which business method patents can now be obtained has spawned thousands of such applications. No prudent business would allow its competitors to patent key business processes without attempting to obtain some patents of their own. And so we, and virtually every other large Internet company, must accept the law as it is and aggressively attempt to obtain patents wherever we can. This has a price for our company and our nation: in addition to the substantial direct legal costs of prosecuting new patent applications, one must consider in such circumstances the enormous time that technical and programming staff devotes to a patent application, taking them away from developing the kind of innovations I outlined above.

The experience with reverse auctions is just one of many illustrations of how business method patents don't make much sense. One shudders to think what might have happened if this kind of patent had been liberally permitted throughout the last half century. If Signature Financial Group is permitted to obtain a patent on the hub-and-spoke system for mutual fund investment allocations, shouldn't similar protection have logically been available for the original hub-and-spoke system of the airline industry? If electronic coupons distributed online can be patented, then what of paper coupons? Indeed, if Sabre had simply patented a "method for direct sales of airline tickets through electronic means" when it launched easySabre in the 1980s, there would today be a single online retailer for travel. Obviously, these results would have been bad for consumers.

I think our experience is representative of a larger problem. I read with interest the article in Friday's *Wall Street Journal* about the continuing saga of the "inventor" who is suing the American Red Cross for violating his business method patent on online fundraising. The number of patents issued with the word "Internet" in their description has skyrocketed since *State Street*. Our Patent and Trademark Office is clearly overburdened by the huge number of patent applications for business methods and, lacking the resources to conduct a thorough prior art review for each such application, the results are predictable.

In order to remedy this situation, Congress and the PTO must institute some basic changes to the procedures by which business method patents are examined as well as providing more meaningful opportunity for the affected business community to challenge the validity of a business method patent claim.

As a threshold matter, we do not accept the contention that business method patents are no different than any other patent. Clearly, these patents can be distinguished from more traditional patents, and are already subject to different rules than other patent claims. For instance, pursuant to the American Inventors Protection Act, supported overwhelmingly by this Committee and enacted into law last Congress, business method patents may not be enforced against prior users. The PTO's Business Methods Patent Initiative also properly recognizes these patents as a distinct class.

We wholeheartedly supported the American Inventors Protection Act, and believe that this legislation has significantly improved the American patent system. We congratulate the Chairman and other Members of the Subcommittee on their role in its enactment. However, as the Members are well aware, this bill did not go as far as it might have in improving the patent system. For instance, reform of the PTO's funding mechanisms and publication of all patent applications continue to be priority matters for Congress to address.

In addition, within the specific area of business method patents, significant reforms are necessary. Most importantly, the patent process for business method patents must be more transparent and provide greater opportunity for input by experts and those knowledgeable in the field. Many of these applications are highly technical or involve the identification of "prior art" that may not be easily unearthed by a patent examiner.

Business method patent claims based on Internet applications of obvious or well-known "bricks and mortar" business techniques should also be given greater scrutiny than a truly novel business method claim. Merely transferring a familiar or ob-

vicious process into a new communications medium should not provide an "inventor" with a twenty-year monopoly on that procedure. In the dynamic and innovative world of the Internet, transient monopolies and the leverage of "first movers" are common phenomena. However, if these nascent powers are given exclusive control over a mode of business by *statute*, then innovation, consumer choice, and competition will founder. Congress and the PTO should be reluctant to provide this monopoly status without a fair degree of certainty that the patent claims are valid.

Finally, the patent system should permit a more equitable means of challenging the validity of a patent grant. For instance, as I have discussed, we are convinced that the "reverse auction" patent was wrongly issued. However, in order to vindicate our position we would be forced to initiate litigation that would likely end up costing our company hundreds of thousands of dollars, if not millions. For a company striving to achieve profitability, such a significant charge on our earnings without any assurance of success is not a good investment. Other companies and developing start-ups in our industry have even fewer resources upon which to draw. There ought to be recourse other than the costly path of litigation to discharge this flawed patent. Sensible legislation would release competitive forces in this stagnant area of business.

We recognize that the Patent and Trademark Office has undertaken steps to address some of the complaints regarding business method patents. The PTO reports that it has hired additional, highly qualified examiners, and that it is providing added educational and training assistance for these examiners. Improving the Scientific & Technical Information Center—Electronic Information Center and supplementing other PTO resources are also important and useful undertakings. The PTO is also apparently reviewing patent review guidelines and procedures, which is obviously necessary.

We think the recommendations put forward by the American Intellectual Property Law Association are helpful, though they don't go far enough. Many of these echo efforts already underway in the PTO, but their legislative proposals are also noteworthy. AIPLA has also proposed amending current law to provide for early reexamination of patents with a right of judicial appeal by a third party, and with no estoppel attaching to PTO determinations not reviewed by the court. While the reexamination process is often biased in favor of patent holders and appellate litigation is often a difficult and costly proposition, third parties should at least have the option to actively participate in these proceedings and should not be prejudiced in court by determinations made by the PTO Board of Patent Appeals and Interferences. AIPLA's proposal would be an improvement over current law, but likely would not provide an adequate remedy to this problem.

Separately, we also strongly support the longstanding efforts of AIPLA, the Committee, and others to restore all patent fees to the use of the PTO, rather than having them diverted to the general Treasury. Patent owners and applicants should not be forced to fund unrelated government programs, particularly in an era of budget surpluses. Such a "tax on innovation" is intolerable in a nation that thrives on the power of its ideas and ingenuity.

At bottom, we believe even more must be done to resolve the problems we are addressing in this hearing. Legislation introduced by Congressmen Berman and Boucher in the last Congress, H.R. 5364, the Business Method Patent Improvement Act, would be a significant advance in addressing this problem and we urge the Subcommittee's favorable review of such a bill in the current session.

The publication of business method patents after 18 months is sound policy and consistent with the laws of nearly every other world economic power. We regret that this did not become law in the last Congress. By publishing all business method patents after 18 months, experts in the relevant field will have a timely opportunity to raise issues before the PTO and submit prior art, as provided in the bill. The bill also permits members of the public to request that the PTO hold a hearing to determine whether the business method was known or used, or was in public use, or on sale in the U.S. prior to the filing of the application. Such hearings would be very useful in bringing relevant prior art and expert views before the PTO before a patent claim is granted.

The Berman-Boucher bill also creates a desperately needed post-grant opposition procedure for business method patents. While third parties objecting to patent claims do have the ability to avail themselves of the existing reexamination procedure, this process is profoundly biased in favor of the patent holder, and does not provide the challenger a meaningful opportunity to participate in the proceedings or raise all relevant challenges. Conversely, the Berman-Boucher bill creates an expert tribunal, with ample evidentiary rights for all parties. This process would be far less burdensome and costly than judicial litigation, would be concluded within

18 months of its initiation, and would still offer the opportunity for a judicial appeal for either party.

We would point out several areas for improvement in the legislation. Parties to the opposition proceeding are estopped from raising matters adjudicated in that proceeding. We would urge that the legislation be amended to permit de novo review of any issue in a subsequent judicial appeal.

Another vital reform in this legislation is the modification of the burden of proof with regard to business method patent claims. Whereas now a third party must produce "clear and convincing" evidence to invalidate a claim, the Berman-Boucher bill would permit a successful challenge upon a showing by a "preponderance" of the evidence. Because of the inherent difficulties in producing tangible evidence of prior art demonstrating a business practice, particularly in the transient world of the Internet, the "preponderance" standard is a much more reasonable burden to place on a patent challenger.

We would go one step further. In addition to modifying the burden of proof for those contesting a business method patent, we believe that the Congress should consider adopting the English rule of attorneys fees for such contests. That is, the prevailing party in any dispute over the validity of a business method patent should be entitled to recover its attorneys fees. This would discourage those with such patents from prosecuting infringement actions that did not have a high probability of success and would encourage those with limited resources to pursue a contest, and would likewise deter frivolous challenges.

Finally, the Berman-Boucher bill creates a rebuttable presumption of "obviousness" for any patent claim that merely implements an existing practice with the use of computer technology, which we support. While this would seem to be a simple proposition, Travelocity's experience with online patents leads us to believe this clarification is needed.

While we believe passage of this legislation would vastly improve America's patent system and would prevent many of the abuses we have experienced in the past, we remain concerned that the bill does not go far enough to rectify problems that would predate its enactment. We recognize that there may be due process and takings issues and difficult administrative complexities in resolving problems with existing patents, but we do not believe this should absolve Congress from confronting the problem. Clearly, there are a number of dubious patents that would not be subject to this bill, and we do not believe that the marketplace should be forced to deal with these aberrations for 20 years. The Internet and electronic commerce are now in their formative years and if significant market spaces continue to be occupied by dubious patent holders, the growth and utility of the Net will be severely harmed.

Another potential avenue of relief could be congressional clarification of the "misuse" defense to patent infringement. Under this recognized legal defense to infringement, the holder of a patent that is valid may still be required to license it broadly on reasonable terms if that business method is the only efficient means to conduct a particular process. By invigorating this defense in the field of business method patents, Congress would enliven competition in various fields dominated by companies who have obtained patents on processes for which there is no viable substitute.

Many scholars and practitioners have called for the elimination of all business method patents. Recently, the Patent Office of the United Kingdom, after extensive consideration, chose to preclude the issuance of patents on methods of doing business¹. The office's logic was compelling:

"Business methods are of course as old as business itself. The traditional arguments against patenting them are that innovations in ways of doing business are not like new drugs or pesticides which require much costly R & D. The advantages of stealing a march on competitors, albeit temporarily, are incentive enough to seek to develop them. Moreover the nature of business methods can lead to very wide patents—a patent for a particular sales method can affect all the sectors in which that sales method might be useful . . .

There is no sign, at least to date, of a want of innovation in computer-implemented business methods, and nor was there in the US before business methods became patentable in 1998. Intense innovation has characterized this field. The Government's conclusion is that those who favour some form of patentability for business methods have not provided the necessary evidence that it would be likely to increase innovation."

¹ See <http://www.patent.gov.uk/about/consultations/conclusions>

Ultimately, it may become necessary for Congress to go as far as the UK in order to rectify the current problems with these patents. We do believe that urgent action is necessary and that significant harm could occur to important sectors of our economy if current policies and practices remain in place. The PTO has taken positive steps toward addressing the shortcomings in its review process, and some progress has been made. Other proposals to modify the examination and post-grant challenge process, such as those by AIPLA and Congressmen Berman and Boucher, should also be quickly adopted.

Mr. Chairman, Congressman Berman, thank you for the opportunity to appear before the Subcommittee this afternoon. I'm pleased to answer any questions you and your colleagues may have.

Mr. COBLE. Thanks to each of you. The red light also applies to us, so let me start my race with the red light and put a series of questions to each of you, starting with Mr. Godici and working to my left.

This is a rhetorical question, but I want to spread your answers over the record to give us yet one more bit of fortification in our defense to protect the fees of the PTO. Do you all concur with me that the PTO fee diversion should be stopped dead in its tracks?

Mr. GODICI. Mr. Chairman, obviously——

Mr. COBLE. Or maybe I am not going to get the answer I wanted. [Laughter.]

Mr. GODICI. Any organization would welcome more resources to do the job, and if the USPTO got additional resources, we would apply them to better quality examination, more timely examination, and investments in infrastructure. We do look forward to working with the new Administration, particularly at the Department of Commerce and OMB, on the issue of fee retention at the USPTO.

Mr. COBLE. Mr. Kirk?

Mr. KIRK. Yes.

Mr. MYRICK. Very simply, yes.

Mr. COBLE. Thank you, sir.

Mr. STEINBERG. Yes.

Mr. COBLE. Thank you, gentlemen. And I have talked with the administration, too, Mr. Godici. I will get to that later.

Pardon our immodesty, but we are proud of the American Inventors Protection Act. Most of us worked very diligently on that. But I suspect you all are of the opinion that AIPA, even though a good start, there still needs to be further patent reform for this modern economy, do you not? Do each of you agree with that or not? Mr. Godici?

Mr. GODICI. I believe that there are some issues that could be worked on with respect to the AIPA. I think Mr. Kirk and Mr. Myrick mentioned the fact that strengthening the reexamination process that was started in AIPA is something that may merit consideration, as well as some way for the USPTO to look at prior art that comes in after the granting of a patent to give us a second chance with respect to second examination.

Mr. COBLE. Mr. Kirk?

Mr. KIRK. Mr. Chairman, as I noted in my written statement, we think the reexamination provisions are deficient. We would propose either strengthening them and/or adding a post-grant opposition similar to the one that Mr. Berman introduced yesterday, the 18-month publication for all patent applications—again in your earlier bill, but not limited to business methods—and thirdly, to extend

prior user rights across the board for all patents and all inventions, not just business methods. Thank you.

Mr. COBLE. Mr. Myrick?

Mr. MYRICK. Yes, Mr. Chairman. In my concluding oral remarks, I also mentioned the same three items, so I would wholly support that.

Mr. COBLE. Thank you, sir. Mr. Steinberg?

Mr. STEINBERG. Yes, as well. We think the bill is a good start, but there is room for more reform. In particular, we think that the process for reviewing business method patents needs to be more transparent and provide a greater opportunity for input by experts and those knowledgeable in business.

Mr. COBLE. Again, I think I know the answer, but I want it for the record, gentlemen. I will start with you, Mr. Godici. Do you all believe that *State Street* should be overruled, the *State Street* opinion?

Mr. GODICI. I think that the *State Street* opinion clarifies for the USPTO and clarifies the U.S.'s position with respect to the interpretation of laws that you have promulgated with respect to eligibility for patenting. I believe that it is the position of the U.S. PTO that our job is to administer those laws, and it is very clear from that decision what our job is to do here.

Mr. KIRK. No, Mr. Chairman, we do not think that *State Street* should be overturned. We think it was a very sound decision and, in its very analytical approach to how the patent law should be interpreted, we think clarified the law. Thank you.

Mr. MYRICK. Mr. Chairman, the IPO position is that *State Street* merely elucidated that which was already the law and just had been misunderstood before, because business method patents had been around for a very, very long time, long before *State Street*.

Mr. COBLE. Thank you, sir. Mr. Steinberg?

Mr. STEINBERG. I guess I am the holdout on this. I do not think the case was necessarily wrongly decided, but I think that it is Congress' task to look back and say, what is the real purpose of the patent system and what ill effects are coming from the patenting of these business methods. So I would certainly support legislation that would overturn that decision. That is not what we believe is currently on the table, but that is how we feel about it.

Mr. COBLE. I see my red light has not yet appeared, but it is imminent. Before I recognize Mr. Berman, there is a vote on now, but I think we will have time for Howard to question you all during his 5-minute period.

Let me conclude by sharing this with you. I think I told Mr. Berman this earlier, speaking on the diversion of fees. I was speaking with someone on the Hill recently who defended this practice and she said to me, she said, "I do not like your use of the word diversion. Use another word," she said. I said, "Would legalized larceny be better?" [Laughter.]

Mr. COBLE. "Oh, no, she said, you may go back to diversion." So I feel strongly about that. Thank you all for your answers.

I am pleased to recognize the gentleman from California. After Mr. Berman's questioning, gentlemen, we will depart and go to the floor, where I am told there will be three votes, which means we will be away about 20 minutes, probably. Mr. Berman?

Mr. BERMAN. Thank you, Mr. Chairman.

I think, first, Mr. Steinberg made an offer which I will take him up on, because sometimes the specific helps us to understand the general.

Mr. COBLE. If the gentleman will suspend, Mr. Berman, I am now told there will be only one vote, so that means we will not be away that long. You may proceed, Mr. Berman.

Mr. BERMAN. Right. They will have the second and third vote as soon as we get back here. [Laughter.]

Mr. BERMAN. You thought that the Priceline reverse auction patent was invalid, but you decided not to challenge it. I think it would be instructive for the Subcommittee Members to hear further why you chose not to challenge the patent, and can you describe the options for challenge that would have been available, why these were unpalatable, and can you relate the barriers that exist to a successful challenge, and what are the costs of such a challenge and how do they affect a business like yours?

Mr. STEINBERG. Thank you. I would first like to answer that by talking about a comparison, which is in my written testimony, between what has happened in the area of auctions online and reverse auctions online, because I think you have a very good control test there.

eBay, of course, is the pioneer and the largest online company that conducts auctions, but there are also auction sites at AOL and Yahoo! and a bunch of other companies. There is EDNET and some others. As a result, there has been tremendous competition, technical innovation on auction technology. They are all going out after each other. There is no overriding patent that eBay can claim to prevent others from doing online auctions.

Of course, with the case of the Priceline patent and reverse auctions, that is not the case. In a reverse auction, as you know, the buyer announces the price that he is willing to pay. The sellers are allowed to respond. This is traditionally referred to as a Dutch auction, but when Walker, I think it is called Walker Asset Management, got its patent, it was clear that there would be no such competition over the technology for implementing reverse auctions online, and I think if you now look online, you will see that really only Priceline uses this technology, with one exception which I will come to.

In our case, we looked at the Priceline patent. The airline inventory that they have is not unique, but because they had a patent, in effect, we decided to stay out of the market. We really had two choices. One was to do what our competitor, Expedia, which is another large successful online travel company, did. They ignored the patent and they put up a name-your-own-price hotel function, and then Priceline, which, of course, in those days was a company with a \$150 billion market capitalization and lots of patent lawyers running around the globe, sued them. Presumably, Microsoft and Expedia made the decision that they would simply take such a lawsuit.

We did not believe that that was a good course for us. I did not want us to get sued, so we chose a different course. Instead, we set up a customer referral program with Priceline. That had a real effect on the utility of that product because we could not integrate

it into our site, and if you go on our site, you will see it is just a referral to Priceline. So we were never given the chance to improve on that technology.

Mr. BERMAN. Do you get a referral fee?

Mr. STEINBERG. We both get referral fees. But the point of this is that the result of the patent was to discourage innovation by us and by others, because there are no other competitors for name-your-own-price technology now. So I think we were between a rock and a hard place. We chose to do a customer referral deal with Priceline. We like them. They are good partners to work with. But I do not think it is the right result as a matter of public policy. I think we should have been able to compete with them on the same basis.

Mr. BERMAN. So, fundamentally, your point is that here is a case where the patent works against the innovation that patents were designed to encourage.

Mr. STEINBERG. Absolutely. There is no question in my mind had that patent not been out there, we would have implemented a name-your-own-price function, and I would like to think with our track record we would have improved on the functionality of it and there would be more choices, rather than fewer choices, for consumers to—

Mr. BERMAN. And your contrast with the regular auction is that eBay, even though they were the first mover and apparently still the largest, did not seek to patent the Internet version of or implementation of an auction, a computer-implemented auction—

Mr. STEINBERG. I do not know—

Mr. BERMAN [continuing]. And so other companies could come in.

Mr. STEINBERG. Congressman, I do not know whether they tried. They do not have a patent that I am aware of, an overarching patent that would prevent anyone from doing auctions online. Hopefully after some legislation is adopted, they would not be able to get such a patent.

Mr. BERMAN. I am curious. I almost want to ask the Patent Office if they are familiar with the history of this patent application, and whether it was because you thought that no one had ever come up with the idea of a reverse or Dutch auction before and that there was, therefore, no prior art and that this was truly novel, that you decided to issue that patent, or is that beyond you—

Mr. GODICI. It is kind of difficult for me to make remarks with respect to a specific patent and the validity of a specific patent. Filings are now at about 300,000 a year, so—

Mr. BERMAN. Is it discretion or just lack of information about that specific one?

Mr. GODICI. Well, actually, our patent examiners are very well versed in the statutes that they apply toward the examination and whether or not a patent is eligible for patenting.

Mr. BERMAN. My time has expired. I have more questions, but perhaps we will have a chance for a second round.

Mr. COBLE. I hope we will have time for a second round. The Subcommittee will stand in brief recess and we will return imminently.

[Recess.]

Mr. COBLE. We will start our second round. We are going to be interrupted again pretty soon.

Let me put another question to you guys while we are waiting for the rest of the crew to come in here. Under the law, Mr. Director, the director has the ability to initiate a reexamination of an intellectually defective patent. It is my belief that this is rarely used or used infrequently. If the media claims that there are so many defective patents in the business method area are accurate, why is the procedure not used more frequently?

Mr. GODICI. The procedure you are talking about is the Director-ordered reexamination, and the criteria for ordering a Director-ordered reexamination is discovery of pertinent prior art that would render one or more of the claims invalid in that patent. We also have another procedure where a third party, an interested third party, can send to us prior art and we will consider it in the normal reexamination process.

But you are right, it is fairly infrequent that the Director-ordered reexamination route is used. If there is some controversy with respect to a patent and it is valuable to a third party to bring it to our attention, it is normally through the route of a normal reexamination procedure by the third party.

Mr. COBLE. Let me put this question to each of the four of you and then I will recognize Mr. Berman for a second round. Do you all believe that the Congress should pass special laws for business method patents or should any changes be across-the-board changes? We will start with you, Mr. Director.

Mr. GODICI. I think that, administratively, we are on the right track in terms of dealing with business methods. I think that we ought to allow those procedures and the initiative that we put into place to work to see if it satisfies what the users of the community need. If we are going to look at modifications with respect to legislation, I think across-the-board modifications along the lines of looking at the reexamination process or post-grant opposition are things that would be valuable to the system.

Mr. COBLE. Mr. Kirk?

Mr. KIRK. We would strongly prefer across-the-board equal application to all areas. Thank you.

Mr. COBLE. Mr. Myrick?

Mr. MYRICK. Precisely the same. Changes should be adopted which can be applied generally.

Mr. COBLE. Mr. Steinberg?

Mr. STEINBERG. The holdout again, I am afraid. I think that they should be treated differently. The existing law already acknowledges some differences. Business method patents, I think, are the ones that are subject to the greatest area of abuse. They are the closest things that are out there to patents on mere ideas. If you read some of these patents, you can see that the invention really is not describing a practical way to implement the so-called invention. It is describing an idea, which many times you already had, and then it is sort of reverse engineered. From the idea comes some drawings to support the idea, and from the drawings comes a very fancy name so that a patent on reverse auctions becomes a method and system for identifying buyer aggregated demand and a computer, you know, et cetera.

So I think a lot of these things are invalid almost on their face, and I think it is noteworthy, too, that the United Kingdom, which has a long history of protecting against patent monopolies, from which our patent laws were born, has concluded that methods of doing business simply should not be patentable. So we would support that approach.

Mr. CORLE. Thank you, gentlemen.

The gentleman from California?

Mr. BERMAN. Thank you, Mr. Chairman.

I am struck by this whole issue of we are on the right track, we are focusing more on the individual business method patents, we are granting fewer than we used to grant. The implication of that is you have granted some bad ones in the past. This whole issue of prior art—all right, perhaps you are not familiar with that specific reverse auction patent, but one did not need a huge amount of resources to conclude there was prior art on the subject. My favorite is the one where—the patent for a method for combing your hair to hide baldness, where I do believe there is prior art. [Laughter.]

Mr. STEINBERG. Many of us are infringing on a regular basis.

Mr. BERMAN. And perhaps ongoing infringement. [Laughter.]

Mr. BERMAN. Perhaps any of the three of you could address—let us take this issue of the patent on the reverse auction. Why was that a good idea? What about these arguments that a better way to conduct an Internet reverse auction is being chilled or killed by virtue of the existence of that patent, the comparison with the situation, the vibrancy, the competition, and the innovations that are constantly made in the auctions as opposed to these reverse auctions. I would like to hear the three of you respond to Mr. Steinberg's points there.

Mr. KIRK. Let me say first of all, Mr. Berman, that we would not come here and tell you that we believe that every patent that is ever issued in any field is valid. With over 3,000 examiners, there are going to be some mistakes made. Let us all acknowledge that. The goal is to try to do the best job possible.

With respect to the specific question you asked, I would relate it, I think, to pioneer patents in other fields, and let me hasten to add, I am not calling the reverse auction patent a pioneer patent. I am not commenting on the validity of that patent at all. I am just commenting in general.

If you have a pioneer patent in a particular field, one could easily say a couple of things. Number one, if it is truly a pioneer patent and it broke new ground, it will indeed block a lot of other activity following that particular patent because it is a pioneer and it will likely be a fairly broad patent. That is not to say, however, that people cannot work in this area and try to develop improvements. If, in fact, other develop improvements on this pioneer—whatever it is—process, product, or whatever, they can obtain patents if their inventions satisfy the patentability criteria.

So work can continue. Patentees, being commercially oriented and seeing a patent that will perhaps erode some of their market, can get very friendly in terms of cross-licensing, so additional development work can proceed. I therefore do not believe that a pat-

ent would necessarily preclude all further work to develop improvements.

Mr. BERMAN. Mr. Myrick?

Mr. MYRICK. Mr. Berman, I would just say, somewhat along the lines of Mr. Kirk, that the patent system assumes that early patents in given areas will have some competitive impact. That is a given with the patent system. But it is also the reason why the patent system exists, to provide an innovative or a support, shall we say, for the further development of innovation in a given area by rewarding the early inventors certain exclusive rights.

I think back to the basic example we have used for years of the chair and the rocking chair. The first chair that was developed and was patented—let us assume it was—excluded everybody from making chairs for 20 years from the filing date, assuming the law existed as it does now. Did that stop everybody from making and innovating rocking chairs? No. They dreamed up making a rocking chair even though they might become an infringer of the chair patent by doing it, but also by doing so, they probably interested the maker of the chair or the chair patent holder in a cross-license to make that improved chair, that rocking chair, because it would expand his market as well as it would expand the market of the second patentee to have a cross-license and to be able to make both products and so forth.

That is the way the patent system does generate more innovation. It provides rewards to both the original patentee and the improver patentee.

So when you say—I have no idea whether the reverse auction patent is valid or not, but assuming arguendo it is, I do not believe that that patent completely covered the entire field of all possibilities for how you can do innovative selling on the Internet. There are lots of other ways to do innovative selling on the Internet, and the mere fact that somebody has not come up with those innovative ways of selling on the Internet is just a latent opportunity that is waiting out there for somebody to develop something that will be of interest enough to the public to use that new method and perhaps even interest enough to those who own the patent on reverse auctions to take a cross-license.

Mr. BERMAN. Mr. Chairman, I would like to at some point, if we have a chance, like to hear Mr. Steinberg's response to those comments, but I think since Mr. Boucher did not get his first round, I would like to stop my questioning and let him have a chance.

Mr. COBLE. Let me have a bench conference with my teammates here a minute. Mr. Boucher says that 5 minutes will be sufficient for him, in which case we can excuse the panel, unless, Howard, you want to come back after we vote, and I yield to whatever you guys want.

Mr. BERMAN. I would like to just verbally ask two questions, which to the extent people on the panel would like to answer them in writing afterwards—

Mr. COBLE. Sure. That will be fine.

Mr. BERMAN [continuing]. Rather than hold everybody here for the two more votes, so I will do that just after Mr. Boucher.

Mr. COBLE. The gentleman from Virginia.

Mr. BOUCHER. Thank you very much, Mr. Chairman. I will be very brief.

I think that we have examined thoroughly the subject matter today—

Mr. COBLE. If the gentleman would suspend, Mr. Boucher, in case we do not get to put both questions from Rick or Howard or me, we will correspond with you all in writing subsequently. Mr. Boucher?

Mr. BOUCHER. Thank you, Mr. Chairman. I think we have thoroughly covered the subject matter and I want to thank our witnesses for their well-prepared and delivered statements today and their responses to the questions. I particularly want to thank you, Mr. Steinberg, for bringing to us a real world example of how a business method patent has occupied an entire field and served to inhibit competition in that field and innovation in that field, and I hope our Subcommittee will take to heart that very helpful example.

Mr. Kirk, let me ask you a little bit about the TRIPs. You mentioned that in your testimony. Do you believe that business method patent protection is required to be extended in accordance with TRIPs?

Mr. KIRK. I think one can make a very good argument that if you look at Article 27.1 of TRIPs, which states, "Patents shall be available for any inventions, whether products or processes, in all fields of technology, providing they are new, useful, and non-obvious." The European Patent Office Diplomatic Conference was in the process of modifying the exclusion from the EPC of computer programs because of this TRIPs language. It was postponed at the last minute because of some controversy coming in from various interests. The matter was deferred to a "second basket", but I think that there is a general agreement that you cannot exempt a particular technology without running afoul of Article 27.1.

Mr. BOUCHER. So you would argue, then, that Europe is out of compliance with TRIPs. The United Kingdom is not in compliance with TRIPs. Japan is not in compliance with TRIPs, because in none of these places are business method patents recognized and awarded. Are you saying that they are out of compliance?

Mr. KIRK. I would not agree with the fundamental statement that business method patents are not being issued by those three jurisdictions. I think if you look at what is actually being issued by the European Patent Office and by the Japanese Patent Office, you will find that there are techniques that will allow a skilled patent draftsman to get claims that cover business methods.

Mr. Myrick and I were just last week at an international conference dealing with a number of cutting-edge topics and a pertinent resolution was adopted by that group, the International Association for the Protection of Industrial Property. They adopted a resolution on Business Method Patenting which, if I might take a second—

Mr. BOUCHER. Well, let me say, Mr. Kirk, my time is almost gone now and we are going to have to vote.

Mr. KIRK. Okay.

Mr. BOUCHER. But let me just make the point that the only country among the industrialized nations that has clearly considered di-

rectly the question of business method patents and made an affirmative finding that we are going to extend that patent protection is the United States. The United Kingdom found exactly the opposite and made an affirmative decision not to award business method patent protection. And in your testimony, you suggested that if the Berman-Boucher bill were adopted, and we provide some special procedures and one substantive differentiation with regard to business method patents as compared to other patents generally, that we might be in violation of TRIPs.

I kind of wonder two things. First of all, we have already adopted a prior user defense that is specific to business method patents. I gather, based upon your testimony, you would question whether that American law is in violation of TRIPs. As a matter beyond that, I think, based upon your testimony, you would probably conclude that the practice in the United Kingdom is not consistent with TRIPs, even if you assume that you can get business method patents awarded in Europe and Japan. It would seem to me that if we have amended the statutory law once to provide a special process for business method patents and we have had no complaint from anyone as far as I know under TRIPs, that we could perhaps do so again.

In the time that I have, let me ask you, Mr. Secretary, for a bit of an explanation of what we might be able to do at this point about the business method patents that have already been awarded that many people suggest are inappropriate. We have heard Mr. Steinberg talk about the reverse auction business method patent. I am concerned about the one that was awarded that is enabling an individual to claim that he has got ownership of the entire space that allows people to solicit charitable contributions online, and we can cite other examples. Mr. Berman had a whole range of them in his statement.

Is there any way that your office can now go back and look at these patents after they were awarded, given the illumination of comment and commentary and perhaps some of the comment here and Mr. Steinberg's very helpful examples and take a second look and decide whether or not these patents, in fact, were appropriate? And if you can do that, do you intend to do that?

Mr. GODICI. Absolutely. A process exists. It is called reexamination, open to anyone, including the patent owner, who would like to bring additional prior art, information that we did not consider in the first go-around to our attention so that we could take a second look. That process has been in place for many, many years and we have in the neighborhood of 300 or 400 of those proceedings each year, where either the patent owner or an interested third party, a requester, comes to the office, gives us prior art, and we deal with it with respect to taking a second look at a patent that we have issued in the past.

Mr. BOUCHER. Do you have any reexaminations underway with regard to business method patents at the present time?

Mr. GODICI. That, I am not aware of. Like I said before, we have 300 to 400—

Mr. BOUCHER. Would you be so kind as to go back and take a look—

Mr. GODICI. Okay.

Mr. BOUCHER [continuing]. And provide this Subcommittee with precise information about any business method patents that you may be reexamining at the moment.

Mr. GODICI. I would be happy to.

Mr. BOUCHER. Now, the last part of my question is—

Mr. COBLE. If the gentleman could speed up, because the time is running out.

Mr. BOUCHER. I understand, Howard. I just have one other question, and that is, given what you have heard here today, does it motivate you to go back and take another look at the ones that have been the topic of this hearing primarily, such as the reverse auction patent or the charitable contributions online patent?

Mr. GODICI. Again, with respect to any specific patent, I think we have a process in place that will allow any member of the public to come to us for a very nominal fee, bring in prior art, and we will gladly take a second look at these patents.

Mr. BOUCHER. Okay. Thank you very much. Thank you, Mr. Chairman.

Mr. COBLE. Folks, pardon the abrupt departure, but we are going to have to go. Mr. Berman and I both have additional questions we will submit to you in writing.

[The questions of Mr. Coble and Mr. Berman follow.]



UNITED STATES
PATENT AND
TRADEMARK OFFICE

Under Secretary of Commerce For Intellectual Property and
Director of the United States Patent and Trademark Office
Washington, DC 20231
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APR 27 2001

The Honorable Howard Coble
Chairman, Subcommittee on Courts,
the Internet and Intellectual Property
Committee on the Judiciary
House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

Thank you for your letter with follow-up questions relating to your Subcommittee's oversight hearing on Business Method Patents. Your questions and our responses are set forth below:

1. Can you please describe in greater detail what steps the PTO is taking to reach out to financial and insurance industries in response to their concerns about business method patent quality?

We have created a Business Methods website on our USPTO homepage that provides a variety of information designed to answer frequently asked questions related to business methods. This website is available publicly, and specific efforts have been made to communicate this availability to all industries and organizations that we have a partnership relationship with (including the finance and insurance industries). The website includes such information as 103 rejection examples, the revised examination guidelines for computer-implemented inventions, and training materials for computer-implemented inventions -- all of which demonstrate that business method patent quality is being addressed in this area.

Additionally, we continue our efforts to reach out to our industry stakeholders, including the insurance and finance industries, and communicate our progress on the Business Method Initiatives announced in the Business Method Action Plan. In conjunction with the Business Method Initiative, the USPTO held a roundtable in July 2000. Panelists on the roundtable included individuals from the finance and insurance industries. We also hosted our inaugural business methods partnership meeting on March 1, 2001, as a part of these efforts. In attendance were approximately 60 representatives from the business and legal community, trade associations and academia. Furthermore, since September 2000, we have increased the number of our partnership participants from 10 to 21 industry organizations. In doing so, representatives of Technology Center 2100 (TC 2100) have actively participated in various industry-sponsored seminars and formal meetings. For

example, TC 2100 has participated in several industry-sponsored speaking engagements hosted by organizations such as AIPLA, BITS (formerly the Banking Industry Technology Secretariat), NACHA (the Electronic Payments Association) and the American Council of Life Insurers. We have also worked aggressively to identify examiner educational needs in the business method areas, and we have solicited Industry to provide training on business method-related topics specific to the finance and insurance areas. Representatives from BITS, NACHA, Fireman's Fund Insurance, the American Bankers Association and Edelman Financial Services have come to the USPTO and provided technical training and business insight in these areas.

We are also planning publication of an Official Gazette (OG) notice which requests input from interested parties on additional sources of prior art that the USPTO could utilize in the examination of applications in Class 705. A full and complete listing of the current core databases for Class 705 is provided in the notice for comment, along with a detailed description of the mandatory search that is now required for all applications examined in Class 705.

2. The PTO has implemented a number of measures to improve patent quality for business method applications. These measures focus on providing more tools, conducting a "second check" for accurate rejections and allowances and the like. Can you tell us what the PTO is planning to do beyond these measures to improve the quality of patents in this sector?

We have formed seven new art units in the business method work group and aligned these art units to be technology specific. Thus, all examiners are now matched with their specialty areas based on their experience and educational backgrounds. Additionally, we initiated an examiner work assignment program to bring experienced examiners with the necessary backgrounds into the business method area from other areas of the USPTO. Examiner resources were doubled, and 16 new primary examiners and 1 new Supervisory Patent Examiner were added. Of these transfers, 22 have advanced or multiple degrees, 8 have law degrees, 3 have Ph.Ds, 14 have their Master's Degree (including 3 MBAs), and 15 have experience in the legal, insurance, financial, and/or computer industries.

Training is a primary concern, and so we have expanded our training efforts beyond what was originally outlined in the Action Plan initiatives. We have begun efforts to implement follow-up training for the business method examiners for applying Sections 101 and 103 of the Patent Statutes, searching in the business methods art, and writing reasons for allowance. It is envisioned that this expanded training will further improve the quality of patents issued in this area.

Additionally, we are currently developing an electronic chat room for the business method examiners to provide a more flexible means for these examiners to consult with peers on searches and before issuing a case. Furthermore, a chat room mechanism will assist in identifying relevant technology-specific prior art. We are also in the process of preparing a proposal to capture the non-patent literature (NPL) prior art references that are being cited by applicants in Information Disclosure Statements (IDS). The purpose of

this effort is to capture information in an IDS that is not otherwise readily available and place that information in a database so that it can be retrievable by the business method examiners.

3. Business method patents and other developments have heightened attention on the work product of the PTO. Would the PTO be receptive to changes in its examination procedures aimed at capturing more of the examiner's understanding of the invention during evaluation, searching, and examination?

The USPTO is always receptive to improving our examination process in order to ensure the issuance of high quality patents in all fields of innovation. Many of the initiatives mentioned above are the result of our efforts in this regard, including training and prior art initiatives aimed at improving our examiners' ability to understand the claimed invention and locate the most pertinent prior art. In addition, many of the new examination procedures are a direct result of feed-back received from various industries. Of course, the benefits of these types of changes and initiatives need to be considered in light of the overall pendency and examination costs involved.

4. We have heard that the mere porting of a known business method to the Internet should not be sufficient to overcome a prima facie finding of obviousness. Is this the current view of the PTO? What additional steps is the PTO taking to integrate this perspective into its examination process and to apply it rigorously?

Yes, it is the current position of the USPTO that automating a known business method or process using the Internet is not sufficient grounds in and of itself to impart patentability. This view is currently reflected in the Section 103 Rejection Examples for Business Method Inventions (refer specifically to example 9) which is currently posted on the Business Methods Website at <http://www.uspto.gov/web/menu/pbmethod/>. All business method examiners have recently been retrained on these examples. Additionally, Chapter 2106 of the Manual of Patent Examining Procedure will be revised in June-July 2001, to include the language "merely using a computer to automate a known process does not by itself impart nonobviousness to the invention. See *Dann v. Johnson*, 425 U.S. 219, 227-30, 189 USPQ 257, 261 (1976); *In re Venner*, 262 F.2d 91, 95, 120 USPQ 193, 194 (CCPA 1958)."

5. Critics of business method patents argue that they allow individuals to obtain exclusive rights over all solutions to a business problem, rather than a specific solution that was actually developed. Our understanding is that purely functional patent claims covering "results" rather than "implementations" are not patentable. Does the PTO agree with this view? Would the PTO support reforms to the examination process that would better enable the examiner to prevent the issuance of purely functional claims?

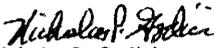
The courts have consistently held that the patent statute does not require any particular language and that an inventor is free to claim the invention in any manner as long as it complies with the requirements of 35 U.S.C. 112, see, e.g., *In re Swinehart*, 439 F.2d 210

(CCPA 1971). In fact, the sixth paragraph of 35 U.S.C. 112 expressly authorizes an inventor to claim the invention as a "means or step for" performing a function.

Secondly, an inventor who is the first to discover a solution to a particular problem is entitled to claim the invention in broad terms that avoid the closest prior art. While the claim may be infringed by other solutions that are discovered by subsequent inventors, such a result is inherent in our patent system. It is important to note that potential infringement of an earlier patent does not prevent technological advancements from being made. Licensing agreements are a common means to allow progress to occur, while protecting the patent rights of the first inventor. History is replete with pioneering inventions that have spurred innovation and technological advancement. One need only to look at earlier versions of the cellular telephone that required a brief case for carrying both the telephone receiver and a large battery. Needless to say, significant improvements have been made over time to those earlier versions of the cellular telephone.

I hope this information is helpful, and I look forward to continuing to work with you to ensure successful operation of our patent system.

Sincerely,



Nicholas P. Godici

Acting Under Secretary of Commerce for Intellectual Property and
Acting Director of the United States Patent and Trademark Office



UNITED STATES
PATENT AND
TRADEMARK OFFICE

Under Secretary of Commerce For Intellectual Property and
Director of the United States Patent and Trademark Office
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APR 27 2001

The Honorable Howard Berman
Ranking Member, Subcommittee on Courts,
the Internet and Intellectual Property
Committee on the Judiciary
House of Representatives
Washington, DC 20515

Dear Representative Berman:

Thank you for your letter of April 10, 2001, regarding questions about patent protection for business method inventions. As noted in your letter, the United States Patent and Trademark Office (USPTO) takes concerns regarding these inventions seriously and will continue to work to ensure the issuance of high quality patents in all fields of endeavor.

Your questions and our responses are set forth below:

- (1) Does the PTO believe that a business method that is not computer implemented, has no technological element, and involves no physical transformation, is eligible for patent protection? To use a specific example, if it hadn't existed prior to today, would American Airlines be able to get a patent on the idea of utilizing a "hub and spokes" method of organizing an airline's flight operations?

As to the first part of the question, the courts have made it clear that there is no exception for "business method" type inventions from statutory patentability requirements, *see State Street Bank & Trust Co. v Signature Financial Group, Inc.*, 149 F.3d 1368 (Fed. Cir. 1998). A claim directed to a business method, whether or not computer-implemented, will be treated similarly as other claims. Eligibility for patent protection is determined by our patent statutes as interpreted by the courts.

In the landmark case of *Diamond v. Chakrabarty*, 447 U.S. 303 (1980), the United States Supreme Court found that Congress intended the statutory subject matter under 35 USC 101 of the patent law to include "anything under the sun that is made by man." The Supreme Court has also noted that there are limits to patentability. Indeed, in *Diamond v. Diehr*, 450 U.S. 175 (1981), the Court explicitly identified three specific areas of subject matter that are excluded from patent protection. These three areas are: (1) laws of nature, (2) natural phenomena and (3) abstract ideas. Thus, an invention directed toward a pure algorithm or manipulation of abstract ideas with no practical application is not patentable. The Court of Appeals for the Federal Circuit has found that the key question to be answered is whether the claimed invention, when looked at "as a whole," is an abstract idea, such as a disembodied mathematical concept, or

whether the invention produces a practical application providing a "useful, concrete and tangible result." See *State Street*; see also *In re Alappat* 33 F.3d 1526 (Fed. Cir. 1994)(en banc).

With respect to the second part of the question, the USPTO is not in a position to comment on the patentability of possible inventions apart from the evaluations of specific claims made in specific applications. However, as a general matter, if an invention complies with the patent eligibility requirements mentioned above, and it further complies with the additional statutory requirements for patentability, such as novelty, non-obviousness and utility, such an invention would be patentable.

- (2) I understand that since the inception of the Business Method Patent Initiative, approvals for such patents have gone from nearly 70% to down around 35%. This success does beg a question. If a second set of examiner eyes has such a dramatic effect on approval rates, does it indicate that many invalid business method patents were previously approved?

With respect to the allowance rate issue, our statistics from the technology center including Class 705 indicate that the allowance rate in Class 705 for the quarter ending March 2000, at the time of the announcement of our Business Methods Patent Initiative, was 57%. This allowance rate for the quarter ending March 2001 was approximately 47%. For comparison purposes, the overall Patent Examining Corps allowance rate has been at about 70% for the past several years.

Many factors may influence allowance rate, including changes in processing time, changes in the total number of disposals, and the rate applications are refiled. Since the start of the Business Method Patent Initiative we are taking more care in our examination of these applications. It is our perception that the 10% drop in this allowance rate is related to the increased training our examiners have received and the resultant decisions they are making.

While all United States patents are presumed valid (35 USC § 282), if there is a concern regarding the validity of a particular patent, *ex parte* and *inter partes* reexamination procedures carried out by the USPTO are available to interested parties to ensure that the most pertinent prior art is considered.

I hope that this information is helpful, and I look forward to continuing our work together on these issues which are vital to the continued successful operation of our patent system.

Sincerely,


Nicholas P. Godici

Acting Under Secretary of Commerce for Intellectual Property and
Acting Director of the United States Patent and Trademark Office

AIPLA**AMERICAN INTELLECTUAL PROPERTY LAW ASSOCIATION**

2001 JEFFERSON DAVIS HIGHWAY • SUITE 203 • ARLINGTON, Virginia 22202

April 23, 2001

The Honorable Howard Berman
 Subcommittee on Courts, the Internet, and Intellectual Property
 2330 Rayburn House Office Building
 United States House of Representatives
 Washington, D.C. 20515

Dear Congressman Berman:

Thank you for your letter of April 10, 2001 in which you ask certain questions regarding my testimony before the Subcommittee on Courts, the Internet, and Intellectual Property on April 4. I have attempted to respond to your questions by providing my answers following each question.

Question.

In your testimony, you stated that it would possibly be inconsistent with the TRIPs Agreement to include "technological contribution" as a requirement for patentability. However, I note that the TRIPs Agreement only requires patent protection for inventions in "fields of technology." So, doesn't the TRIPs Agreement already require some technological contribution, or at least technological element, for its obligations to be implicated? The term "fields of technology" is not equivalent to "fields of endeavor," is it?

Answer:

The text of Article 27.1 is an appropriate starting point to respond to your question. Article 27.1 reads:

"Article 27

Patentable Subject Matter

1. Subject to the provisions of paragraphs 2 and 3, patents shall be available for any inventions, whether products or processes, in all fields of technology, provided that they are new, involve an inventive step and are

capable of industrial application.¹ Subject to paragraph 4 of Article 65, paragraph 8 of Article 70 and paragraph 3 of this Article, patents shall be available and patent rights enjoyable without discrimination as to the place of invention, the field of technology and whether products are imported or locally produced.

The purpose of the first sentence of Article 27.1 was to lay down a basic rule that patents should be available for all inventions, both product and process inventions, that were new, useful, and non-obvious. The only other requirement is that of Article 29.1 that:

"1. Members shall require that an applicant for a patent shall disclose the invention in a manner sufficiently clear and complete for the invention to be carried out by a person skilled in the art and may require the applicant to indicate the best mode for carrying out the invention known to the inventor at the filing date or, where priority is claimed, at the priority date of the application."

There is no requirement that an invention must also make a "technological contribution." The addition of the phrase "in all fields of technology" was to ensure that countries could no longer refuse to grant patents for certain inventions (primarily pharmaceutical inventions) or to limit the grant of patents for such inventions to process patents. Similarly, the use of the phrase "the field of technology" in the "non-discrimination" obligation of the second sentence of Article 27.1 was to ensure that patent rights for all inventions would be enjoyable without suffering the limitation of a compulsory license – again, a practice that had been prevalent primarily with respect to pharmaceutical patents. Viewed in this context, the possible inconsistency of adding a further requirement of "technological contribution" as a requirement for eligibility of patent protection is clearly present, as stated in my testimony. My reason for stating that such an additional requirement would be "possibly" inconsistent with the TRIPs Agreement is that ultimately this question can be answered only by a WTO dispute settlement panel.

Question:

Do you believe that a business method that is not computer implemented, has no technological element, and involves no physical transformation, is eligible for patent protection? To use a specific example, if it hadn't existed prior to today, would American Airlines be able to get a patent on the idea of utilizing a "hub and spokes" method of organizing an airline's flight operations?

¹ For the purposes of this Article, the terms "inventive step" and "capable of industrial application" may be deemed by a Member to be synonymous with the terms "non-obvious" and "useful" respectively.

Answer:

With respect to the first question, a business method that, as claimed, lacks any "computer implementation," "physical transformation," or "technological element" can be eligible for patent protection if it is claimed in a way that meets the test for a "useful, concrete and tangible result." Similarly, with respect to the second question, assuming the American Airlines "hub and spokes" method of organizing an airline's flight operations produced a "useful, concrete and tangible result," it would be eligible for patent protection because it is patentable subject matter. Whether American would actually be able to get a patent for it is entirely another matter and would depend on whether it satisfied all of the statutory criteria for patentability, particularly (given the premise of the question) non-obviousness.

Question:

U.S. patent law appears to be rife with examples of differing treatment for different types of patents. In fact, business method patents themselves are already subject to differential treatment under U.S. law through both the "prior user" defense and the PTO's current Business Method Initiative. Therefore, why would further provisions regarding business method patents be so troubling?

Answer:

Initially, it is noted that the prior use defense set forth in 35 U.S.C. 273 is not limited to business method patents. The defense extends to all methods for "doing or conducting business." In this regard, the Section-by-Section Analysis accompanying S. 1948 which became the American Inventors Protection Act of 1999, offers the following with respect to the methods to which the defense applies:

"The method that is the subject matter of the defense may be an internal method for doing business, such as an internal human resources management process, or a method for conducting business such as a preliminary or intermediate manufacturing procedure, which contributes to the effectiveness of the business by producing a useful end result for the internal operation of the business or for external sale."

Thus, it is clear that the defense applies to a rather broad range of subject matter, far beyond just business method inventions.

In addition, a distinction must be drawn between the prior use defense of 35 U.S.C. 273 and the PTO's Business Method Initiative. The latter has to do with ensuring that inventions in some areas related to business activity receive the same quality of examination that inventions in other areas receive. In time, when the PTO is confident that these inventions are receiving the same quality of examination as other inventions, it is foreseeable that the PTO would phase out the Initiative (or if it proves to be a harbinger of a better way of examining, perhaps extend it to all applications).

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The prior use defense is in a different category. As you will recall, the AIPLA strongly supported a prior use defense that applied across the board to all patents. The limitation of the term "method" to "a method of doing or conducting business" was inserted at a late stage in the consideration of the American Inventors Protection Act in the House in the Summer of 1999.

A broad prior use defense applying to all patents can be justified as a permissible exception to the rights granted by a patent under Article 30 which provides:

"Exceptions to Rights Conferred

Members may provide limited exceptions to the exclusive rights conferred by a patent, provided that such exceptions do not unreasonably conflict with a normal exploitation of the patent and do not unreasonably prejudice the legitimate interests of the patent owner, taking account of the legitimate interests of third parties."

Of course, the case can still be made that the Article 30 right to have an exception to the exclusive rights conferred by a patent, which a prior use right is, does not excuse such an exception when exercised in a discriminatory manner. In this regard, I should emphasize that AIPLA certainly did not support so limiting the prior use right.

I appreciate the opportunity to respond to your questions and look forward to working with you to improve our patent system.

Sincerely,



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April 27, 2001

The Honorable Howard L. Berman
Ranking Member, Judiciary Subcommittee on
Courts, the Internet, and Intellectual Property
House of Representatives
Washington, DC 20515 0526

Dear Mr. Berman:

Thank you for the opportunity to appear before the Subcommittee on April 4. We are responding to the two follow-up questions relating to business method patents posed in your letter of April 10. Your questions are reproduced below followed by our responses.

Question:

It appears that you and I share the same opinion on an important issue - namely that high-quality patents promote innovation and the success of our economy. Are you concerned about the quality of business method patents that have been issued by the PTO? If so, would you say that the greatest patent quality problems at the PTO today are in regards to business method patents?

Response:

IPO indeed shares your opinion that high quality patents promote innovation and the success of our economy. The PTO needs to devote special efforts to maintaining and improving quality in emerging or rapidly expanding technology areas such as business method patents. Such areas may require the PTO to build databases of prior art, train examiners in new subject matter, and hire examiners with special educational backgrounds. These special efforts should not be at the expense of quality of patents in general.

As indicated in my testimony, we believe the PTO's "Action Plan for Business Method Patents" undertaken last year calls for reasonable steps to ensure proper examination of business method patents. We believe the PTO is making headway with its special efforts. Still other actions are desirable, such as additional programs to make prior art available to examiners. No special legislation is needed with regard to business method patents at the present time, in our opinion. To ensure high-quality business method patents, we suggest the Subcommittee should carefully monitor the administrative actions of the PTO and continue its

REPRESENTING PATENT, TRADEMARK, COPYRIGHT, AND TRADE SECRET OWNERS

The Honorable Howard L. Berman
 April 27, 2001
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work to fund the PTO at the necessary level for both high quality and reasonable pendency times.

Question:

In your testimony, you quote the *Graham v. John Deere* decision for the proposition that "the primary responsibility for sifting out unpatentable material lies in the Patent Office. To await litigation is - for all practical purposes - to debilitate the patent system." Thus it would appear that we agree that patents should be of the highest quality when they are issued by the PTO. Part of assuring the issuance of quality applications by the PTO is ensuring that PTO examiners are aware of all relevant prior art. Do you agree that mechanisms allowing third parties to bring prior art relevant to a pending application to the attention of PTO examiners will contribute to patent quality?

Response:

We agree patents should be of the highest quality when they are issued by the PTO. High quality patents are essential for providing certainty for patent owners and competitors about the validity and scope of individual patents.

A critical ingredient in patent quality is ensuring that PTO examiners are aware of relevant prior art. It is necessary to place some limits on mechanisms for encouraging third parties to bring prior art relevant to a pending application to the attention of PTO examiners, however, in order to avoid harassment of patent applicants by competitors or undue delay in granting patents.

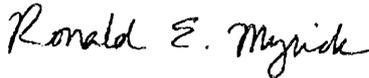
For many years IPO has been against pre-grant opposition proceedings. The American Inventors Protection Act in 1999 included a new section 122(c) in title 35, United States Code, to prohibit administratively established pre-grant opposition procedures after publication of a patent application. The act allows third parties to bring prior art relevant to a pending application to the attention of PTO examiners without hobbling patent applicants with slow and expensive pre-grant proceedings. Any pre-grant mechanism should be limited as provided in section 122(c).

Efforts to improve patent quality should not end with the grant of the patent. In the interest of quality, we support enhancement of the AIPA's *inter partes* reexamination procedure. The procedure should permit third party requesters to bring relevant prior art to the attention of PTO examiners in a reexamination procedure in which the requester will have a reasonable opportunity to participate and an opportunity for court appeal.

The Honorable Howard L. Berman
April 27, 2001
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We look forward to working with you in addressing patent quality problems.

Sincerely,

A handwritten signature in cursive script that reads "Ronald E. Myrick".

Ronald E. Myrick
President

Mr. COBLE. I thank you all for your testimony. We appreciate your contribution.

This concludes the oversight hearing on business method patents. The record will remain open for 1 week. Thank you for your cooperation, and good day. We stand adjourned.

[Whereupon, at 3:31 p.m., the Subcommittee was adjourned.]

APPENDIX

APRIL 4, 2001

ADDITIONAL MATERIAL SUBMITTED FOR THE HEARING RECORD

PREPARED STATEMENT OF STEVEN L. FRIEDMAN, ESQUIRE

As the counsel who was privileged to successfully convince the Federal Circuit to reject the so-called business method exception to patentability in the *State Street* case, I have been following with interest the debate unleashed by that decision. While it was foreseeable that the patent system would experience a period of transition as a result of *State Street*, the level of criticism is troubling. I am particularly concerned about the proposals involving legislation that would either eliminate or sharply curtail certain patents that are deemed "business methods." Such legislation, if passed, would constitute a substantial step backwards and would unnecessarily and unfairly deny the benefits of patent protection to certain industries.

Before addressing specific proposals and criticisms, it is important to consider the patent world prior to *State Street*. As several witnesses made clear, the *State Street* decision did not hold that business methods were patentable. Rather, the Court simply held that the so-called "business method" exception to statutory subject matter is no longer viable. Judge Rich, writing for a unanimous panel, explained it far better than we could:

[T]he Court relied on the judicially-created, so-called "business method" exception to statutory subject matter. We take this opportunity to lay this ill-conceived exception to rest. Since its inception, the "business method" exception has merely represented the application of some general, but no longer applicable legal principle, perhaps arising out of the "requirement for invention"—which was eliminated by §103. Since the 1952 Patent Act, business methods have been and should have been, subject to the same legal requirements for patentability as applied to any other process or method

State Street Bank & Trust Co. v. Signature Financial, 149 F.3d 1368, 1375 (Fed. Cir. 1998). Judge Rich went on to point out that the business method exception had never been invoked by the Federal Circuit or its predecessor to deem an invention unpatentable. *Id.*

State Street and its progeny did not represent a sea change in the law creating a new form of intellectual property. Instead, the decision merely clarified the law. In fact, we believe that the tremendous increase in patents now characterized as "business methods" can be largely attributed to the removal of the confusion and uncertainty surrounding such patents by the *State Street* decision.

Because *State Street* did not constitute a change in existing law, those who argue for a return "to the good old days" before *State Street*, have missed the point. Indeed, those who advocate legislation should properly recognize that they would be grafting a brand new exception onto the patent laws and not simply returning the system to the status quo ante.

Turning now to the criticisms and proposals before the Committee, it seems there are three principal concerns:

1. The quality of the business method patents that are issuing;
2. The effect such patents will have on certain industries—namely e-commerce and/or the internet; and
3. Should "business methods" be patentable at all and, if so, should there be different rules and standards.

While the issues overlap somewhat, we will address them one at a time.

First, as to quality, this issue is not unique to the "business method" debate. Nor is there any real dispute. The desire that the Patent and Trademark Office ("PTO") only issue quality patents rewarding genuine innovations applies to the entire patent system. The fact that early on in the process some business method patents of questionable validity may have issued is not the basis for radical surgery to the Patent Act. Rather, the proper allocation of experience and resources will self-correct this problem. We note that the PTO and the Courts are already well on their way to solving this concern, without legislation, through increased resources and better internal procedures to process these applications.

One of the unfortunate results of *State Street* is that much of the debate and criticism is being aired in the mainstream press. Interestingly, however, virtually none of the criticism has focused on specific claims, choosing instead to rely on the perceived danger associated with a handful of high-profile patents. Indeed, the current debate, as it has been conducted in the press, seems to blur the issue of "bad patents" and arguably silly inventions. At bottom, the question of quality is separate and distinct from, the question of commercial viability. Ultimately, the marketplace will effectively winnow out particular inventions, that, while perhaps patentable, are destined to become marketplace no shows.

Second, the concerns raised about the effect of such patents on certain industries is misplaced. While the industries mentioned at the hearing included e-commerce and the internet, others have raised concerns in the past about patents affecting the financial services industry, the computer industry and the bio-tech industry. The argument is always the same: the particular industry is somehow "different" from all other industries and should be protected from some hypothetical harm created by "patents." The logical extension of this argument is that no innovation, no matter how novel, unique, non-obvious and useful, warrants patent protection if it affects this particular industry.

The incentives offered by patent protection, however, have served this country well as an engine for fostering innovation. The Federal Circuit explained the importance of the patent system in its landmark *Alappat* decision:

Law and public policy intertwine in embracing new fields in the scope of Section 101. Patent law has nicely fostered technological advance in the United States, for its principles are particularly suited to a free market system; it requires neither governmental intrusion nor federal funds to provide the incentive for industrial innovation; the innovation incentive is the direct consequence of the patent grant. I know of no major technological advance, no new industry or evolving technology, that has not participated in the patent system. It is estimated that 85-90% of the world's technology is disclosed only in patent documents.

In re Alappat, 33 F.3d 1526, 1570-71) (Fed. Cir. 1994) (en banc) (Newman J. concurring). As Judge Newman points out, the patent system has time and again proven its wonderful resiliency to absorb and integrate new technologies.

Stated differently, the patent system works. It has served to foster innovation from manufacturing to genetics and there simply is no reason to believe that it will not have the same effect on the internet or e-commerce, or whatever other new industry emerges in the future. Consequently, Congress should be leery of arguments that seek to treat any industry differently by denying or curtailing patent protection. Our collective history strongly suggests that such legislation is bad public policy.

Interestingly, the effect of *State Street* on the financial services industry is starting to come into sharper focus and at least two ramifications are emerging. First, however one defines a "business method", an abundance of technological innovation occurs within financial institutions which previously had been "protected" either by trade secrecy, whatever first mover advantage could be garnered or, on occasion, loosely by copyright. In contrast, information services businesses have been robustly patenting, licensing and realizing revenue for their technology, system and platform innovations for years. At a minimum, *State Street* has provided the impetus for financial services businesses to patent their own technological innovations and platforms and provides a means for them to effectively compete in areas previously dominated by traditional information service firms.

Second, and on a broader scale, *State Street* has enabled financial service businesses to effectively separate and independently protect intellectual property rights from their underlying innovative products, services or systems. Ultimately, these patent rights will have an independent economic value to the firms and perhaps even give rise to a separate marketplace for their innovative ideas, separate and apart from the market place for their products or services. Thus, only three years

after *State Street*, it appears to have generated more value creation opportunities rather than signaling the downfall of the patent system as first and direly predicted.

Finally, the debate concerning whether business methods should be patentable at all and, if so, subject to different rules and standards is, at best, premature. The *State Street* decision is not even three years old. While there are many predictions as to whether the decision will have a favorable or negative effect on certain industries, it is fair to say that more time is needed to reasonably come to a conclusion. This is especially true where, as here, many of the early concerns raised by the decision have already been alleviated by the PTO and the Courts. The type of fundamental change that such legislation would entail simply should not be rushed.

If, however, such legislation is to be considered now, we believe that it would be a serious error to treat business method patents differently. As an initial matter, the term "business method" is not easily defined. Indeed, the PTO recognized the difficulty of defining the boundaries of a "method of doing business" prior to the *State Street* decision and had eliminated the term from consideration in deciding whether to grant a patent. See 61 Fed. Reg. at 7479.

Because of the difficulty in defining the term, there is a legitimate concern that any legislation will be a weapon to single out certain types of industry as warranting "protection" from patents. In other words, methods used in e-commerce will be unprotectable business methods while methods utilized to control steel inventory will not. Both are integral to "doing business" but only one will be denied patent protection. Congress has avoided the temptation to create such artificial distinctions in the past and should continue to do so in the future.

The inevitable result of trying to treat business method patents differently is to permit subjective value judgments in the examination process. Such a result should be rigorously avoided. Every useful invention should stand or fall based on its own weight after being measured by the time-tested tools of novelty, non-obviousness and the other requirements of the patent statute. Once issued, the marketplace will further sort out the trivial from the revolutionary. In short, if patents of questionable validity are issuing, allocating appropriate resources so that the PTO can conduct a quality examination is the right solution. Creating special rules based on the perceived worthiness for a particular subject matter is not.

It is frequently stated that we are living in an Information Age. This is a result of the massive, free-flow of information through means that only a few years ago seemed impossible. The mere existence of the Internet alone has created an unprecedented flow of information. By protecting the inventions of the Information Age, we are engaging in the same successful, public policy determination—limited protection in exchange for knowledge—that has helped foster previous technological revolutions and made our patent system the envy of the world.

