IP BUSINESS

SUMMER 2003

MANAGED PORTFOLIO: Revisit, Recycle, Review

BUSINESS METHODS: After the Gold Rush

PATENT LITIGATION: Is There an Alternative?

MARKET SHARE: The Almost-New Product

Filing a provisional patent application can save you time, money, and competitive edge.

IF YOU'RE CAREFUL.

THE PROPER PROVISIONAL

Paid Advertising Supplement to Washington Business Journal

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Getting Strategic About Intellectual Property

While some businesses still think only in traditional terms (cash, property, equipment) when they're tallying the value of their enterprise, most companies—helped along by federal regulations—have started to add in such relative intangibles as relationships (with customers, employees, partners, and suppliers), brand equity, and, of course, intellectual property.

What's sometimes lost in the discussion of IP as an asset, however, is the strategic dimension. For while it's now clear that the value of a company's IP portfolio can be calculated, it's also true that the portfolio is not static. It's evolving—and devolving—over both the short and long term.

If there's a theme, then, that runs through all the articles in this issue of *IP Business*, it's the importance of thinking strategically when taking any action related to IP. Should you go to the expense of seeking a patent on a specific product, technology—or, for that matter, business method? Should you hedge your bets and file a provisional patent application? Should you litigate when you suspect infringement—or find a way to leverage your patent instead? Should you actually abandon some of the patents you've held for years? The answers to the questions are couched in a careful assessment of myriad intersecting business and legal issues—and they're different for every business and every situation. Working through them underscores the fact that more and more, IP is not just an asset, it's a vital strategic tool.

IP BUSINESS

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The Perils and Promise of PROVISIONALS

To save time and money—and to hedge their bets—more and more companies are filing provisional patent applications. But sometimes, haste clearly makes waste.

By Jennifer Taylor

Illustration by John Dykes

"If you have a bore that can't be drilled," Railhead Underground Products boldly proclaims on its website, "you better get the Incredibit."

The Texas-based maker of drilling equipment describes its toughest tool in breathless terms: How it "dances" in a hole, unlike any other bit, unbowed by shale or sandstone. Backing up the company's claims in glowing testimonials, customers declare they wouldn't bore with anything but the Incredibit.

It's easy, then, to understand why Railhead Underground—then known as New Railhead—went to court in May 1999 to stop two competitors from using the Incredibit technology that one of the company's co-founders had developed more than seven years earlier. And it is all the more unsettling, especially to those with intellectual property to protect, to hear the outcome: Thanks to a simple—and avoidable—mistake made early in the patenting process, New Railhead lost the case and its vaunted Incredibit was rendered vulnerable.

To understand why, let's back up a bit. In February 1997, New Railhead filed a provisional patent application for the Incredibit. This served as a kind of "placeholder" until the inventor was ready to file a formal utility patent application, which New Railhead did less than a year later, in line with the requirements of the U.S. Patent and Trademark Office. All seemed fine until New Railhead sued Vermeer Manufacturing and Earth Tool Company, alleging infringement. From New Railhead's perspective, the case was as easy as drilling with the Incredibit. The company had followed the rules. It had the patent.

The court disagreed, finding that the disclosure in the provisional application did not adequately describe the invention claimed in the utility application. The court ruled the provisional application ineffective. Since the Incredibit had been on sale for more than a year before the utility application was filed, New Railhead's patent was held invalid. The result: New Railhead still sells the Incredibit, but so do other companies, albeit under different names. No one has—or will have—an enforceable patent on this product.

The company has declined to comment on the case, but the case has been the talk of IP lawyers since it was affirmed by the U.S. Court of Appeals for the Federal Circuit last summer. Underlying these discussions is the question—and practicality—of provisional applications. "While this is really nothing new in terms of the risks associated with provisionals that we've been counseling people about all along," says Richard Goldenberg, a senior partner in IP at Hale and Dorr, "we now have some case law to show people when we talk about those risks."

The positives of provisionals

For many, the allure of provisional patent applications is that they are cheaper, faster, and less complicated to file than are for-

mal, utility patent applications. Unlike a formal patent application, the provisional application only has to include a written description of what the invention is, how to make and use it, and any drawings necessary to understand it; it need not include claims. The inventor can claim "patent pending" status for a year, after which the provisional application expires.

The provisional application was established in 1995 to remove an advantage that foreign filers had in the U.S. system. Foreign inventors could file a patent application in their own country, then, within a year, file a patent application in the U.S., claiming protection from the date of the foreign filing. As a result, they were able to add an additional year to the U.S. patent term. The provisional patent application gives U.S. filers that extra year as well. And that extra year of patent protection can be very lucrative.

The provisional application benefits U.S. filers overseas as well. For while the U.S. gives inventors one year from the date of an offer for sale or the public disclosure of an invention to file a patent application, most of the world does not offer this grace period. A provisional can be used to preserve those foreign rights.

Eric Prahl, a senior partner in IP with Hale and Dorr, says that while he would not use a provisional application in a case—like New Railhead's—in which the inventor was approaching a "hard bar date," after which patentability could be lost, there are, he says, cases when provisional applications should be used. These include cases where time is clearly of the essence.

"Sometimes a client will call and tell you that one of their scientists is giving a presentation on an invention, and they're doing it today," says Shann Kerner, a senior partner in IP with Hale and Dorr who holds a doctorate in biomedical sciences. "You can take their printed presentation, put a cover sheet on it, and file it as a provisional application that day. Then you can file additional provisional filings later that are more complete."

Prahl points out that provisional applications can be useful for inventors who want to protect their idea while in talks with investors. "That would establish proof that they had the idea before the discussions," says Prahl, who is also an engineer.

Provisional applications are also cheaper to file, both in terms of patent office fees and sometimes legal fees. The Patent Office charges $160 for a provisional patent filing versus $750 for a utility patent filing (both fees are reduced by 50 percent for individuals and small companies). "Companies are watching their money closely these days," says Goldenberg. "Sometimes they've got 10 ideas that might be useful on a product, but they don't have the money to file formal patent applications on all of them. So they'll file provisionals while they decide which ideas are worthwhile."

These advantages have clearly resonated with companies seeking patent protection. While in 1996—the first year provisional applications were accepted—the U.S. Patent and Trademark Office received just over 20,000 provisional applications, the USPTO was processing nearly 100,000 by 2002.

The problems emerge

Steve Kunin, deputy commissioner for patent examination policy at the USPTO, says his office has not seen widespread problems like the New Railhead case. But Kunin's perspective may be tem-

GLOSSARY: Talking the Talk

ABANDONMENT: what happens to a non-provisional patent application if the applicant fails to file a timely response to a patent office notice or action.

ABSOLUTE NOVELTY: an invention that has never been publicly disclosed, or published. Most foreign countries require absolute novelty. The U.S. does not.

PATENT PENDING: can be used in connection with a product after an application—including a provisional application—has been filed.

PRIOR ART: any published material or public use before the priority date that the patent office can use to reject an application on the grounds that the invention is not novel or unobvious.

PRIORITY DATE: presumed to be the date the patent application was filed. The inventor can get the benefit of an earlier priority date by filing a provisional application or by filing an application in a foreign country that adequately describes the later claimed invention. Used to determine what is prior art or who is entitled to a patent.

PUBLIC USE: any use that is not confidential or, even if confidential, is for the patentee's gain. Experimental use that is not part of commercial development is not public use. Starts the one-year clock running for filing for a U.S. patent.

STATUTORY BAR DATE: date by which a patent application must be filed to preserve patentability in the U.S. An inventor has one year from a "barring event"—public use, offering for sale, publication, oral presentation—to file a U.S. application. —*J.T.*

pered by the fact that problems with provisionals generally won't surface until litigation—when it may be too late.

For the most part, Kunin notes, patent examiners do not even look at provisional applications, saving whatever scrutiny they apply for the utility application, a year later. An exception, Kunin says, would be if an inventor needs the earlier filing date of the provisional application in order for his utility patent application to be approved. In that case, he says, "a patent examiner might find technical literature—published after the filing date of the provisional application but before the filing date of the utility application—that would affect the invention's patentability."

Come litigation, however, mistakes made early on could well be exploited by a defendant to prove the patent was not actually valid. In *New Railhead*, the court found that a key feature of the drill bit was that it was angled with respect to its housing. The description in the provisional application did not indicate that the bit body was to be angled, nor did the drawings in the provisional application clearly show it was angled. The provisional application, therefore, was not specific enough to support the utility application.

"It sounds like a case of sloppy drafting at the outset," says Kerner. "Sometimes when an application is first filed, the important elements are not apparent but become more obvious as the inventors continue to work."

Goldenberg says he has had clients come to him with provisional applications that were "very skimpy in terms of disclosure." If a problem is caught early enough, he says he would re-file a provisional application with a more complete description.

But sometimes, problems are caught too late. Prahl says a client was considering acquiring another company's patent portfolio, but one patent in the portfolio had a New Railhead-type problem. A provisional application with very little information had been filed, but the inventor was depending on the provisional to establish priority over another patent application. Prahl says the best a lawyer might be able to do in that situation would be to find a way to argue that the description in the provisional was adequate.

New Railhead may be the exception that proves the rule.

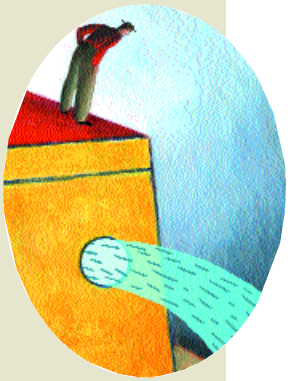
Take the case of Darren Hill, CEO of WebLinc, a Philadelphia-based Internet development firm. Hill's company filed a provisional patent six years ago for WorkArea.com, an online time clock that tracks employees' hours in real time. They used the one-year grace period to finalize documentation and filed a utility patent application in less than a year. Today, Hill says, 1,900 companies use the patented system. "We knew we had something unique. But we knew someone else would come up with the same idea. We had to get to the gate fast. It worked out great."

Journalist and law school graduate Jennifer Taylor wrote about the Hatch-Waxman Act in the Winter 2003 issue of IP Business.

The Time Machine

The boom in provisional patent applications has been fueled in part by the boom in biotechnology.

Provisional patent filings have become standard procedure in the high-stakes, fast-paced biotech field and in the life sciences in general. And for good reason. As Shann Kerner, an intellectual property attorney at Hale and Dorr, notes, provisional patent applications allow researchers to protect their discoveries while they continue to do research on them before filing a utility patent application.



"They can use the year to collect data and enable and develop their work further," Kerner says. "We can file a first provisional, then as we get data, we will file a second provisional and even further provisionals as we get more data. But still, within a year of filing the first provisional, we will file for the utility patent." In the end, the utility patent application can have several provisional filings associated with it. The inventor gets intellectual property protection from the earliest possible date, without having to wait until all the research is complete.

Provisional patent applications can also be beneficial to a biotech inventor years later, at the end of the patent's term. In 1995, the length of the patent term was changed from 17 years from the issuance of a patent to 20 years from the filing of a patent application. A provisional patent application predates the ticking clock, thereby effectively extending the life of the patent up to 21 years after the provisional filing date.

For some inventions, such as computer software, where both money and obsolescence come early, that 21st year may not actually mean much. In both the pharmaceutical and the biopharmaceutical fields, however, where it could take years to complete research and get governmental approval to market a drug, it's a different matter. "If you're talking about a blockbuster drug that brings in $100 million a year," says Steve Kunin, deputy commissioner for patent examination policy at the USPTO, "you've made your company another $100 million just by filing a $160 provisional patent application." — *J.T.*

Litigation as a Last Resort

The decision to apply for a patent also means being ready to defend it. Unless you can come up with a better strategy.

By Stephanie O'Neill

Illustration by Ellen Weinstein

In 1999, Ralph Benghiat, a 74-year-old scientist who had patented a meter-reading device, approached Itron Inc., a Spokane, Washington-based company, to see if it would be interested in licensing his device. Not only wasn't Itron interested, it responded with a claim that Benghiat's patent was in conflict with a meter reader it was already using. Benghiat sued Itron for infringement—and the jury agreed with him, deciding Itron had willfully infringed Benghiat's patent and awarding him $7.4 million.

Benghiat's experience underscores a basic but often misunderstood reality of patents: Just because you've been awarded a patent doesn't mean the battle's over.

"A patent does not give you the right to make something," notes James B. Lampert, senior partner and chair of Hale and Dorr's Intellectual Property Department. "All a patent gives you is the right to exclude others from doing something." In other words, patents are not per se self-enforcing. It is up to patent holders to keep others from treading on their ideas.

But does that mean that patent holders will inevitably end up in court? By no means, says Richard Goldenberg, a senior partner at Hale and Dorr. "Yes, there are people who are chomping at the bit to sue anyone who invades their market space. But many others get patents for more defensive reasons," he says. "They may simply want to build up a portfolio that will make any competitor think twice before suing them, and allow them to make their products without interference from other companies."

The point is that there are a variety of ways to use patents: they can be a deterrent that fends off lawsuits and infringers before they start, help in settling a lawsuit, or simply a license to litigate. In short, a patent is a tool—and it is up to the individual patent holder to determine how and when to use that tool to defend its ideas, its products, and its markets.

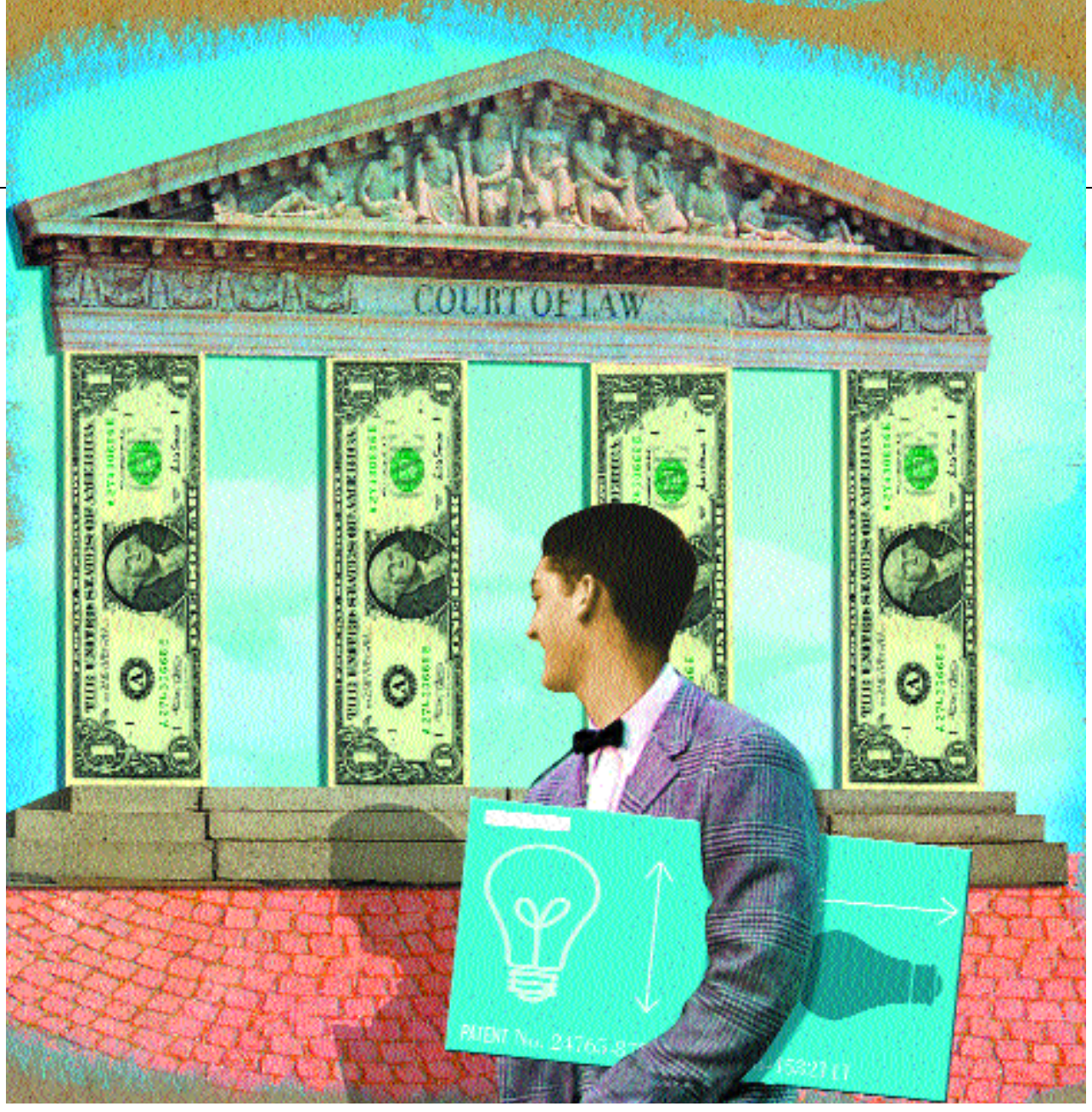
Deciding to patent

Ideally, companies should start thinking about how they will use a patent before they even apply for it. They should have a clear understanding of why they want a patent in the first place, and whether or not it is worth the effort, given the need to remain vigilant and enforce it over the long term. Surprisingly, Goldenberg says, companies often don't make that calculation: "If you are going to spend $10,000, $20,000, or more to get one, you ought to know why you are getting it," he says.

There are, of course, many reasons for pursuing a patent. In some cases, companies and individual inventors will pursue patents in order to make money licensing technology to other organizations—or getting damages when they don't, as scientist Ralph Benghiat did.

New startup firms may get patents to secure financial backing. "When it comes to young companies, investors love patents," says Lampert. That is especially true in the biotech field. Since the typical biotech firm isn't profitable for 10 years, its patent portfolio is its primary asset.

"In the biotech world," says Ken Haas, president and CEO of two-year-old Protein Mechanics in Mountain View, California, "the rule is basically: no



patent, no company. In other areas of technology, you create value by technology, by sales and marketing, and by operational efficiency, but biotechnology companies primarily create value through technology." As a result, a viable patent portfolio is essential to attracting the lifeblood of startup biotech companies: venture capital firms and larger pharmaceutical corporations looking to collaborate on the next blockbuster drug.

For most established companies however, patents are useful because they let them defend their markets and keep competitors at bay. For these companies, the key is considering whether "you have the technology to make a successful product, whether you are going to be able to sell that product, and if you are going to be able to establish any exclusivity of your own in that product," says Lampert. "It goes straight across your business strategy. It's not simply that you want an exclusive on widgets. I always tell clients their major goal is to sell product."

As Andy Gibbs, co-author of *Essentials of Patents* and founder of Patentcafe.com, an online service that provides data, news, and education about patents and other IP properties, puts it, "There's a philosophical difference between looking at a patent as the end game versus looking at the product in the marketplace and the patent as a tool to protect revenue. A patent is a protection of a market. If there's no market, forget the patent."

The strongest possible patent

At least as critical as the decision to patent, experts agree, is the way the patent is written. A carefully crafted

"A patent does not give you **the right to make something**," notes Lampert. "All a patent gives you is the right to exclude others from doing something."

patent goes a long way toward ensuring the collection of royalties and/or damages should infringement—and litigation—occur. A poorly written patent, however, can be tantamount to no patent protection at all. In between are patents that don't quite do what their holders hoped they would.

Take, for example, a "narrow" patent that is written with extensive but unnecessary detail. "Let's suppose that a patent claim is written for an engine that contains eight cylinders," Lampert suggests. "It says there is a spark plug for each of the eight cylinders. That claim no longer covers any steam or diesel engines, which have no spark plugs. It doesn't cover engines in smaller cars because they typically have four to six cylinders and this patent is written for eight cylinders. It's a much narrower claim, and it covers a lot less."

Beyond the writing of the patent application is the need for a thorough search of "prior art"—the applicant's proof that that patent is "new" or "novel." Given that a defendant in a litigation action is likely to have upwards of 20 independent defenses available to refute your patent's validity—and only one of those has to hit the mark—it's clear that doing your homework up front will pay off later.

The responsibility for doing that research clearly rests with the patent applicant. An application may well result in a blessing from the U.S. Patent and Trademark Office (USPTO), but, while the office does do a prior art search, its research time, and its reach, is limited; in the event of a lawsuit, your competitors are going to have a big incentive to really dig deep in the search for prior art that might render your patent invalid. So it's best that you do the digging first.

Before You Patent

"You get patents even if you're unwilling to litigate them," says Hale and Dorr's Jim Lampert. But there should be a strategy behind the patent, based on answers to such questions as:

- Does a market exist for your invention?
- Do you have the technology to make a successful product?
- Will you be able to sell the product?
- Will you be able to establish exclusivity in your product?
- Are there other benefits, such as licensing opportunities inherent in your product—or the technology behind it?
- Will having a patent on this product help you protect your hold on the market?

Protecting your territory

Once a patent is in place, companies should be ready to enforce it—though this doesn't mean rushing headlong into litigation. No matter how strong your patent is, experts caution, the typical patent lawsuit will run into seven figures. And that's just the financial consideration. "There's also the personnel drain," says Goldenberg. "When your tech managers are not developing your next product and instead are talking to lawyers about last year's work, there's both a significant money cost and an opportunity cost."

Given the costs of litigation, even the best outcomes might not be worth the effort, especially if other options exist—and they quite often do. In fact, Lampert notes, the vast majority of patents never get litigated, in part because patents tend to keep other people from selling complete knock-offs of your product in the first place, and in part because there are a number of avenues to explore before going to court.

For example, he suggests, there's the bargaining chip a patent provides. "Say I have a patent on tires, and you have a patent on a transmission. A car needs both. You and I now have an opportunity to make a great deal, and we can both go out and sell cars."

A sizable patent portfolio, of course, makes that bargaining chip even stronger. "Having only one patent is like having one star player on a basketball team," says Patentcafe.com's Gibbs. "A portfolio makes it more difficult for someone to challenge your patent when you have different ways to go." Moreover, he adds, if someone accuses you of infringement, you're in a better position to bargain outside of court by offering another of your patents as a settlement.

That, in essence, is what Sanyo Electric Co. offered Eastman Kodak Co. to settle an infringement lawsuit. In lieu of a courtroom showdown, the two companies agreed to cross-license their patented digital camera technologies. Under the

"For people who aren't experienced with patent litigation or are in a real rush to get started, **a patent feels like a saber**, and they often want to get out and rattle it," says Goldenberg.

agreement, Sanyo provided Kodak with access to its digital camera patents and offered Kodak's online photo-finishing services with its digital cameras. In exchange, Kodak dropped the lawsuit and gave Sanyo a license to more than 1,000 Kodak patents.

If you must sue...

Not every company, however, is in position to strike a bargain or discourage competitors with its patent portfolio—and, at times, litigation may be the only way to protect a critical product or market. But before heading to court, it's wise to do some research to find out what you're getting into. "Find out what type of a company the competitor is," says Goldenberg. "For example, if you are getting ready to sue someone that only has a single product and it's based on the technology in question, what you are putting on them is a life-or-death struggle—and they'll fight hard."

Goldenberg also recommends taking a good look at the products involved and determining objectively whether they are what you think they are. In doing such work, he says, "we generally obtain a sample of the infringing product, and confirm through testing or reverse engineering that it really does work the way we think it does, and that it really does infringe the patent."

It's important to look at the patent itself, as well. "Are you sure it's what you think it is?" Goldenberg asks. "Have you realistically estimated its strength? Talk to the inventors of the product, for example, to make sure that since the time you filed the patent, they haven't come to the belief that the thing is actually invalid because of some prior art that has surfaced, or that it is less useful than they originally thought."

Often, by the time people are ready to litigate, they want to move ahead quickly—but that's a temptation to which they shouldn't succumb, experts warn. "For people who aren't experienced with patent litigation or who are in a real rush to get started, a patent feels like a saber, and they often want to get out and rattle it," says Goldenberg. That, he notes, can be a dangerous approach. A procedural misstep in the early stages of a lawsuit can result in enormous—and unnecessary—extra costs, time, and hassle.

Goldenberg describes a hypothetical small company in Washington, D.C. that believes that Microsoft—in Redmond, Washington—has infringed on one of its patents. The company sends a letter and a copy of the patent to Microsoft, demanding that the software giant stop using the technology. Microsoft comes back with a "declaratory judgment action." The catch: The action will take place at a court in Redmond. "So instead of enforcing your patent on the East Coast, where you live, you now have to hire lawyers in Redmond and enforce there," says Goldenberg. "The risk involved in sending the hard, threatening letter is that you empower the recipient or grant them the standing to sue for declaratory judgment."

Critical in this—and probably almost any other example—is the tone of your initial contact with the alleged infringer. Do you want to adopt a tough stance? Or might a kinder, gentler approach better serve your needs? While every case is different, Lampert suggests one rule of thumb: consider the consequences in any action you take, any strategy you adopt. "If, for example, you sue IBM, think about what's coming back over the fence," he says. "If you throw a hand grenade and a nuclear bomb comes back, that wasn't a very good trade."

California-based journalist Stephanie O'Neill wrote about harmonization in the Winter 2003 issue of IP Business.

Before You Sue

While a well-written patent based on a strong business case may appear to give the patent holder an edge in litigation, the costs of litigation often mitigate against it as a strategy. Consider the following:

- Are you willing to license the technology to the infringer?
- Can you form an alliance that is mutually beneficial?
- Can you use the patent—or other patents in your portfolio—as a bargaining chip?
- Have you considered the strengths of your adversaries and the consequences of a suit?
- Have changing business realities made the patent less important to you, or undermined its validity?
- Are you sure your patent does, in fact, cover the technology in question?

Building a Better Portfolio

Intellectual property should be managed—not just collected.

By Peter Haapaniemi

Illustration by Mick Wiggins

It has become a fundamental business tenet that intellectual property is a vital asset—but you wouldn't know it by looking at how it's handled at many organizations. "A lot of companies don't have much direction in managing their intellectual property," says Henry Wixon, senior partner at Hale and Dorr. He explains that some companies try to patent virtually everything they invent. Others limit their patent efforts to new products they develop—or simply focus on patenting inventions that are backed by the most persuasive executives.

For most companies, a more disciplined approach can pay off in several ways. By managing their collections of patents as an interrelated whole—that is, as a portfolio—companies can protect themselves and their products, and compete more effectively.

They can also save money, Wixon adds. "If you were to file a patent application and obtain a patent in every country that's under the Paris Convention for the Protection of Industrial Property (more than 150 member countries), you would be talking about an investment of up to $1 million, plus ongoing maintenance fees," he says. "Certainly, most inventions don't justify that kind of extensive coverage, but there clearly is a significant expense involved in filing. So you want to be in a position to make rational decisions about how you spend your IP dollars."

Each situation is different, but a few basic guidelines can help most companies take a more rigorous approach to building and managing an effective IP portfolio.

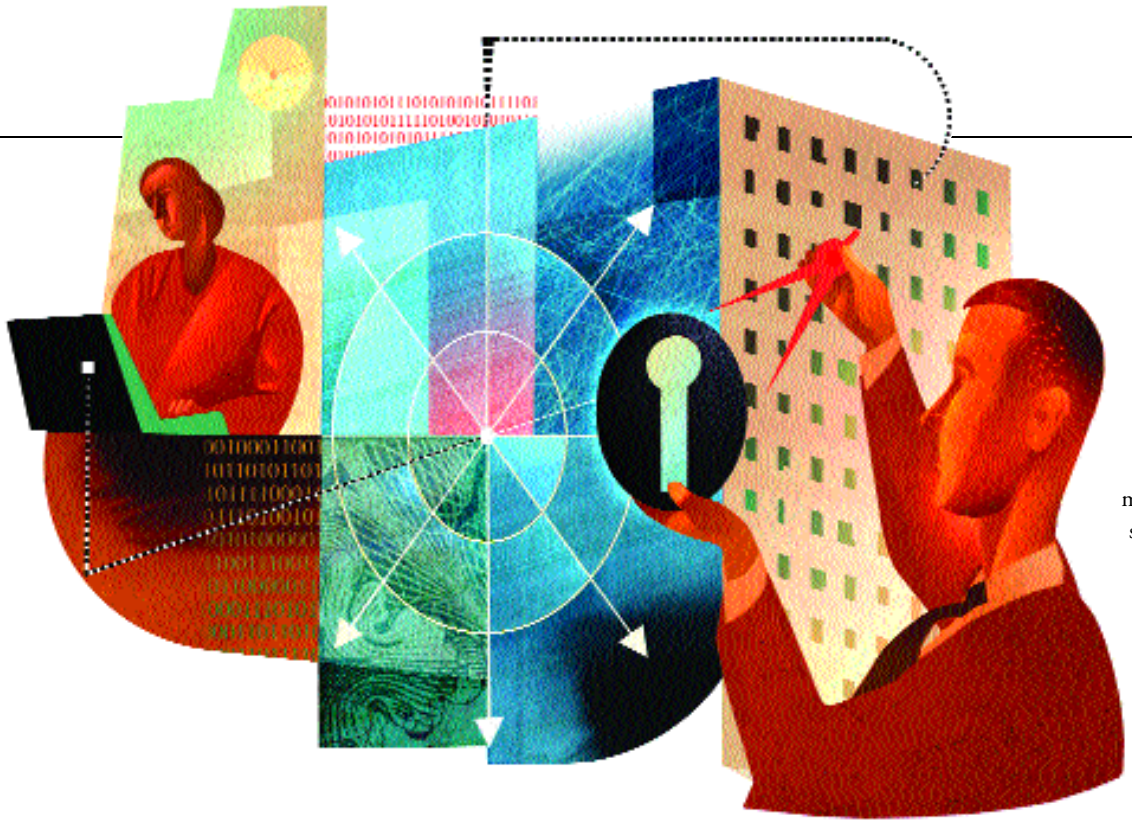
GET THE RIGHT PEOPLE INVOLVED

Companies should have a formal IP committee that is in charge of maintaining the IP portfolio—and that committee should include people from several key areas, says Wixon. In addition to IP attorneys, it should have executive-level representatives from R&D, production, and the CFO's office—"so the committee is in a position to make decisions about spending money," Wixon says.

That list should also include marketing, in order to head off some common problems. "For example, marketing people often like to tell customers about new products that the company is going to make available," Wixon says. "Under U.S. law, you have one year from the first offer for sale of a product to file your patent application. After that, you lose the right to get a patent. The clock can start ticking when marketing starts talking to customers, but the patent people don't know that's happening, so they might end up filing a year and a half later—which is too late. If you have marketing people on the IP committee, they are less likely to be getting out in front of the patent people."

THINK BEYOND THE PRODUCT

Inventors are naturally inclined to find a solution to a problem and move on, without considering a lot of alternate ways to solve the problem—and that approach can miss a lot of potential value. A pharmaceutical researcher, for instance may find a molecule that works with a certain recep-



tor in the body—but there may be dozens of other variants that might work just as well. "The researchers won't want to bother hunting those down," says Michael Twomey, junior partner at Hale and Dorr. "But when you try to obtain a patent and you have just a single example of something, the patent office will often limit you to that single example. On the other hand, if you can show that two or three members of a class of compounds works, you might get patent claims that cover that entire class."

The broader patent would, of course, be harder for competitors to design around. Also, with a range of related patents in hand, a company can create a defensive "picket fence" that can discourage competitors from getting close to its product space for fear of infringing on one of its patents, Twomey explains. Such patents can also be used as bargaining chips in case the company is sued for infringing someone else's patents. Overall, he says, "You can sometimes gain a lot of protection from a little additional research that is relatively easy and cheap."

RECYCLE UNUSED IP

"IP is an asset—it's not something that you collect like stamps," says Twomey. "When that asset ceases to serve a useful purpose for you, see if you can get something for it." Certainly, some patents that are no longer relevant should be abandoned. But others might provide a basis for a new business or division, or be of value to other companies. "The classic example is Texas Instruments," says Wixon. "Years ago, they took a hard look at their portfolio. Not all of it was pertinent to their core business, but a lot of it was pertinent to somebody's business." Texas Instruments created a group that actively licenses its IP to other companies—and that group generated billions in licensing revenues for the company, Wixon adds.

REVISIT THE PORTFOLIO REGULARLY

Changes in business direction can cause a disconnect between the business and the portfolio. For example, a startup company that sets out to be in several related businesses, such as vaccines, drug discovery, and medical devices, may pursue patents in all those areas. A few years later, however, it may be focused solely on vaccine development—but still be paying to prosecute and maintain patents in all those areas. "The business plan has changed, but the word never gets out to the people who are working on the portfolio, and the company is hemorrhaging money as a result," says Twomey. The solution: Regular IP audits to make sure that the portfolio stays in sync with the business.

FIGURE OUT WHAT YOU HAVE

The IP committee should perform an audit to determine what, in fact, the company has in its portfolio. The audit should be thorough, and include not only patent applications but such other IP as trademarks, trade secrets, and copyrights. "The idea is to create a complete picture of what the company owns, either for its own use or for licensing to others," says Wixon. That complete picture can be used to identify gaps and opportunities in the portfolio and create plans for managing the portfolio over time. "The IP audit is a critical starting point for the IP portfolio," Wixon says. "It lets you begin to make systematic, business-driven decisions about IP, and make sure that this important asset is not approached as an afterthought."

Bringing Method to the Madness

Now that the hype over business-methods patents has cooled, these patents appear to be regaining an important role in IP strategy.

By Peter Haapaniemi

In 1998, the Court of Appeals for the Federal Circuit ruled, in a case known as *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*, that Signature Financials' patent for pooling and handling mutual funds was, indeed, valid.

The impact of the case was quickly felt far beyond the financial services industry. In essence, the ruling solidly affirmed that business methods were patentable—much to the surprise of many IP experts, who had long thought that business methods, like the laws of nature, could not be protected. Now, the court was telling the experts to think again.

The ruling triggered something of a gold rush. Many companies raced to file patents on business methods—especially firms in the high-tech and financial services fields, where innovative approaches to business are considered key competitive assets. The combination of the *State Street Bank* ruling, the rise of computer-driven business practices, and the advent of the Internet "was a 'perfect storm' that really prompted phenomenal increases in [business-methods] filings " says Brigid Quinn, deputy director of public affairs at the U.S. Patent and Trademark Office (USPTO).

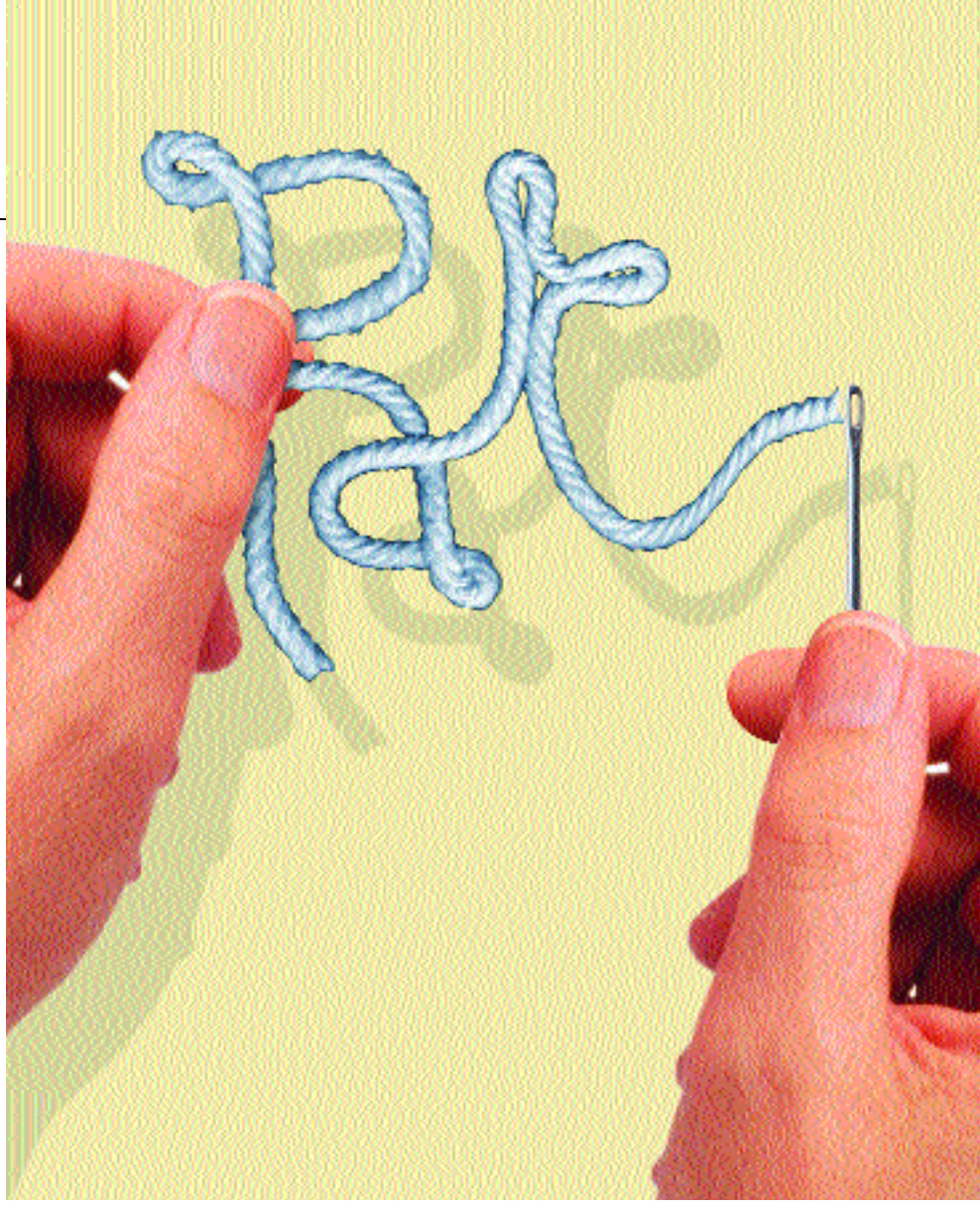
Within a short time, patents were being granted for such methods as selling music online, handling online credit card transactions, managing electronic shopping carts, and tracking Web-user activity. So overwhelmed was the USPTO with business-methods patent applications that when Andy Gibbs visited the patent office and found himself in "a room that had method patent applications in yellow folders, the room glowed." says Gibbs, who is CEO of PatentCafe.com, an online service that covers the intellectual property community. "They had to dedicate a room just to handle the applications that they hadn't even opened yet."

Soon, high-profile business-methods patent infringement cases were making headlines. Amazon.com sued Barnesandnoble.com for infringing on its famous "one-click" shopping method. Priceline.com sued Microsoft over Priceline.com's patent on the reverse-auction method, which lets users name their own prices for products.

As often happens in a gold rush, however, the furor seemed to die down as suddenly as it had arisen. Within just a few years, the number of filings tapered off significantly. The news media moved on to other topics. Today, says Peter Dichiara, a senior partner at Hale and Dorr in Boston, "getting a business-methods patent is something of an uphill battle."

But that does not mean that the issue has died and gone away. "The feeling right now is that the flurry is over and we're in the eye of the storm, so everything is calm," says Gibbs. "There's kind of a wait-and-see attitude." There are still a lot of issues to sort out, Gibbs says, but business-methods patents are most likely here to stay. As a result, he suggests, com-

Illustration by Milan Trenc



panies should start determining what these patents might mean to their intellectual property portfolios, and how to best take advantage of this evolving field.

What happened?

The notion of patenting business methods is not totally new—indeed, claims have been made for methods involving mechanical and, later, electronic data processing for a century, according to the USPTO. But the *State Street Bank* case thrust the issue squarely into the public spotlight and provided clear, official approval for business-methods patents. "After 1998, people felt much more secure filing patents in that area," says the USPTO's Quinn. Many business methods fall under the patent office's Class 705 group, which encompasses data processing methods. From 1998 to 2001, the patent office saw a six-fold increase in the number of patent applications in that class, and a doubling of the number of patents granted in the group.

If the *State Street Bank* case opened the door to business-methods patents, what closed that door just a few years later? "A big factor was the bursting of the dot-com bubble," says Hale and Dorr's Dichiara. "A lot fewer people are filing applications now, and for a lot of the applications that have already been filed, the dot-com companies no longer have the money to continue pursuing them." In addition, he says, potential filers may be put off by the delays in getting applications processed, which have only increased due to the backlog of work dating from the late 1990s. "Today, you are looking at a two-to-three-year wait before the patent office even begins to consider an application on its merits," Dichiara says.

The decline in applications may also be due to uncertainties about what's in all those applications that are waiting to be processed, says Gibbs. That is, companies may well want to see what is already in the pipeline to be patented before going ahead with their own applications. "Once [those patents] start issuing, the field that you can patent in becomes narrower and narrower," Gibbs notes. Naturally, companies may be reluctant to invest in patenting their own methods without a better sense of what patents they might end up infringing on.

Finally, changes at the patent office itself seem to be contributing to the drop-off of business-methods patents. In the late 1990s, a number of observers criticized what they saw as inappropriate patents for all sorts of methods, citing, for example, an airline toilet reservation system ("The method: first come, first served," noted the *Los Angeles Times*), or a technique for swinging a child's swing from side to side, rather than front to back. Many of the Internet-based business methods, they argued, were really just applying computers to traditional,

commonly used paper-based practices, rather than providing anything new.

The controversy was enough to prompt Jeff Bezos, the CEO of Amazon.com—which had borne its share of the criticism—to write that "the patent laws should recognize that business-methods and software patents are fundamentally different than other kinds of patents." He suggested that business-methods patent applications be subject to a public comment period and be given a shorter lifespan than traditional patents.

"You can imagine that when we started issuing patents on ways of doing business on the Internet—which itself was relatively new—some people became very skeptical," says the patent office's Quinn." I think a lot of that was a misunderstanding about what is patentable and how the whole thing works. But when you have a public perception, you have to deal with it."

In response, the patent office added examiners to its Class 705 area, and began to build up its database of Class 705 "prior art," or documentation that helps examiners assess the originality of an invention. Perhaps most notable were changes to the review process itself. "We put in place some quality initiatives above and beyond the normal ones that most patent applications go through," says Quinn. "Probably the best known of these is what we call the 'second pair of eyes,' where a supervisor at the end of the line checks before a patent is issued."

That second review has clearly made it more difficult for questionable applications to make it through the process, and presumably dampened some of the hype and excitement around business-methods patents. "Some of the early business-methods patents were fairly broad… We're much narrower now," James Rogan, director of the USPTO, told the *Los Angeles Times* earlier this year. "We've gone from a 75 percent acceptance rate to a 75 percent rejection rate" on such patents.

Playing by the new rules

The question, then, is what does the changing business-methods landscape mean to a company's intellectual property strategy? Scott Alter, a senior partner at Hale and Dorr in Washington, recommends starting with the basic questions that would apply to any patenting effort—factoring in, of course, the increased scrutiny and longer processing times that now apply to business-methods applications. Alter points out that these basic questions are the same for business methods as they are for any other technology, that is, does the invention meet the three basic patent criteria of being novel, non-obvious, and useful? "You should thus ask, what are the odds of getting it through the patent office, based on a consideration of these basic questions," says Alter. "What scope of protection might you hope to maintain when all is said and done? Is it worthwhile to go this route as opposed relying on some other form of intellectual property protection?"

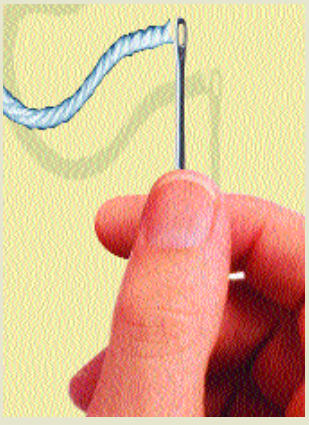
Companies should also consider the international ramifications of pursuing a business-methods patent. For example, a method that is patented or published in the U.S. won't necessarily make it through the European patent process, where business methods aren't patentable. That means that a European company might then be free to use the method without the U.S. company's permission, says Hale and Dorr's Dichiara. "Business-methods patents are largely a creature of the U.S., so you probably want to start out by assuming that a patent is just going to give you protection in the U.S.," he says.

In pursuing a patent, it may be worthwhile to go the extra mile in completing the application, Dichiara contin-

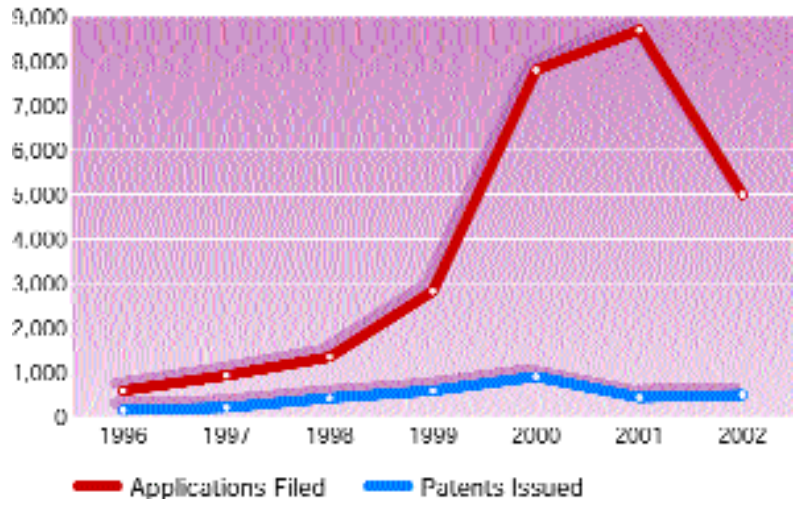
What Is a Business Method?

That's a good question, experts say.

Despite the attention business methods have received, the term "business method" hasn't been carefully defined by the courts or Congress. For its part, the USPTO looks at methods in terms of the technology they relate to, rather than as a distinct, narrowly defined type of invention. For example, methods for teaching would fall into Class 434, Education and Demonstration, while methods for improving farming would be in Class 47, Plant Husbandry. With the rapid evolution of e-business, many business methods have been put into Class 705, which carries the somewhat cryptic title of "Data processing: financial, business practice, management, or cost/price determination." In essence, says Hale and Dorr's Scott Alter, the world of business-methods patents is evolving, and "it's not a hard, fast science."



CHARTING THE RUSH



In the 1990s, the number of applications and patents granted for the USPTO's Class 705—which is typically associated with business methods patents—rose dramatically, driven in large part by the advent of e-business. The number of patents granted fell significantly from 2000 to 2001, coinciding with USPTO efforts to improve the quality of patents in the class. The number of applications fell the following year, presumably because of higher patent office standards for granting business-methods patents—and the demise of many dot-com companies that had been pursuing such patents.

ues. "There is no legal requirement that you do this, but you can sort of state your case as to why you think this really is an invention and not just an obvious idea," he explains. "You might provide, for example, newspaper articles or third-party declarations saying that, yes, there's a real invention here."

Often, patenting may not be the best route, especially in light of the long processing times for Class 705 and the increasingly short lifespan of business innovations. For example, if the business method is used only internally, a company might simply keep it a trade secret. Or, inventors might look for ways to move a business method out of Class 705, and thereby avoid that second pair of eyes, by giving it a more traditional technical character—a move that can also make the innovation more patentable in Europe. For example, a company might talk about its innovation as being a computer network, rather than a method of presenting information and collecting sales input.

For a sound, innovative business method, however, the rigorous review process may not be all that bad. "You may not always want to hope you avoid Class 705," says Alter. "If you want a patent that's able to withstand more scrutiny in litigation, maybe it's not so terrible for the application to be in Class 705, since it will receive a more thorough review. It will probably take longer and cost more money, but it may be a blessing in the long run. On the other hand, if money and/or time is a critical factor or you're obtaining a patent primarily for reasons that would not likely involve litigation, Class 705 might not be desirable."

Gibbs recommends including licensing efforts in any business-methods strategy. That is, while a company is pursuing a business-methods patent, it can also be searching for related patents that are pending and try to get licenses for them. If the licensed method is eventually granted a patent, it can augment your method and strengthen your defensive patent position. And if your own method fails to win a patent, you can continue to move forward with your business using the licensed method. What's more, it's probably a good time to be in the market for licensing business methods, Gibbs points out. "Many of them are going to be [held by] the dot-comers that are still hanging on, and they are likely to look at a very reasonable price for a license," he says.

Certainly, business-methods patents are not as easy to come by as they were in the immediate wake of the *State Street Bank* case—and anyone pursuing them will have to be diligent and patient. But no company should shy away from trying to patent a business method—if the idea deserves patenting. "It may take a bit longer and the patent office may be a little more hard-nosed about it," says Hale and Dorr's Alter. "But that doesn't mean business-methods patents aren't being issued. They are. And courts are finding at least some of them valid and infringed. For example, eBay was just found liable for infringement, resulting in an award of damages for the patent owner in the tens of millions of dollars. So if you think you have something that is novel and non-obvious, you should still go for it."

Peter Haapaniemi, a Farmington, Michigan-based journalist, writes frequently about business, technology, and the law.

Faster, Better, Cheaper...

Following up on several stories covered previously in IP Business.

Madrid Protocol Global Trademarking Made Easy

While U.S. patent holders won't see a harmonized global patent system in the near future ("A Better Mousetrap," *IP Business*, Winter 2003, page 2), U.S. trademark applicants are just months away from enjoying a one-stop international trademark system. Beginning this November, the U.S. will join 56 other nations in a global trademark agreement called the Madrid Protocol. "American businesses—large and small—seeking to market their products in new countries can gain valuable protection for their trademarks faster and less expensively," says Anne Chasser, the U.S. Patent and Trademark Office Commissioner for Trademarks.

For instance, she says, the streamlined process will allow applications to be submitted in English, eliminating costly translation fees. What's more, applicants will pay a single set of fees rather than multiple fees to all the nations in which a trademark is sought.

Under the new procedure, U.S. applicants will file their request for trademark protection with the USPTO. The form will allow them to simply check off the nations in which trademark protection is desired. The USPTO will send the form to the World Intellectual Property Organization (WIPO), which will forward it to the chosen nations. Trademark officials from those countries will examine the application. If approved, an international trademark will be established for 10 years.

—Stephanie O'Neill

Hatch-Waxman Reform: Sidelined but Not Forgotten

International events have largely pushed Hatch-Waxman reform further down Congress' agenda, but new Food and Drug Administration rules that would bolster generic drug competition are still in the works ("Whose Drug is It, Anyway," *IP Business*, Winter 2003, page 6). The Bush administration proposed the new rules, which are designed to get generic drugs to the market faster, last October, and all sides had a chance to file their comments with the FDA in December. Generic drug companies and consumer groups say they like the new rules because they would close some of the perceived loopholes in Hatch-Waxman, the law that essentially launched the generic drug industry. Brand-name pharmaceuticals say the new rules go too far and could discourage innovation. The proposed rules should become official in the coming months, after final FDA revisions.

—Jennifer Taylor

And Now for Something Not Exactly Completely Different

Not limited by the new rules is a pharmaceutical company's ability to file a patent on a slightly different formulation of a drug that is about to go off-patent—an apparent effort to preserve market share. For example, it was nearly impossible to miss last year's barrage of TV ads for Clarinex, a cousin of the allergy drug Claritin. Claritin's patent expired in December 2002; as expiration approached, Schering-Plough began its blitz to get people to switch to newly patented Clarinex. Some saw this as a kind of "bait-and-switch" game to use a new, but not necessarily better, drug. But the strategy is perfectly legal, says Nels Lippert, an intellectual property attorney and partner-in-charge of Hale and Dorr's New York office. "It's nothing more than getting people to be aware of the new product, go to their doctor, and say 'It's supposed to be better,'" Lippert says. "Then their doctor will write them a prescription."

The strategy seems to have had some limited success. U.S. sales of Clarinex totaled $146 million in 2002, with much of that coming from people converting from prescription Claritin to Clarinex, according to the company. Schering-Plough has also started selling an over-the-counter Claritin, but even the company acknowledges that with generic competition, it would be impossible for Clarinex and OTC Claritin to make up for lost prescription Claritin revenue, which reached $1.8 billion in 2001.

—Jennifer Taylor

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