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Alice's Wonderland? Software Patents after the Supreme Court's *Alice Corp.* Decision

By Thomas M. Morrow



It has been a tumultuous six months since the Supreme Court's *Alice Corp.* decision. An increasing number of patents have been found invalid and more Section 101 challenges are being filed. The future of software patents remains unclear. Intellectual property lawyers are wise to keep abreast of every new development.

THE U.S. SUPREME COURT'S JUNE 19, 2014 decision in *Alice Corp. Pty. Ltd. v. CLS Bank Int'l*¹ ushered in a bruising six months for software patents. In *Alice*, a unanimous Court held that four software patents never should have been granted by the U.S. Patent Office because they covered merely an "abstract idea" ineligible for patenting under Section 101 of the Patent Act.²

In the six months following *Alice*, the vast majority of courts considering a Section 101 challenge to a software patent held the patent invalid as covering an unpatentable abstract idea. The Patent Office responded to *Alice* by issuing not one, but two sets of guidelines to its examiners following the decision, and took further steps to halt the issuance of some software patents that stood approved by the Office.

Alice, and the eventful six months that ensued, present a number of intriguing considerations and challenges for those who invent, own, and litigate software patents.

The Road by Which Software Patents Rose to Prominence

The first electronic computer was the model 701, introduced by IBM in 1953.³ At the time, the term "software" was not yet in use—it emerged as a term of art in 1960—and IBM did not seek a patent on the model 701, having earlier decided that computer programs and processes were not eligible for patenting under U.S. patent law.⁴

The categories of inventions that are eligible for patenting are identified in Section 101 of the Patent Act, which states:

Whoever invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent therefor, subject to the conditions and requirements of this title.⁵

The foregoing language is drawn nearly word-for-word from the original Patent Act of 1793, authored by Thomas Jefferson,⁶ "the first administrator of our patent system."⁷ Over the years, courts have identified and enforced three important exceptions to Section 101's broad definition of patentable subject matter, namely, that "laws of nature, natural phenomena, and abstract ideas are not patentable."⁸ As the Supreme Court has explained:

A new mineral discovered in the earth or a new plant found in the wild is not patentable subject matter. Likewise, Einstein could not have patented his

celebrated law that $E=mc^2$; nor could Newton have patented the law of gravity. Such discoveries are manifestations of ... nature, free to all men and reserved exclusively to none.⁹

Thus, IBM's decision in 1953 not to patent the first computer was neither illogical nor unusual; indeed, more than a decade later, the efforts of another early software developer, Informatics Corporation, to patent its Mark IV file management system—an early database—were stymied in the United States due to the prevailing view that mathematical laws (and inferentially, computer algorithms used in the Mark IV system) were not patent-eligible under Section 101.¹⁰

But in the late 1960s, the Patent Office began reconsidering this view, in fits and starts, articulating a position in August 1966 that computer programs could be eligible for patenting so long as they met the requirements of either a "process" or an "apparatus,"¹¹ then issuing contradictory guidelines in October 1968 that took a more restrictive view,¹² only to rescind those guidelines a year later.¹³ Software patents began issuing, an early example being U.S. Patent No. 3,533,086, titled "Automatic System for Constructing and Recording Display Charts," which issued in October 1970 and covered a product that could read a computer program and generate and print a flowchart that accurately depicted the program, thereby relieving the software developer of such "documentation chores."¹⁴ Still, questions continued to exist about the boundaries of patent protection for software.

The U.S. Supreme Court weighed in on the issue three times between 1972 and 1981. The Court's first two decisions rejected patent applications under Section 101: *Gottschalk v. Benson* (1972) unanimously rejected an application on a method for using a computer to convert binary-coded decimal numbers into pure binary numbers¹⁵ and *Parker v. Flook* (1978) held unpatentable a process for automatically updating an alarm limit within a computer control system in a chemical plant—but by a 6-3 margin this time.¹⁶

Finally, in *Diamond v. Diehr* (1981), the Court deemed patentable an invention involving the use by a computer of a mathematical formula—namely, a method for controlling the operation of a rubber press, by measuring the temperature within the press, feeding the temperature to a computer and causing it to continually recalculate the optimum cure time via a mathematical equation long-used within the industry to calculate cure time.¹⁷ *Diehr* was a 5-4 decision that turned on the reading given to the patent's claims (the closing portion of a patent that delineates the precise boundaries of the invention for which the patent right is claimed). Viewed one way, the



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claims could be seen as covering a patentable method of operating a rubber press. Viewed another way, the claims could be seen as covering a method of updating the cure time, strikingly similar to the unpatentable process for automatically updating an alarm limit rejected three years earlier in *Flook*.¹⁸

Diehr, decided in 1981, was the Supreme Court's last foray into the patent-eligibility of software patents for 29 years. The next year, 1982, saw the creation of the Court of Appeals for the Federal Circuit (the Washington, D.C.-based appeals court that has nationwide jurisdiction over appeals in all patent cases),¹⁹ and in 1998, that court issued its famous *State Street*²⁰ decision that caused software patenting to skyrocket. *State Street* upheld the validity under Section 101 of a patent for a computerized accounting system for managing mutual funds, and explicitly clarified that business methods can be patentable subject matter.²¹ An explosion of patents on software-embodied business methods ensued.²²

Alice's Path to the Supreme Court

Within a decade, warning flags began to emerge. The Federal Circuit abrogated *State Street* in 2008 in *In re Bilski*, a case in which it held ineligible, under Section 101, a patent application for a method of teaching buyers and sellers of commodities how to hedge against the risk of price fluctuations in the energy market.²³ The Federal Circuit in *Bilski* articulated a "machine or transformation test" as a new standard for patentability under Section 101, but on appeal, the Supreme Court made clear that the Federal Circuit's new test was not the sole test for patent-eligibility.²⁴

The Supreme Court did confirm that business methods were not *per se* unpatentable; however, as to *Bilski*'s particular invention, the Court affirmed the Federal Circuit's decision that it was unpatentable under Section 101, amounting to merely an attempt to patent the abstract idea of risk hedging, as a concept and a mathematical formula.²⁵

Post-*Bilski*, amid the uncertainty over the proper framework with which to analyze the patent-eligibility of software patents, the Federal Circuit continued to uphold some software patents under Section 101. For example, it upheld U.S. Patent No. 7,346,545, directed to a method for distributing copyrighted media products over the internet via a facilitator, in *Ultramercial, Inc. v. Hulu, LLC*, reversing a trial court's decision that the '545 patent failed to satisfy Section 101.²⁶ However, the Supreme Court granted cert, vacated the decision, and remanded for further consideration in view of its decision in a Section 101 case dealing with medical test kits.²⁷ Yet on remand, the Federal Circuit maintained its position that the software patent in *Ultramercial* remained patent-eligible under Section 101.²⁸

And the Federal Circuit upheld the four patents in *Alice Corp.* Those patents dealt with a system and method for reducing settlement risk for parties to commercial transactions, using a computer system as a third-party intermediary:

The [computer system] intermediary creates “shadow” credit and debit records (*i.e.*, account ledgers) that mirror the balances in the parties’ real-world accounts at “exchange institutions” (*e.g.*, banks). The intermediary updates the shadow records in real time as transactions are entered, allowing “only those transactions for which the parties’ updated shadow records indicate sufficient resources to satisfy their mutual obligations.” At the end of the day, the intermediary instructs the relevant financial institutions to carry out the “permitted” transactions in accordance with the updated shadow records, *ibid.*, thus mitigating the risk that only one party will perform the agreed-upon exchange.²⁹

The four patents-in-suit in *Alice* were granted by the Patent Office between 1999 and 2010.³⁰ In 2007, while some of the patents were still pending in the Patent Office, CLS Bank brought a declaratory judgment suit asserting that the issued patents were invalid, unenforceable or not infringed. Before the trial court, after the Supreme Court’s decision in *Bilski*, the parties cross-moved for summary judgment as to the eligibility of the patents under Section 101. The trial court held them unpatentable under Section 101, as covering merely an abstract idea of using a neutral intermediary to facilitate simultaneous exchange of obligations to minimize risk.³¹

The three-judge panel of the Federal Circuit hearing the appeal reversed 2-1, holding that CLS Bank had not made it “manifestly evident” that the patents were directed to an abstract idea.³² But the full Federal Circuit then took the case *en banc*, granted a rehearing, vacated the panel opinion, and issued a single-paragraph *per curiam* opinion affirming the trial court.³³ The *per curiam* opinion was accompanied by five separate opinions authored by various blocs of the *en banc* court,³⁴ evidencing the difficulty the judges encountered in grappling with the patent-eligibility of *Alice*’s patents.

The Supreme Court’s Decision in *Alice*

Against that background of a deeply divided Federal Circuit, the most breathtaking aspect of the Supreme Court’s decision in *Alice* was the utter ease with which a unanimous Court held the patents invalid under Section 101. Justice Clarence Thomas’s opinion began by emphasizing the basis for the long-held exceptions to patentability:

[T]he concern that drives this exclusionary principle [is] one of pre-emption. Laws of nature, natural phenomena, and abstract ideas are the basic tools of scientific and technological work. Monopolization of those tools through the grant of a patent might tend to impede innovation more than it would tend to promote it, thereby thwarting the primary object of the patent laws. We have repeatedly emphasized this concern that patent law not inhibit further discovery by improperly tying up the future use of these building blocks of human ingenuity.³⁵

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Justice Thomas then applied a two-step framework for evaluating patent eligibility. First, a court determines whether or not the patent is directed to one of the patent-ineligible concepts (laws of nature, natural phenomena, and abstract ideas); if it is not, Section 101 is satisfied. If, however, a patent-ineligible concept is involved, then a court will search for “an inventive concept—i.e., an element or combination of elements that is sufficient to ensure that the patent in practice amounts to significantly more than a patent upon the ineligible concept itself.”³⁶

In step one, Justice Thomas readily found the patents to be drawn to the abstract idea of intermediated settlement. Likening it to the risk hedging in *Bilski*, he found intermediated settlement to be a long-standing, fundamental economic practice. Indeed, he found “no meaningful distinction between the concept of risk hedging in *Bilski* and the concept of intermediated settlement at issue here. Both are squarely within the realm of ‘abstract ideas’ as we have used that term.”³⁷ Proceeding to step two, he found no inventive concept, but merely routine, generic computer implementation of the idea of intermediated settlement.³⁸

Reviewing *Benson*, *Flook* and *Diehr*, Justice Thomas concluded that those cases showed that “the mere recitation of a generic computer cannot transform a patent-ineligible abstract idea into a patent-eligible invention. Stating an abstract idea while adding the words ‘apply it’ is not enough for patent eligibility. . . . Thus, if a patent’s recitation of a computer amounts to a mere instruction to implement an abstract idea on a computer, that addition cannot impart patent eligibility.”³⁹ Finding *Alice*’s four patents to amount to no more than implementation on a generic computer of the abstract idea of intermediated settlement, he deemed them ineligible for patenting under Section 101.⁴⁰

Alice’s Aftermath

Eleven days after *Alice*, the Supreme Court took up *Ultramercial* again, and once more granted cert, vacated, and remanded (G-V-R) for further consideration, this time in view of *Alice*.⁴¹ (Indeed that day, the Court considered three petitions for certiorari arising from Federal Circuit decisions on the patent-eligibility of software; the Court denied cert in the two cases in which the Federal Circuit held the software patents to fail Section 101, and granted cert only in *Ultramercial*, where as noted above, the Federal Circuit had upheld the software patent under Section 101.)⁴² A few months later, when the Federal Circuit decided *Ultramercial* for the third time, it finally held the patent ineligible under Section 101, deciding that it covered only the abstract idea of using advertisements as currency, e.g., showing an ad before delivering free content.⁴³

Indeed, in the roughly six months between *Alice*’s issuance on June 19, 2014 and December 15, 2014, courts deciding Section 101 challenges to software patents appeared to be invalidating the patents at nearly an 80% clip. Among the

software patents held invalid under Section 101 following *Alice* are those directed to:

- Guaranteeing performance of an online transaction (*buySAFE v. Google, Inc.*)⁴⁴
- Capturing color and spatial properties of an imaging device (*Digitech*)⁴⁵
- Generating a single record of multiple services for accounting (*Amdocs*)⁴⁶
- Facilitating marketing dialogs (*OpenText*)⁴⁷
- Receiving transaction amount data, applying a formula, and making deposits into different accounts per the formula (*Every Penny Counts*)⁴⁸
- Converting loyalty points among vendors (*Loyalty Conv. Sys.*)⁴⁹
- Paying down a mortgage early when funds are available (*CMG Fin. Servs.*)⁵⁰
- Automating lip-synching and facial expressions of 3D characters (*McRo*)⁵¹

Three district courts upheld software patents under Section 101 during this time period. One case involved a patent on software used to create a tool usable to form sheet metal into different parts, primarily for car parts (*AutoForm Eng’g*).⁵² Another involved remotely monitoring data associated with an internet session and controlling network access (*Helios Software*).⁵³ And a third case upheld four patents covering methods of encoding and decoding data in accordance with a form of error correction code (*CalTech*).⁵⁴

A Ray of Hope for Software Patents? The Federal Circuit’s *DDR Holdings* Decision

After a rocky six months, software patent holders took heart from a December 5, 2014 Federal Circuit decision that upheld a software patent over a Section 101 challenge, albeit in a 2-1 decision over a strong dissent. In *DDR Holdings, LLC v. Hotels.com, L.P.*, the Court considered the patentability of U.S. Patent No. 7,818,399, which covered systems and methods for generating composite webpages that combined visual elements of a “host” website with content from a third-party merchant.⁵⁵

The ‘399 patent aimed to solve problems experienced by host websites that displayed third-party ads. Website visitors, attracted by the ads, would click on them and be transported away from the host website to the website of the third-party advertiser. The patent’s solution was to let the website visitor “be in two places at the same time,” as the court described it. With the patented system, when a website visitor clicked a third-party ad, the system created a composite website that

displayed product information from the third-party merchant, but kept the “look and feel” of the host website.⁵⁶

The panel majority found this patentable under Section 101. Acknowledging that the patent did address a business challenge (retaining website visitors), the majority emphasized that the challenge was not a “fundamental economic or longstanding commercial practice” but rather a challenge particular to the internet. As the majority saw it, the inventors had not begun with a pre-internet business practice and patented its performance on the internet, but rather, had patented the solution to a problem uniquely existing on the internet.⁵⁷

Yet, that arguably also had been the case in *Ultramercial*, decided a few weeks earlier, wherein the Federal Circuit finally accepted that *Ultramercial*’s patent couldn’t satisfy Section 101, post-*Alice*. The *DDR Holdings* majority explained why it found the ‘399 patent a stronger candidate under Section 101. Whereas *Ultramercial*’s patent covered only the idea of offering media content in exchange for viewing an advertisement—an “abstract business practice” that wasn’t patentable merely by being performed on the internet—in contrast, the ‘399 patent in *DDR Holdings* achieved a “result that overrides the routine and conventional sequence of events ordinarily triggered by the click of a hyperlink.”

Whereas before the ‘399 patent, a click on a third-party ad transported the user off the host website, the systems of the ‘399 patent permitted a different outcome, one in which the user no longer left the host website. To the majority, this was enough to be patent-eligible under Section 101.⁵⁸

Senior Circuit Judge Haldane Mayer, in dissent, bought none of it. He made clear his distaste for the entire premise of the ‘399 patent, criticizing it as “duping” and “confusing customers,” “long on obfuscation but short on substance,” and “border[ing] on the comical.”⁵⁹ More substantively, Judge Mayer primarily disagreed with the majority because he found the ‘399 patent insufficiently technical.

Premising his dissent on his view that *Alice* introduced a “technical arts” test for patentability,⁶⁰ Judge Mayer emphasized that the ‘399 patent offered no new computer technology, but rather, relied on conventional technology; it offered only an entrepreneurial solution to a problem rather than a technological solution. Believing that “*Alice* made clear that claims untethered to any advance in science or technology do not pass muster under section 101,” he found the ‘399 patent insufficiently technical to be patent eligible.⁶¹

The Past Six Months in Perspective

The Supreme Court’s decision in *Alice* and its decision to G-V-R *Ultramercial* for a second time, while declining to hear contemporaneously pending appeals from cases in which the Federal Circuit struck down software patents under Section 101, are immensely significant.



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First, the ease with which the *Alice* Court swept aside the issues that had so troubled the Federal Circuit sounded a wake up call to those who considered it murky or difficult to decide a software patent's eligibility under Section 101. Post-*Alice*, it is now clear that software inventions cannot rest on their computer-implementation alone to be patent-eligible.⁶²

Second, *Alice* seems to have served as a tipping point for lower courts. Whereas in the two years before *Alice*, software patents encountered fewer Section 101 challenges in litigation and survived them roughly a third of the time, this rate plummeted to 20% in the six months post-*Alice*, and the frequency of such challenges increased markedly.⁶³

Third, *Alice* caused the Patent Office to revamp its procedures for examining software patents. Six days after the decision, the Patent Office issued its examiners "Preliminary Examination Instructions" for inventions involving abstract ideas, particularly those implemented on computers.⁶⁴ The Patent Office subsequently supplemented those June 25 Instructions with additional guidance on December 16, 2014, and even this latest guidance is expected to be further revised after public comment closes in mid-March 2015.⁶⁵ The Office further took steps to halt the issuance of patents on applications that already had been examined and received Notices of Allowance.⁶⁶


For software developers deciding whether to protect their software invention through patents versus copyright and trade secrets, the events of the past six months may cause them to focus more closely on the latter two forms of intellectual property. Yet, they also should consider whether the software invention relates to a business method or, in contrast, to what may be termed industrial software. Industrial software patents, such as those upheld in *AutoForm Eng'g*⁶⁷ and *Diehr* may be better equipped to pass muster under *Bilski* and *Alice*.⁶⁸

Patent litigators on the plaintiff's side likely will re-evaluate their confidence in the validity of software patents issued by the Patent Office pre-*Alice*, as the Office's determination that those patents satisfied Section 101 was made under a far more permissive framework than that now being applied by courts. Litigators deciding whether to take on a contingent fee representation involving assertion of a software patent will scrutinize the patent even more closely than usual. In addition to evaluating the patent under *Alice*'s two-step framework, litigators will compare the patent in question to those at issue in *Benson*, *Flook*, *Diehr*, *Bilski* and *Alice*.

Indeed, as one court has observed, "so far, the two-part test for identifying an abstract idea appears to be of limited utility, while comparisons to previously adjudicated patents—or more precisely, to past cases' characterizations of those patents—have done the heavy lifting."⁶⁹ Plaintiffs' counsel also may consider the benefits of teeing up the Section 101 issue early, rather than urging the court to wait to decide it until after the patent's claims have been interpreted by the court later in the suit.

Lastly, plaintiffs' counsel should study the numerous decisions invalidating software patents post-*Alice* to identify arguments that are not being found persuasive.

For defendants' counsel, considerations include whether to challenge a software patent under Section 101 in court, or, if defending against certain software patents covering financial products or services, to file a Covered Business Method Review proceeding in the Patent Office,⁷⁰ or both (though certain estoppel provisions⁷¹ apply). Timing is a consideration—courts increasingly are demonstrating amenability to such challenges as early as the pleading stage, and a diminishing number appear to be deferring such challenges until after claim interpretation.

Post-*Alice*, software remains patentable as a general principle, but the bar has been raised significantly. Business method patents appear to suffer the most under the new framework, while industrial software patents may be less affected. The next six-to-twelve months may prove just as illuminating as the past six months. The Federal Circuit will begin hearing appeals of the trial court decisions rejecting software patents under Section 101 and may resuscitate some of the patents that currently stand rejected. This area of the law merits close attention going forward. 

¹ 134 S.Ct. 2347.

² *Id.* at 2359-60.

³ Martin Campbell-Kelly, "Not All Bad: An Historical Perspective on Software Patents," 11 *Mich. Telecomm. Tech. L. Rev.* 191, 210 (2005).

⁴ *Id.*

⁵ 35 U.S.C. §101.

⁶ *Diamond v. Chakrabarty*, 447 U.S. 303, 309 (noting that the most recent codification of the patent laws in 1952 left Jefferson's language largely intact, merely using "process" to replace "art" in Jefferson's original version).

⁷ *Bilski v. Kappos*, 130 S.Ct. 3218, 3245 (2010) (Stevens, J., dissenting).

⁸ *Alice*, 134 S.Ct. at 2354 (noting that the Court has applied this exception to patentable subject matter since its 1853 decision in *LeRoy v. Tatham*, 14 L.Ed. 367).

⁹ *Chakrabarty*, 447 U.S. at 309.

¹⁰ Martin Campbell-Kelly, 11 *Mich. Telecomm. Tech. L. Rev.* at 212-13 (recounting Informatics' efforts to patent the Mark IV); see also *id.* at 213 n.113 (noting that Informatics did succeed in patenting the Mark IV in Canada and the United Kingdom).

¹¹ *Id.* at 214 (describing the Patent Office's August 1966 advisory).

¹² Examination of Patent Applications on Computer Programs, Notice of Issuance of Guidelines, 33 FR 15609-10 (Oct. 22, 1968).

¹³ Examination of Patent Applications on Computer Programs, Notice of Rescission of Guidelines, 34 FR 15724 (Oct. 10, 1969) (noting that the rescission was spurred by the decision of the Court of Customs and Patent Appeals in *In re Prater*).

¹⁴ U.S. Patent No. 3,533,086 at Col. 1, line 64 - Col. 2, line 5. See also Martin Campbell-Kelly, 11 *Mich. Telecomm. Tech. L. Rev.* at 214 (describing the '086 patent as "one of the earliest software product patents granted" and opining that the invention "was a tour de force of computer programming that even today is an impressive piece of coding").

¹⁵ *Gottschalk v. Benson*, 93 S.Ct. 253, 254, 257 (1972).

¹⁶ *Parker v. Flook*, 98 S.Ct. 2522, 2524, 2529 (1978) (holding unpatentable a process for using a computer to update an alarm limit on a variable measured during chemical processing).

¹⁷ *Diamond v. Diehr*, 101 S.Ct. 1048 (1981).

¹⁸ *Diehr*, 101 S.Ct. at 1067-68 (Stevens, J., dissenting).

¹⁹ The Federal Circuit, as the court is known, was created by merging the U.S. Court of Customs and Patent Appeals with the appellate division of the U.S. Court of Claims.

²⁰ *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*, 149 F.3d 1368 (Fed. Cir. 1998).

²¹ *Id.* at 1375-77 (upholding the validity of U.S. Patent No. 5,193,056 "Data Processing System for Hub and Spoke Financial Services Configuration").

²² See John R. Allison and Emerson H. Tiller, "The Business Method Patent Myth," 18 *Berkeley Tech. L. J.* 987, 991 (2003) (noting that the number of patents issued by the Patent Office within class 705 "Data processing: financial, business practice, management, or cost/price determination" rose from 469 in 1998 to 1,006 by 2000); see also Michael J. Meurer, "Business Method Patents and Patent Floods," 8 *Wash. U. J. L. & Policy* 309, 313 (2002) ("The *State Street* decision set

off a flood of e-commerce patents.”).

²³ See *In re Bilski*, 545 F.3d 943, 959-60 (Fed. Cir. 2008). *State Street* had held that “the transformation of data, representing discrete dollar amounts, by a machine through a series of mathematical calculations into a final share price” satisfied Section 101 “because it produces a useful, concrete and tangible result.” *State Street*, 149 F.3d at 1373. In *Bilski*, the Federal Circuit withdrew the “useful, concrete and tangible result” test in favor of a new “machine or transformation” test. *Bilski*, 545 F.3d at 959-60. The Federal Circuit in *Bilski* did reaffirm that business method patents were not *per se* unpatentable. *Id.* at 960.

²⁴ *Bilski v. Kappos*, 130 S.Ct. 3218, 3226-27 (2010) (affirming the Federal Circuit’s decision that the patent in suit did not satisfy Section 101, but holding that the Federal Circuit “incorrectly concluded that this Court has endorsed the machine-or-transformation test as the exclusive test”).

²⁵ *Id.* at 3228-29 (business methods not *per se* unpatentable), 3231 (Bilski’s application unpatentable as an attempt to patent hedging as a concept and mathematical formula).

²⁶ *Ultramercial, Inc. v. Hulu, LLC*, 657 F.3d 1323 (Fed. Cir. 2011).

²⁷ *Wildtangent, Inc. v. Ultramercial, LLC*, 132 S.Ct. 2431 (2012) (remanding for consideration in view of *Mayo Collab. Servs. v. Prometheus Labs., Inc.*, 132 S.Ct. 1289 (2012)).

²⁸ *Ultramercial, Inc. v. Hulu, LLC*, 722 F.3d 1335, 1349-54 (Fed. Cir. 2013) (concluding that “the ‘545 patent does not claim a mathematical algorithm, a series of purely mental steps, or any similarly abstract concept. It claims a particular method for collecting revenue from the distribution of media products over the Internet [A]s a practical application of the general concept of advertising as currency and an improvement to prior art technology, the claimed invention is not so manifestly abstract as to override the statutory language of section 101.”) (cites and quotes omitted).

²⁹ *Alice*, 134 S.Ct. 2347, 2352 (June 19, 2014).

³⁰ U.S. Patent No. 5,970,479 issued on Oct. 19, 1999, and U.S. Patent No. 7,725,375 issued on May 25, 2010.

³¹ *Alice*, 134 S.Ct. at 2353 (tracing the procedural history of the case).

³² *CLS Bank Int’l v. Alice Corp. Pty. Ltd.*, 685 F.3d 1341, 1352, 1356 (Fed. Cir. 2012).

³³ *CLS Bank Int’l v. Alice Corp. Pty. Ltd.*, 717 F.3d 1269 (Fed. Cir. 2013) (*en banc*). Specifically, a majority of the full Federal Circuit held that the claims of the patents that were directed to methods and to computer-readable media failed to satisfy Section 101, while as to the system claims, the full court split evenly and thus affirmed the trial court’s holding of invalidity as to those claims as well. *Id.*

³⁴ *Id.* at 1273 (plurality opinion authored by Judge Lourie and joined by four other judges, deciding all claims of the patents ineligible under Section 101); *id.* at 1292, 1311 (opinion by Chief Judge Rader, concurring in part and dissenting in part, viewing the system claims as satisfying Section 101 because they involved, not a disembodied abstract idea, but an idea “integrated into a system utilizing machines”); *id.* at 1313 (opinion by Judge Moore, dissenting in part, arguing that the system claims satisfied Section 101); *id.* at 1321 (opinion by Judge Newman, concurring in part and dissenting in part, arguing that all claims—system, method, and computer readable media—satisfied Section 101); *id.* at 1327 (dissenting opinion by Judges Linn and O’Malley, arguing that all claims were patent-eligible under Section 101).

³⁵ *Alice*, 134 S.Ct. at 2354 (citations and quotes omitted).

³⁶ *Alice*, 134 S.Ct. at 2355 (citations and quotes omitted). The Court previously had introduced this two-step framework in *Mayo Collab. Servs. v. Prometheus Labs., Inc.*, 132 S.Ct. 1289, 1294, 1296-97 (2012), which concerned the eligibility under Section 101 of patents for medical diagnostic tests. Yet even this two-step framework seems structurally less than solid, and it would not be surprising if the Court reworks this formulation in future cases. As one trial court observed, “Describing this as a two-step test may overstate the number of steps involved. If the claim is not ‘directed’ to a patent-ineligible concept, then the test stops at step one. If the claim is so directed, but we find in step two that the claim contains an ‘inventive concept’ that ‘transforms’ the nature of the claim into something patent eligible, then it seems that there was a categorization error in finding the claim . . . ‘directed to an abstract idea’ in step one.” *McRo, Inc. v. Activision Publ’g, Inc.*, 2014 WL 4759953, *4 (C.D. Cal. Sept. 22, 2014).

³⁷ *Alice*, 134 S.Ct. at 2355-57.

³⁸ *Id.* at 2357-60.

³⁹ *Id.* at 2358 (citations and quotations omitted).

⁴⁰ *Id.* at 2359.

⁴¹ *Wildtangent, Inc. v. Ultramercial, LLC*, 134 S.Ct. 2870 (June 30, 2014).

⁴² See *Bancorp Services, L.L.C. v. Sun Life Assurance Co. of Canada (U.S.)*, 134 S.Ct. 2870 (June 30, 2014) (denying cert in a case where the Federal Circuit invalidated under Section 101 a patent for administering and tracking the value of life insurance policies); *Accenture Global Servs., GmbH v. Guidewire Software, Inc.*, 134 S.Ct. 2871 (June 30, 2014) (denying cert in a case where the Federal Circuit invalidated under Section 101 a patent for using a computer system in connection with insurance claim processing). One trial court noted, “Conspicuously, the Supreme Court vacated the only Federal Circuit opinion, *Ultramercial*, upholding a software patent and declined certiorari over the two actions, *Bancorp* and *Accenture*, that invalidate software patents.” See *Every Penny Counts, Inc. v. Wells Fargo Bank, N.A.*, 2014 WL 4540319, *4 n.4 (M.D. Fla. Sept. 11, 2014).

⁴³ *Ultramercial, Inc. v. Hulu, LLC*, 772 F.3d 709, 715-16 (Fed. Cir. Nov. 14, 2014).

⁴⁴ *buySAFE, Inc. v. Google, Inc.*, 765 F.3d 1350, 1355 (Fed. Cir. Sept. 3, 2014)

(deciding that the patent’s claims “are squarely about creating a contractual relationship—a ‘transaction performance guaranty’—that is beyond question of ancient lineage [and] thus are directed to an abstract idea,” that “the claims’ invocation of computers adds no inventive concept,” and thus “with the approach to this kind of section 101 issue clarified by *Alice*, it is a straightforward matter to conclude that the claims in this case are invalid”).

⁴⁵ *Digitech Image Technologies, LLC v. Electronics for Imaging, Inc.*, 758 F.3d 1344

(Fed. Cir. July 11, 2014).

⁴⁶ *Amdocs (Israel) Ltd. v. Openet Telecom, Inc.*, ___ F.Supp.3d ___, 2014 WL 5430956, *5-11 (E.D. Va. Oct. 24, 2014) (invalidating the claims of four patents).

⁴⁷ *Open Text S.A. v. Alfreco Software Ltd.*, 2014 WL 4684429, *5 (N.D. Cal. Sept. 19, 2014) (“The asserted claims in the ‘372 and ‘007 patents . . . fail to transform the abstract idea into a patent-eligible invention. The asserted claims in both patents implement the basic marketing scheme on a generic computer system without any meaningful limitations.”).

⁴⁸ *Every Penny Counts*, 2014 WL 4540319 at *5 (invalidating a method patent because it claims “an abstract idea that is implemented by well-understood, routine, conventional activities previously known to the industry” and invalidating a system patent because it “merely implements—on a generic, unspecified computer—the [method patent’s] unpatentable method”).

⁴⁹ *Loyalty Conv. Sys. Corp. v. Am. Airlines, Inc.*, ___ F.Supp.2d ___, 2014 WL 4364848, *6-14 (E.D. Tex. Sept. 3, 2014).

⁵⁰ *CMG Fin. Servs., Inc. v. Pacific Trust Bank*, F.S.B., ___ F.Supp.2d ___, 2014 WL 4922349, *17-19 (C.D. Cal. Aug. 29, 2014).

⁵¹ *McRo, Inc. v. Activision Publ’g, Inc.*, 2014 WL 4759953, *4 (C.D. Cal. Sept. 22, 2014).

⁵² *AutoForm Eng’g GmbH v. Eng’g Tech. Assocs., Inc.*, 2014 WL 4385855, *3-4 (E.D. Mich. Sept. 5, 2014).

⁵³ *Helios Software, LLC v. SpectorSoft Corp.*, 2014 WL 4796111, *15-17 (D. Del. Sept. 18, 2014) (“Although ‘remotely monitoring data associated with an Internet session’ or ‘controlling network access’ may be principles fundamental to the ubiquitous use of the Internet or computers generally, [defendant] has provided no support for that position. As such, the Court cannot agree with [defendant] that the patents-in-suit are drawn to an abstract idea.”).

⁵⁴ *California Institute of Technology v. Hughes Communications Inc.*, ___ F.Supp.3d ___, 2014 WL 5661290, *14-20 (C.D. Cal. Nov. 3, 2014). The Court stated:

“Caltech’s patents recite methods of encoding and decoding data in accordance with an IRA [irregular repeat and accumulate] code. At step one, this Court determines that all asserted claims are directed to the abstract idea of encoding and decoding data for the purpose of achieving error correction. Nonetheless, at step two, this Court finds that the claims contain elements that provide an inventive concept. When claims provide a specific computing solution for a computing problem, these claims should generally be patentable, even if their novel elements are mathematical algorithms. That is the case with all of Caltech’s asserted claims, which the Court has concluded are patentable.” *Id.* at *14.

⁵⁵ *DDR Holdings, LLC v. Hotels.com, L.P.*, ___ F.3d ___, 2014 WL 6845152, *1 (Fed. Cir. Dec. 5, 2014). Two patents had been asserted successfully at trial, and were taken up on appeal by the Federal Circuit. Of the two patents, one (the “‘572 patent”) was held invalid over prior art by the panel, which thus did not reach the Section 101 issue as to that patent, but considered Section 101 only as to the ‘399 patent.

⁵⁶ *Id.*

⁵⁷ *Id.* at *10.

⁵⁸ *Id.* at *12.

⁵⁹ *Id.* at *17 (Mayer, J., dissenting).

⁶⁰ Judge Mayer has articulated this view multiple times post-*Alice*. See, e.g., *Ultramercial*, 772 F.3d at 717 (Mayer, J., concurring); *IP Engine, Inc. v. AOL Inc.*, 576 Fed. Appx. 982, 992 (Fed. Cir. Aug. 15, 2014) (Mayer, J., concurring).

⁶¹ *DDR Holdings*, 2014 WL 6845152 at *18-19 (Mayer, J., dissenting).

⁶² “*Alice* did categorically establish a clear rule that had previously been subject to debate: mere recitation of a generic computer cannot transform a patent-ineligible abstract idea into a patent-eligible invention.” *McRo*, 2014 WL 4759953 at *4.

⁶³ My colleague Chris R. Johnson and I searched for Section 101 cases involving software patents decided after the Supreme Court’s March 20, 2012 decision in *Mayo Collab. Servs. v. Prometheus Labs., Inc.*, 132 S.Ct. 1289 but before the Court’s *Alice* decision. Of 30 decisions, we found nine upholding the patents, 19 deeming them invalid under Section 101, and two decisions upholding some claims of the patents but invalidating others. For the six months post-*Alice*, we reviewed 20 decisions, 4 of which upheld the patents under Section 101, the remainder of which invalidated them.

⁶⁴ U.S. Patent and Trademark Office, “Preliminary Examination Instructions in view of the Supreme Court Decision in *Alice Corporation Pty. Ltd. v. CLS Bank International, et al.*,” available at www.uspto.gov/patents/announce/alice_pec_25jun2014.pdf (last visited Jan. 5, 2015).

⁶⁵ 2014 Interim Guidance on Patent Subject Matter Eligibility, 79 FR 74618-33 (Dec. 16, 2014).

⁶⁶ See Update on USPTO’s Implementation of *Alice v. CLS Bank* (Aug. 4, 2014), available at http://www.uspto.gov/blog/director/entry/update_on_uspto_s_implementation (last visited Jan. 7, 2015).

⁶⁷ *AutoForm Eng’g GmbH*, 2014 WL 4385855 (E.D. Mich. Sept. 5, 2014).

⁶⁸ Cf. Bernard Chao, “Finding the Point of Novelty in Software Patents,” 28 *Berkeley Tech. L.J.* 1217, 1222-23, 1226-28 (2013) (distinguishing business method patents from industrial software patents, noting the “intense criticism” often given to business method patents, and opining that “from a policy perspective [industrial software patents] are indistinguishable from other industrial patents that are not implemented through software and . . . have not been subject to the same criticism as their business method cousins”).

⁶⁹ *McRo*, 2014 WL 4759953 at *5.

⁷⁰ The CBM Review process is available for patents having claims directed to “financial products or services” that are not directed to “technological inventions.” See for example the Patent Office’s discussion of its CBM Review program at http://www.uspto.gov/aia_implementation/faqs_covered_business_method.jsp (last visited Jan. 7, 2015).

⁷¹ A defendant in a lawsuit who also petitions the Patent Office for CBM Review is estopped from raising in the patent suit any grounds for invalidity that are (i) actually raised and (ii) subject to a final decision in the CBM Review proceeding. See *id.*



Test No. 76

This self-study activity has been approved for Minimum Continuing Legal Education (MCLE) credit by the San Fernando Valley Bar Association (SFVBA) in the amount of 1 hour. SFVBA certifies that this activity conforms to the standards for approved education activities prescribed by the rules and regulations of the State Bar of California governing minimum continuing legal education.

1. Appeals from patent cases tried in California federal courts are heard by the Court of Appeals for the Federal Circuit in Washington, D.C.
 True False
2. Section 101 of the Patent Act defines the categories of inventions for which a patent may be granted.
 True False
3. A defendant sued for patent infringement must wait until the summary judgment stage of the case before challenging the patentability of the patent-in-suit under 35 U.S.C. 101.
 True False
4. Covered Business Method (CBM) Review refers to the process used in federal courts to challenge the patentability of a software patent.
 True False
5. In *Alice Corp. v. CLS Bank*, the U.S. Supreme Court held that all software patents are *per se* unpatentable.
 True False
6. In the six months following the U.S. Supreme Court's decision in *Alice Corp.*, about half the software patents challenged under 35 U.S.C. 101 were held invalid by courts.
 True False
7. The three exceptions to patent-eligibility—laws of nature, natural phenomena, and abstract ideas—were judicially created.
 True False
8. Copyright law and trade secret law also may afford protection to a software invention.
 True False
9. The six months following the Supreme Court's decision in *Alice* saw an increase in the frequency with which Section 101 challenges were asserted against software patents in litigation.
 True False
10. *State Street Bank* is a decision by the Court of Appeals for the Federal Circuit that held that business method patents were not *per se* unpatentable.
 True False
11. One result of the Federal Circuit's abrogation of the holding of *State Street Bank* is that business method patents are *per se* unpatentable.
 True False
12. The machine or transformation test has been confirmed by the Supreme Court as the sole test for patent-eligibility under Section 101.
 True False
13. The Supreme Court in *Alice* applied a two-step framework for evaluating patent-eligibility under Section 101 of the Patent Act.
 True False
14. Under *Alice*, a patent application that takes a long-standing business practice and implements it on a computer is unlikely to satisfy Section 101 of the Patent Act.
 True False
15. Since the Supreme Court decided *Alice*, the only decisions that have upheld software patents over Section 101 challenges have been decided by district courts, not the Court of Appeals for the Federal Circuit.
 True False
16. The Supreme Court's decision in *Alice* has not affected the Patent Office's processes for examining software patents.
 True False
17. The Supreme Court's decisions in *Benson*, *Flook* and *Diehr* are no longer good law after *Alice*.
 True False
18. Before *Alice*, the Supreme Court had never before held a software patent ineligible for patenting under Section 101.
 True False
19. Software patents were granted by the Patent Office before the Federal Circuit's 1998 decision in *State Street Bank*.
 True False
20. At least one Federal Circuit judge believes that the Supreme Court's *Alice* decision created a technical arts test for patentability.
 True False

MCLE Answer Sheet No. 76

INSTRUCTIONS:

1. Accurately complete this form.
2. Study the MCLE article in this issue.
3. Answer the test questions by marking the appropriate boxes below.
4. Mail this form and the \$20 testing fee for SFVBA members (or \$30 for non-SFVBA members) to:

San Fernando Valley Bar Association
5567 Reseda Boulevard, Suite 200
Tarzana, CA 91356

METHOD OF PAYMENT:

- Check or money order payable to "SFVBA"
 Please charge my credit card for \$_____.

Credit Card Number _____ Exp. Date _____

Authorized Signature _____

5. Make a copy of this completed form for your records.
6. Correct answers and a CLE certificate will be mailed to you within 2 weeks. If you have any questions, please contact our office at (818) 227-0490, ext. 105.

Name _____

Law Firm/Organization _____

Address _____

City _____

State/Zip _____

Email _____

Phone _____

State Bar No. _____

ANSWERS:

Mark your answers by checking the appropriate box. Each question only has one answer.

1. True False

2. True False

3. True False

4. True False

5. True False

6. True False

7. True False

8. True False

9. True False

10. True False

11. True False

12. True False

13. True False

14. True False

15. True False

16. True False

17. True False

18. True False

19. True False

20. True False