Bilski v. *Kappos:* New Guidance for Patentable Subject Matter

On June 28, 2010, the Supreme Court of the United States issued its decision in *Bilski* v. *Kappos*, which addresses the proper analysis for determining whether a process or method claim is directed to patentable subject matter under 35 U.S.C. § 101. The patent community had long-awaited the Court's views on the Federal Circuit's prior *en banc* decision in the case, in which that court held that the "machine-or-transformation" test was the sole method for assessing the patentability of method claims. All nine members of the Court agreed that Bilski's claims were not directed to patentable subject matter, with a five member majority (Chief Justice Roberts and Justices Scalia, Kennedy, Thomas, and Alito) concluding that the claims impermissibly attempted to claim an abstract idea. While the Court noted that the Federal Circuit's machine-or-transformation test is a useful and helpful tool in assessing patentability, it rejected that test as the ***sole*** means for determining whether method claims are drawn to patentable subject matter. Although the four other justices would have ruled that all claims for methods of doing business are *per se* unpatentable, the majority declined go that far.

Bilski's patent application sought to claim a method for buyers and sellers of energy market commodities to protect, or "hedge," against the risk of price changes. Slip. Op. at 2. The *en banc* Federal Circuit rejected the claims for failing to meet the machine-or-transformation test, which the court determined was the sole test for determining patent eligibility of a process under § 101. To satisfy this test, a process must either (1) be tied to a particular machine or apparatus; or (2) transform a particular article into a different state or thing. *In re Bilski*, 545 F.3d 943, 954 (Fed. Cir. 2008).

Writing for the majority, Justice Kennedy first looked to the language of the statute:

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

35 U.S.C. § 101. Thus, four independent categories of new and useful inventions or discoveries are eligible for patent protection: processes, machines, manufactures, and compositions

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of matter. Slip. Op. at 4. While not expressly required by the statute, there are three long-established, specific exceptions to the categories of patent-eligible subject matter: laws of nature, physical phenomena, and abstract ideas. *Id.* at 5. According to the Court, one cannot patent a law of nature, physical phenomenon, or abstract idea because such a claim would not satisfy the "new and useful" requirement of § 101. Because the claims of the Bilski application were directed to a process, the Court also considered another provision of the patent statute that defines "process" as a "process, art or method, and includes a new use of a known process, machine, manufacture, composition of matter, or material." 35 U.S.C. § 100(b).

The Court evaluated two categorical limitations on "process" patent claims, either of which would bar the claims in Bilski's application—the machine-or-transformation test as set forth by the Federal Circuit and an exclusion of all claims directed to "business methods." The Court rejected that the machine-or-transformation test is the sole test for determining patent eligibility for process claims under § 101 as the ordinary meaning of the statutory term "process" does not require that it be tied to a machine or to transform an article. Slip. Op. at 7. But the Court did state that "the machine-or-transformation test is a useful and important clue, an investigative tool, for determining whether some claimed inventions are processes under § 101." *Id.* at 8. Some early commentators characterized the Court's decision as rejecting the machine-or-transformation test, but that is not correct. Post-*Bilski* the machine-or-transformation test continues to be an important test in assessing patentability, but it is not the *only* test. While a method claim that satisfies the machine-or-transformation test is likely patentable, failure to meet the test does not necessarily mean that the claim is directed to unpatentable subject matter.

While accepting that the machine-or-transformation test may provide a sufficient basis for evaluating processes similar to those from the Industrial Age, Justice Kennedy, joined by all the members of the majority except Justice Scalia, questioned whether the test should be the sole criterion for determining the patentability of inventions in the Information Age. The Court noted that exclusive reliance on the machine-or-transformation test could call into question the patentability of such technologies as computer software, medical diagnostic techniques, and inventions employing programming, data compression, or manipulation of digital signals. *Id.* at 9. Justice Kennedy did not comment on whether such modern technologies should be afforded patent protection, but admitted that new technologies may call for new inquiries. While patent law "faces a great challenge in striking the balance between protecting inventors and not granting monopolies over procedures that others would discover by independent, creative application of general principles," Justice Kennedy offered no position on where that balance should be struck. *Id.* at 10.

The majority next considered whether "business methods" as a whole should be excluded from patent protection, but was unwilling to categorically deny patent eligibility for methods of conducting business. The Court noted that "method" is within the § 100(b)'s definition of process, and there is nothing to indicate that the ordinary meaning of "method" or the statutory definition excludes all methods of doing business. The Court further observed that there is no accepted definition for what constitutes a "business method," so it is not clear what the scope of such a prohibition would entail. *Id.* The Court also relied on § 273 of the Patent Act, which Congress amended in 1999 to provide a defense of prior use to a party accused of infringing a claim directed to a "method of doing or conducting business." 35 U.S.C. § 273. Thus, according to the Court, the patent statute contemplates the existence of business method patents, and to exclude all business methods from patentability would render § 273 meaningless.

Justice Kennedy, again joined by all the justices in the majority except Justice Scalia, acknowledged the special problems—particularly vagueness and questionable validity—that claims directed to business methods present to creative endeavor and dynamic change. Slip. Op. at 12. He noted that the Court's precedents on the unpatentability

of abstract ideas provide "useful tools" in crafting a limiting principle for reviewing patents directed to methods of doing business. Justice Kennedy then invited the lower courts to craft such a limitation: "Indeed, if the Court of Appeals were to succeed in defining a narrower category or class of patent applications that claim to instruct how business should be conducted, and then rule that the category is unpatentable because, for instance, it represents an attempt to patent abstract ideas, this conclusion might well be in accord with controlling precedent." *Id.*

After rejecting the exclusive machine-or-transformation test set forth by the Federal Circuit and a broad exclusion of all business method claims, the Court analyzed Bilski's claims themselves. The Court looked to its own precedent in *Gottschalk* v. *Benson*, 409 U.S. 63 (1972), *Parker* v. *Flook*, 437 U.S. 584 (1978), and *Diamond* v. *Diehr*, 450 U.S. 175 (1981), and concluded that Bilski's claims to hedging risk in energy markets were impermissible attempts to patent abstract ideas. Slip. Op. at 13.

According to the Court, *Benson* held that mathematical formulas or algorithms may not be patented. And *Flook* established that one may not avoid the ban on patenting abstract ideas by limiting the use of a formula to a specific technological environment or merely adding insignificant post-solution activity. Under *Diehr*, however, "an *application* of a law of nature or mathematical formula to a known structure or process may well be deserving of patent protection." *Id.* at 14. The Court concluded that Bilski's claims to hedging were unpatentable abstract ideas similar to the algorithms in *Benson* and *Flook*, although the Court did not provide much additional guidance as to how to identify "abstract ideas" beyond the three cited cases.

In a lengthy opinion Justice Stevens, joined by Justices Ginsburg, Breyer, and Sotomayor, concurred in the Court's judgment that Bilski's claims were directed to unpatentable subject matter, but he disagreed strongly with the majority's determination that business method claims are not *per se* unpatentable. Justice Stevens agreed with the majority that while the machine-or-transformation test is generally a reliable indicator of patentability, it is not the exclusive test. Slip. Op. at 1 (Stevens, J. concurring). Reviewing pre-Constitution English patent practices, as well as the history and application of US patent law, however, Justice Stevens concluded that the term "process" does indeed have a distinctive meaning in patent law and that claims directed to a series of steps for conducting business are not patentable. *Id.* at 1-3. According to Justice Stevens, the statute's use of the term "process" was intended to encompass the same scope as the historical phrase "useful arts," which did not include fields such as business and finance. *Id.* at 15-34. Thus, methods of doing business are not patentable subject matter. *Id.* The concurrence does not attempt to define exactly what a "business method" claim is, however, so it is unclear how broad or narrow this new exception to patentability would have been had Justice Stevens' view prevailed.

Justice Breyer also concurred in the Court's judgment, but he wrote separately to highlight four points of agreement he saw between the majority opinion and Justice Stevens' concurrence. First, while the text is broad, there are limits to § 101. Slip. Op. at 2 (Breyer, J. concurring). Second, the machine-or-transformation test has historically been a useful tool in analyzing patentability. *Id.* Third, while the machine-or-transformation test is an "important example" of one way of determining patentability, it is not the exclusive test. *Id.* at 3. And fourth, the Federal Circuit's earlier "useful, concrete, and tangible result" (which the *en banc* court itself rejected in *Bilski*) is not an adequate means for determining patentable subject matter. *Id.*

We note several preliminary observations with respect to the Court's decision. First, as a practical matter, the analysis of whether a method is a patentable process is likely to continue to rely heavily on whether the method satisfies the machine-or-transformation test. Although the Court did not explicitly hold that satisfying the machine-or-transformation test is sufficient to conclude that the method is a patentable process, all the justices endorsed the test as a critical clue and a useful tool in the analysis. Indeed, on the same day that *Bilski* was decided, the US Patent and Trademark Office

issued interim guidance to patent examiners stating that a method claim that meets the machine-or-transformation test is likely patent-eligible unless there is a clear indication that the method is directed to an abstract idea. *See* http://www.uspto.gov/patents/law/exam/bilski_guidance_28jun2010.pdf. It is likely the rare situation, if ever, that a method can meet the machine-or-transformation test but nevertheless be directed to an abstract idea.

Second, the Court did not delineate what would be required for a method claim that does not satisfy the machine-or-transformation test to be considered patentable. Although the Court did not go so far as to hold that a method is a patentable process as long as it is not directed to an abstract idea, it will be interesting to see whether lower courts will require something beyond lack of abstractness to find that a method is a patentable process, especially given the Court's observation that the "laws of nature, physical phenomenon, and abstract ideas" exceptions to §101 are concerned with the "new and useful" requirement of § 101 instead of whether a series of steps are a patentable process. This is an issue that is likely to be the subject of additional litigation in the lower courts, but it is worth noting that the Patent Office's preliminary guidance to its examiners suggests that as long as a method is not abstract then it is directed to a patentable process.[1]

Third, the majority's opinion that claims directed to a method of conducting business fall within the ambit of patentable processes is not as emphatic as may appear on first glance. At least four members of the majority (who presumably would join with the four justices comprising the Stevens concurrence) are willing to entertain a test formulated by the lower court that defines a narrower category of patent claims directed to business methods as unpatentable because they are directed to an abstract idea or are otherwise inconsistent with some other limitation of the statutory text. It remains to be seen whether the Federal Circuit can formulate such a test.

We hope that you have found this advisory useful. If you have additional questions, please contact your Arnold & Porter attorney or:

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1 "If a claimed method does not meet the machine-or-transformation test, the examiner should reject the claim under section 101 unless there is a clear indication that the method is not directed to an abstract idea. If a claim is rejected under section 101 on the basis that it is drawn to an abstract idea, the applicant then has the opportunity to explain why the claimed method is not drawn to an abstract idea," *available at*: http://www.uspto.gov/patents/law/exam/bilski_guidance_28jun2010.pdf.