No. 08-964

IN THE

Supreme Court of the United States

BERNARD L. BILSKI AND RAND A. WARSAW,
Petitioners,

v.

JOHN J. DOLL, ACTING UNDER SECRETARY OF COMMERCE FOR INTELLECTUAL PROPERTY AND ACTING DIRECTOR OF THE UNITED STATES PATENT AND TRADEMARK OFFICE,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

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BRIEF OF *AMICUS CURIAE* TIMOTHY F. MCDONOUGH, PH.D. IN SUPPORT OF PETITIONERS

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QUESTIONS PRESENTED

1. Whether the Court of Appeals for the Federal Circuit erred by holding that a "process" must be tied to a particular machine or apparatus, or transform a particular article into a different state or thing ("machine-or-transformation" test), to be eligible for patenting under 35 U.S.C. § 101, despite this Court's precedent declining to limit the broad statutory grant of patent eligibility for "any" new and useful process beyond excluding patents for "laws of nature, physical phenomena, and abstract ideas."

2. Whether the "machine-or-transformation" test for patent eligibility adopted by the Federal Circuit, effectively foreclosing meaningful patent protection to a business model involving a series of transactions among a commodity provider, consumers, and market participants, contradicts the clear Congressional intent that patents protect "method[s] of doing or conducting business." 35 U.S.C. § 273.

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INTEREST OF *AMICUS CURIAE*[1]

Timothy F. McDonough, Ph.D. is a political economist, inventor and entrepreneur. He is the inventor of "Mechanism and business method for implementing a service contract futures exchange," patent number 7,373,320[2]. He holds a Bachelor of Science in Electrical Engineering from the University of Hawaii at Manoa, a Master of Science in Economic Research from the University of North Texas and a Doctor of Philosophy in Political Economy from the University of Texas at Dallas.

In his 30-year professional career Dr. McDonough has designed components and installations of autopilot and collision avoidance systems for transport category airplanes such as the Boeing 757/767 and Douglas DC-10. He has served as a senior capacity planning analyst on the headquarters staff of American Airlines where he employed the principles of applied microeconomics and operations research to the challenge of efficiently allocating services of one of the largest air carrier networks in the world. As a self-employed business consultant he has assisted major suppliers in the utilities, communications, banking, entertainment, apparel, and food distribution industries to optimize their

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[1] Pursuant to Supreme Court Rule 37, no counsel for any party authored this brief in whole or in part, and no person or entity other than *amicus curiae* made a monetary contribution to the preparation or submission of the brief. Counsel of record for all parties were timely notified 10 days prior to filing and have consented to this filing. Letters of consent have been filed with the Clerk of the Court.

[2] Application filed March 30, 2000 and issued May 13, 2008.

service offerings, product mix, distribution and pricing.

Dr. McDonough has no business or personal relationship with the petitioners and does respectfully submit this brief as a true *amicus curiae* in hope that the policy and economic arguments presented herein may encourage this Court to affirm the two questions presented in this case.

SUMMARY OF ARGUMENT

The present *amicus curiae* takes no position on whether the Petitioner's claims are patentable. His concern is that the economic and policy effects of implementation of the decision of the Court of Appeals for the Federal Circuit in this case would a) hamper the formation of capital in the services sector of the economy, b) degrade or eliminate existing property rights that are essential to continued infant industry protection, and c) eliminate incentive to inventors to disclose innovations that would further the public weal.

INTRODUCTION

American innovation is not confined to Industrial Age mousetraps and other cleverly contrived gadgets. The modern economic agent is more likely to encounter innovation today in the services they consume than in the contraptions they use. The present *amicus curiae* suggests that the decision of the Federal Circuit in this case is an attempt to apply an Industrial Age standard to address a perceived Services Age problem, a problem that the present *amicus curiae* suggests does not exist.

ARGUMENT

IMPEDIMENT TO CAPITAL FORMATION IN THE SERVICES SECTOR OF THE ECONOMY

The sector composition of the United States economy has shifted significantly from agriculture and manufacturing to services since the ratification of the Constitution and the enactment of the first patent legislation in 1790. When the first census to include a breakdown of economic activities was conducted in 1820, it was found that private goods-producing industries[3] accounted for 97% of aggregate output.[4] By 1947 the U.S. Department of Commerce reports that private services-producing industries[5] accounted for 48% of output and the share of private goods-producing industries fell to 40% of output.[6] In 2007 private services dominated the economy with

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[3] Private goods-producing industries consists of agriculture, forestry, fishing, and hunting; mining; construction; and manufacturing.

[4] Historical Census Browser. Retrieved June26, 2009, from the University of Virginia, Geospatial and Statistical Data Center: http://fisher.lib.virginia.edu/collections/stats/histcensus/index.html.

[5] Private services industries consists of utilities; wholesale trade; retail trade; transportation and warehousing; information; finance, insurance, real estate, rental, and leasing; professional and business services; educational services, health care, and social assistance; arts, entertainment, recreation, accommodation, and food services; and other services, except government.

[6] U.S. Department of Commerce. Retrieved June 16, 2009, from the Bureau of Economic Analysis: http://www.bea.gov/industry/gpotables/.

69% of the total with goods production declining to a share of only 31%.[7]

Innovation in the delivery of services is usually manifested in improvements in organization of factors of production to achieve higher efficiencies. The discipline of industrial engineering is a prolific contributor to advancement of service efficiencies but it is not the only contributor. The services themselves are intrinsic innovations that by their presence in the economy division of labor and other input factors of production is enabled and the subsequent economies of comparative advantage accrue to the entire society.

A substantial portion of the 69% share of economic activity represented by the services sector does not result in any physical transformation of any article or state or thing. Some services innovations may only rearrange human labor that may operate in a sedentary physical state with no manipulation of matter yet are easily recognized by a rational person to be a useful, concrete and tangible result. Such innovations surely advance the public weal as much or more so in a services dominated economy than the many cleverly constructed gadgets did in the Industrial Age.

Congressional intent on the patentability of methods is explicitly expressed in 35 U.S.C. § 101 ("Whoever invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof,

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[7] *Ibid.*

may obtain a patent therefore, subject to the conditions and requirements of this title.") and in the statutory definition of "process" in 35 U.S.C. § 100 ("The term "process" means process, art or *method*, and includes a new use of a known process, machine, manufacture, composition of matter, or material." Emphasis added.).

If the prime expression of innovation in the services sector is in methods of doing business then it stands to reason that intellectual property rights that are allocated by law to innovators of Industrial Age *things* should also be allocated to innovators of Service Age *methods* with as much vigor and conviction of the society afforded to the latter as to the former. This Court has done exactly that in denying *certiorari* to the petitioners in *State Street Bank* which has affirmed that business methods are patentable subject matter and thus satisfied the longstanding need to interpret the law of patents to be meaningful in the services dominated economy. *State Street Bank & Trust Co. v. Signature Financial Group*, 149 F.3d 1368, 1375 (Fed. Cir. 1998).

The United States is by public choice a free market capitalist economy that relies on government to preserve property rights but it is left to the devices of the market participants to assemble the means of production without government intervention whenever possible. The American economy is not, however, a perfectly competitive landscape. Market failures and distortions do occur and when they do we turn to government to enable allocation of scarce resources in ways that neutralize the distortions.

One way this is done is to grant temporary monopoly to innovators who are thus shielded from the risks of allocation of substantial capital to start-up or breakout enterprise.

Capital formation in any enterprise in any sector of the economy is fraught with risks that would ordinarily not be mitigated sufficiently to allow it to occur at all if not for the presence of mechanisms such as patent rights. In a series of about 60 interviews of people who invest in startup companies—venture capitalists, high net worth individuals and banks, Columbia Law Professor Ronald Mann found that,

> …for firms that have a credible product idea and the expertise to implement it, venture capitalists plainly accept the idea that their goal is to identify firms that will have sufficient market power to earn extraordinary profits. I[ntellectual] P[roperty] protection is important only indirectly, as a tool that might provide that market power. The key is "sustainable differentiation": something special about the particular firm that will enable it to do something that its competitors will not be able to do for the immediate future. The interviews reflect more picturesque terminology—referring to "secret sauce" or "magic dust." But it is clear that the key to a desirable investment opportunity is in the expectation of market power, and all

> other attributes of the company are indirect predictors of that ultimate goal.

Mann, Ronald J., "Do Patents Facilitate Financing in the Software Industry?", *Texas Law Review*, Vol. 83, p. 976, 2005.

The present *amicus curiae* has personally experienced difficulty in raising capital from private equity and institutional venture capital sources nationwide when no intellectual property could be offered by the *amicus curiae* as a capital contribution. The present case has caused further impediment to capital formation by the *amicus curiae* for a substantial services industry venture even though one of his business method patents is now issued.

Implementation of the decision of the Court of Appeals for the Federal Circuit in this case would permanently hamper the formation of capital in any industry and such impediment would be especially felt in the services sector where an Industrial Age idea of "machine-or-transformation" test is manifestly unsuited to services that now comprise 69% of economic activity in the United States.

DISRUPTION OF EXISTING PROPERTY RIGHTS

It is difficult to count the number of business method patents that have been issued since they can occasionally be classified with many non-method inventions. A popular proxy used for calculating trends in business method applications and issued

patents is patent class 705, "Data processing: financial, business practice, management, or cost/price determination"[8]. During the 20-year period July 1, 1989 to June 30, 2009 the United States Patent and Trademark Office (USPTO) issued 18,238 patents in class 705.[9] Class 705 issues rose sharply from 998 in 2005 to 1,453 in 2006 and then increased steadily to 2,673 in 2008.[10]

By definition, all of these patents have been found by the USPTO to satisfy the statutory requirements of patentability prior to the Federal Circuit decision in this case. This standard was affirmed by this Court in *State Street* and *Diamond v. Chakrabarty,* 447 U.S. 303, 308-309 (1980) ("Congress plainly contemplated that the patent laws would be given wide scope," and that "Congress intended statutory subject matter to 'include anything under the sun that is made by man'").

The Federal Circuit decision in this case has already cast a stifling pall over the more than 18 thousand patents in class 705 that are currently in force. It is difficult to recount a situation in the history of patent law in the United States when the rules have changed so drastically so late in the game for so many.

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[8] Reference tools: Retrieved June 30, 2009, from the USPTO website http://www.uspto.gov/web/patents/classification/.

[9] Patent search: Retrieved June 30, 2009, from the USPTO website http://patft.uspto.gov/netahtml/PTO/search-adv.htm

[10] *Ibid.*

LOSS OF INCENTIVE FOR INVENTORS TO PUBLICLY DISCLOSE INNOVATIONS

This Court has consistently recognized the true purpose of the laws of intellectual property. *Kendall v. Winsor*, 62 U.S. 322, 328 (1858) ("[T]he benefit to the public or community at large was another and doubtless the primary object in granting and securing that monopoly."). *Pfaff v. Wells Electronics, Inc.*, 525 U.S. 55, 63 (1998) ("[T]he patent system represents a carefully crafted bargain that encourages both the creation and the public disclosure of new and useful advances in technology, in return for an exclusive monopoly for a limited period of time."). The Federal Circuit decision in this case threatens to severely compromise that bargain and the sector of the economy that now represents more than two thirds of all output is going to suffer the most if allowed to stand.

Innovative methods of providing services cannot be hidden away in the company safe as readily as the secret gadget and a mountain of non-disclosure agreements are no substitute for intellectual property statutes. Without IP protection capital providers will not have incentive to invest, entrepreneurs will not have incentive to engage in the process of building and nurturing new enterprise and innovators will have no incentive to disclose their ideas to the public.

CONCLUSION

The American propensity to innovate is evident in every economic age. From the Age of Agriculture

through the Industrial Age and now the Age of Services, the American economy has demonstrated an efficiency that is unmatched by any system on the planet. The allocation of intellectual property rights under the laws of the United States has played a pivotal role in that ascendency.

For the foregoing reasons the present *amicus curiae* therefore urges the Court to affirm the two questions presented in this case.

Respectfully submitted,

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