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Patent Lawsuit Raises Issues for Life Insurance Industry

By Michael C. Gilchrist, attorney
Previously published in Law 360, April 24, 2009

An Iowa jury recently found that Transamerica Life Insurance Company has infringed a patent owned by Lincoln National Life Insurance Company related to the administration of variable annuities. The resolution of this case through the appeals process could have significant effects on the variable annuity industry and on the law of so-called "business method" patents.

Lincoln's Patents

Lincoln National Life Insurance Company owns three patents related to the administration of variable annuities. Specifically, the patents relate to popular riders known as Guaranteed Minimum Withdrawal Benefits (GMWB) and Guaranteed Lifetime Withdrawal Benefits (GLWB). It is likely that Lincoln has additional patent applications relating to the riders still pending.

Guaranteed Living Benefits

Most companies that offer variable annuities offer some flavor of a guaranteed living benefit. Generally these riders permit an owner of a variable annuity to participate in the upside of investing in securities, while providing a guarantee that if the value of the underlying securities declines, the beneficiary will still be assured a minimum periodic payment. In their most basic form, they guarantee that an annuity owner will be returned all of their investment in a variable annuity, even if the securities that back the variable annuity decline in value.

For example, a person puts $100,000 into a variable annuity account with a GMWB rider, and withdraws $7,000 per year. If the variable securities perform well, the account value grows, and the owner may increase the amount being withdrawn each year. Furthermore, at the end of the contract, any accumulated value in the account will belong to the owner. However, if the securities do not perform well, and the value of the account drops to zero, the rider provides that the owner will still be entitled to receive the $7,000 per year until the initial investment is repaid in full.

A GLWB provides that the beneficiary is guaranteed to be able to withdraw a percentage of the deposited amount for the rest of their life, even if the account value goes to zero. Commonly a GMWB and GLWB are offered together with the option to choose one or the other at the time of exercising the guarantee. Many of the products also include a "step-up" feature to permit owners to lock-in market gains to the guarantee.

GMWBs, GLWBs and other similar riders have been at least partially responsible for a large surge in the popularity of variable annuities. The vast majority of variable annuities now offer some form of guaranteed living benefit.

Lincoln's Dispute with Transamerica

Lincoln sued Transamerica, alleging that administration of Transamerica's GMWB and GLWB riders infringes their patent. After a trial in the U.S. District Court for the Northern District of Iowa in Cedar Rapids, a jury determined (Feb. 13, 2009) that Lincoln is entitled to $13 million in damages for patent infringement. Lincoln has also requested that the court issue a permanent injunction to stop Transamerica from selling and servicing its infringing products. The court has not yet determined whether such an injunction is appropriate.

Transamerica has filed post trial motions arguing that

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the verdict should be thrown out because the patent is invalid and because they did not perform all of the steps required to infringe the patent. Depending on what happens with the post-trial motions, it seems likely that one of the parties will appeal the matter to the Court of Appeals for the Federal Circuit (the highest court that commonly hears patent appeals, only the Supreme Court is higher) before it is finally resolved.

Lincoln has also sued Transamerica on its other two patents related to variable annuity administration. Those lawsuits are pending in Indiana.

Effect on the Variable Annuity Industry

In addition to Transamerica, Lincoln has also already sued Jackson National Life Insurance Company asserting that administration of Jackson's GMWB and GLWB products infringes the Lincoln patents. That case is pending in Indiana, but probably will not be ready for trial for another year.

If the validity and infringement holdings of the Iowa case are upheld through the appeals process, it could lead to additional lawsuits or demands to cease and desist.

Important Business Method Patent Issues

From a patent law perspective the most important, interesting defense raised by Transamerica is that Lincoln's patent is directed to inappropriate subject matter for patent protection. An appeal of the Iowa case to the Court of Appeals for the Federal Circuit may raise important issues for many financial services patents and other business method patents.

New Test for Business Method Patents

In 1998, the Court of Appeals for the Federal Circuit abolished the rule against business method patents. That resulted in a deluge of financial service and other business method type patent applications. The resulting patents have been widely criticized. Some of Supreme Court justices have even hinted that they question whether such patents are appropriate.

This past fall, the Federal Circuit decided *In re Bilski* which redefined the test for determining whether a claimed method is appropriate subject matter for patent protection. According to the new test, in order to qualify as proper subject matter, the claim at issue must either (1) be tied to a particular machine or apparatus, or (2) transform an article into a different state or thing. In the Bilski case, the Federal Circuit specifically left open the question of whether reciting that the method would be performed by a computer would be sufficient to satisfy the first prong of the test.

Will Computerized Methods Satisfy New Test?

The Lincoln patent claims a "computerized method of administering a variable annuity plan," but otherwise does not recite any structure that might be considered a machine or apparatus. Lincoln argues that by reciting that the method is "computerized" in the preamble, the claim is tied to a particular machine—namely a computer that has been programmed to administer variable annuities.

Thousands of business method and software patents have been issued that use this same general format of reciting a process performed by a computer. If the Federal Circuit determines that performing a process with a computer is sufficient to satisfy the test, then many of the software and financial services patents issued in this form will be saved and patent protection for such inventions will be permitted going forward. On the other hand, if using a computer to perform the steps is not sufficient to tie a process to a particular machine, then these issued patents will be invalid and it will be much more difficult to obtain software and financial service type patents going forward. Therefore, the *Lincoln v. Transamerica* case may have a significant effect on the future of business method patents.

Injunction for Existing Products

If the validity and infringement of the patent are upheld on appeal, there is still the question of whether an injunction is appropriate, especially with respect to the annuity products that Transamerica has already sold. Lincoln is requesting a permanent injunction that not only bars Transamerica from selling the riders in the future, but also from servicing existing customers that purchased the riders. That would appear to create a significant hardship on annuity owners who have structured their retirement portfolios to rely on the riders, which may mean that such an injunction would be denied as against public policy. However, Lincoln has suggested that Transamerica may be able to administer the riders without infringing by performing some or all of the steps by hand rather than computer, or by relocating the computers that perform the steps outside the United States.

Conclusion

The final resolution of the dispute between Lincoln and Transamerica could impact the annuity industry. Furthermore, it could answer important questions relating to the permissible scope of business method patents in general.

Author's Note: The Supreme Court is considering whether to review the Bilski decision, which could result in yet another revision to the law of business method patents.

Patent Reform? Judges First

By R. Scott Johson

While the debate rages in Washington D.C. about how or whether to alter the structure of our system for filing and reviewing patent applications, a separate bill to establish a pilot program for the “enhancement of expertise in patent cases among district judges” has already passed one chamber of Congress. H.R. 628, 111th Cong. § 1 (2009). On March 17, 2009, the House of Representatives passed H.R. 628 by a voice vote of 409 “ayes” to 7 “nays” and 15 “present/not voting.”

An identical bill, S. 299, has been referred to the Senate Judiciary Committee. This legislation would allow district judges to “request” to hear cases relating to patents or plant variety protection. These judges would then be designated by the chief judge to hear those cases. Cases would still be randomly assigned, but if the random assignment resulted in a non-designated judge for the patent or plant variety protection matter, the non-designated judge would then have the option to decline the case. The case would then be randomly assigned to one of the designated judges.

The legislation goes on to limit the implementation of the designation program to judicial circuits which either have local rules for patent and plant variety protection cases or are in the top 15 of district courts to hear such matters. Even if your local court has adopted the required local rules, they must still have at least 10 district judges authorized (all positions must not be filled apparently) and have at least 3 judges willing to be designated.

If qualified, the court may be selected for the pilot program at the discretion of the Director of the Administrative Office of the United States Courts, James C. Duff (appointed by Chief Justice Roberts on April 20, 2006). The legislation also authorizes $5 million for additional training and clerkships. The program is to last for 10 years and requires the Director, in consultation with the chief judges of the designated courts and the Director of the Federal Judicial Center, to submit reports to the Congressional Judiciary Committees at approximately the 5-year and 10-year marks. These reports will include an analysis of the program’s success, effects on efficiency, a comparison of reversal rates and pendency for designated and non-designated judges, a discussion of whether litigants prefer the designated courts, and finally, an analysis of whether the pilot program should be extended.

Many in the legal community will be watching to see if and when this legislation takes effect. Some judges have already commented that such a program may be beneficial, allowing judges to specialize. Others have expressed skepticism, noting such specialization could in itself be problematic. As it was noted in a Chicago Daily Law Bulletin article in May, 2007, Judge Moran of the Northern District of Illinois noted he would volunteer, but jokingly (we assume) commented that allowing “judges over 50 [to] handle computer software issues may be a violation of due process.”

An interesting tidbit – the Senate version of the bill, S. 299, was sponsored by former ranking member of the Senate Judiciary Committee, Senator Arlen Specter (D-PA). There is no indication as to how or if his recent change in party and the ensuing shuffle of seniority within the committee will affect the legislation.

Changes in EPO Claims, Pages and Designation Fees

By Janae Lehman Bell

The number of pages and claims in applications filed in Europe has been on the rise since the late 1980’s. In an effort to reduce the backlog of applications waiting for examination, the European Patent Office has introduced a new fee schedule for those applications filed or entering Europe at the regional phase on or after April 1, 2009. The fees relate to the number of pages and claims in the application and the designation fee.

The new claim fees are imposed on a sliding scale. No excess claim fees are charged in applications having 15 or less claims; however, for those having more than 15 claims but less than 51, each claim will be subject to a fee of about $300. Additional claims over 50 will cost over $700 each.

The new fee schedule penalizes applications having more than 35 pages at the time of filing or entry into the regional phase in Europe. A fee of about $16 is charged for each additional page over 35. Thankfully sequence listings are excluded when determining the total number of pages present in an application.

The new fee schedule also alters the designation fee. Applicants will no longer have the option to pay a designation fee for an individual European Patent Convention (EPC) member state, instead all EPC states are automatically designated and included in a flat fee of about $740.

In light of these changes, if you will be filing an application in Europe, you may want to consider reducing the claim number in your application to 15 or less using multiple dependent claims, a format which is allowable in Europe. We encourage you to contact your patent attorney for further discussion on how these changes impact any current patent applications pending in Europe or for implementing a strategy in any future filings.

College Color Schemes Can Protect Trademarks

Case Illustrates Important Issues that May Apply to Many Businesses

By Mark Hansing

A Federal Court of Appeals has decided a dispute in favor of four universities seeking to protect the colors they use on merchandise, including T-shirts. Particularly noteworthy is that no where did any accused T-shirt use the name, logos, or initials of any of the universities LSU, Oklahoma, Ohio State, or USC. The case of *Board of Supervisors for Louisiana State University Agriculture and Mechanical College, et al. v. Smack Apparel Co., et al.*, held: "We conclude that colors, content, and context of the offending t-shirts are likely to cause confusion as to their source, sponsorship, or affiliation, ….".

Whether color(s) can function as a protectable trademark is by no means a new issue. But the Court admitted that the Smack Apparel direct challenge to the ability of the universities to control use of their historic colors, apart from their school names, logos, mascots, or initials, raised some novel issues.

While the case is interesting for just that reason, it calls for business owners to consider the colors it uses and if that color scheme might be protected by trademark law. As with more traditional trademarks, the universities felt they had to protect what they consider to be valuable assets. A color scheme could, likewise, be such a valuable asset for any business in association with one or more of its products or services.

The Smack Apparel Case

The T-shirts at issue all had a similar approach--the two-color scheme of one of the schools (e.g. crimson and gray for Ohio State) and what the Court called "contextual references" to the school other than the school name, logo, or initials. For example, "contextual references" on the Ohio State t-shirt included:

1. the words "Got Seven?" and "We do! 7 Time National Champs" (found to refer to Ohio State's seven national football championships); and
2. an outline of the state of Ohio with a marker noting Columbus, Ohio (the location of Ohio State).

The Court rejected each Smack Apparel argument, finding, among other things:

a.) each school owns a protectable trademark (stating the color scheme was "capable of distinguishing the [university's products] from those of others" and that the colors were not merely decoration or purely functional (e.g. as a warning, for visibility, for fabric durability, etc.); and

b.) each accused Smack Apparel shirt "creates a likelihood of confusion in the minds of potential customers as to the 'source, affiliation, or sponsorship'" of the shirt (stating "particularly the overwhelming similarity of the marks and the defendant's intent to profit from the Universities' reputation—compel this conclusion").

The Court chastised Smack Apparel for creating "the illusion of affiliation with the Universities and essentially obtaining a 'free ride' by profiting from confusion among the fans of the Universities' football teams who desire to show support for and affiliation with those teams." The opinion mentioned that each school had used its color combination for over a century and had spent millions of dollars marketing with the colors (and particularly with sports apparel); finding that the colors serve "as shorthand for the schools themselves".

Lessons to Apply

The Smack Apparel case highlights that value can exist in any type "word, name, symbol, or device, or any combination thereof" that is used "to identify and distinguish" a company's goods from those manufactured or sold by others and to indicate the source of the goods, even if that source is unknown." *(from Federal Trademark Statute, 15 United States Code, § 1127)*. The term "symbol" can include a color or a color combination.

While not necessarily easy to obtain, every company should review its words, names, symbols, and devices to see if appropriate steps have been taken to protect and enforce color schemes. Protection does not necessarily require a showing of a century of use, millions of dollars of advertising, or national fame as found in Smack Apparel. If a color or color combination is recognized by a significant number of potential customers of that product or service as indicating the source of the product or services, it is eligible for protection. For example, it is doubtful that the public at large is aware that Owens-Corning has a trademark in pink for at least one type of its fiberglass insulation. But builders, insulation contractors, and the like were.

The Smack Apparel case also at least implies that it is easier to protect colors in combination with other words or symbols (i.e. the "contextual references" on the Smack Apparel T-shirts). Therefore, if a company has used a color or color combination for at least several years (five years is one benchmark), consideration should be given to take steps to obtain maximum protection. A trademark lawyer can explain those steps.