

Patents available for franchisors' business methods

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Patents are typically thought of as a means of protecting the innovations of scientists or engineers. It is now possible, based on a recent patent law decision, that certain franchisors may have the ability to protect their business methods through patents. While franchisors have long been successful in obtaining patents for inventions such as equipment or recipes, franchisors have been unable to obtain patents to protect their business methods, which in many cases are at the heart of a franchise. Franchisors typically have turned to trade secret protection for their business methods and simply required confidentiality from those persons who had access to the methods. Now, for many franchisors, there may be a more desirable option for protection.

A patent provides its owner with a legally enforceable right to prevent all others from making, using, selling or offering for sale a competitive product or service covered by the patent. Substantial royalties may be collected from authorized manufacturers, sellers or users of a patented invention. Unauthorized manufacture, use, sales or sales offers of a patented invention may be immediately enjoined by the federal courts, and may result in significant damage awards.

The competitive advantages for a business that protects its products or services with a U.S. patent are significant. Patents provide the owner with exclusive protection for 20 years from the date of filing of the patent application. Moreover, patents provide protection against anyone who makes, uses, offers to sell or sells the patented invention. However, there are two main obstacles to obtaining such patent protection: (1) the system cannot have been in public use or on sale, or described in a single printed publication or patent, for more than one year prior to filing of the patent application; and in addition, (2) the system cannot have been in multiple prior references with a motivation to combine the references.

Questions about the scope of U.S. patent protection were considered, and resolved, in the recent decision of the U.S. Court of Appeals for the Federal Circuit in the case of *State Street Bank & Trust Co. v. Signature Financial Group, Inc.* In *State Street*, Signature owned U.S. Patent Number 5,193,056, directed to a data processing system for hub-and-spoke financial services. When State Street Bank approached Signature to license the technology, it was rebuffed. State Street Bank then challenged the patent. It cited longstanding legal precedent holding that "business methods" are not patentable. If Signature could legitimately claim ownership of this business method, State Street Bank and other critics argued, then theoretically somebody could have claimed ownership of such common business tools as 401(k)s and double-entry accounting, and charge a fortune to anyone who dared infringe on their monopoly.

The federal trial court in Massachusetts that originally heard the case agreed with State Street Bank, holding that business methods are no more patentable than "laws of nature, physical phenomena, and abstract ideas." But on July 23, 1998, the Federal Circuit Court of Appeals in Washington, D.C., overturned the decision, and held that a business method which uses a mathematical formula can be patented so long as it meets the three traditional criteria for legal protection: that it be new, useful, and would not have been

obvious to someone with knowledge in the field. In no uncertain terms, the court slammed the “ill-conceived” legal precedent that had prevented the patenting of business methods. Noting that patent law is designed to give inventors ample incentive to innovate, the court noted that Congress intended the Patent Act “to extend to ‘anything under the sun that is made by man.’”

Because of the massive flowering of new products and services in recent years, as well as innovative management techniques, the State Street decision already is having a strong impact on the financial-services, banking and insurance industries. Some say virtually all United States businesses could be affected by the decision which may be so broad as to allow patenting of marketing techniques and business methods. This opens the door for franchisors with business methods that track or process information that may now be allowed to patent such methods and greatly enhance the value of the intellectual property, which serves as the basis of the franchise system.

Trade secrets more difficult

Trade secret protection is more difficult to enforce than patent protection, but lasts forever provided the trade secret is kept confidential. One disadvantage to trade secret protection is that a franchisor must take action to protect the confidentiality of the trade secret. If a franchisor publishes the business method or lacks controls to ensure the secrecy of a business method, the trade secret protection effectively may be destroyed. However, many companies have been successful in choosing trade secret protection rather than patent protection for their systems or other inventions. For example, Coca-Cola showed much foresight in deciding to protect its recipes via trade secret rather than patent protection. If Coca-Cola had decided to patent its recipe over 20 years ago, the recipe would now be public knowledge and available for public use. Competitors could presumably copy the recipe and market a similar product under another name, thereby greatly reducing the value of the “Coca-Cola” trademark. If a franchisor expects that its business method will still be secret and viable in 20 years, it may be more beneficial for that franchisor to protect the business method as a trade secret.

Apart from opening new doors in patent law, State Street likely will have a longstanding and profound impact on how businesses choose to manage their internally generated know-how. The importance of protecting and judiciously exploiting one’s valuable intellectual property in today’s increasingly competitive marketplace cannot be over emphasized. The ability to protect technical innovations, including methods of doing business, can mean the difference between success and failure. If a franchisor employs a unique process or business method as part of its business, serious consideration should be given to pursuing patent protection of these commodities.