INSURANCE IP BULLETIN

An Information Bulletin on Intellectual Property activities in the insurance industry

A Publication of - Tom Bakos Consulting, Inc. and Markets, Patents and Alliances, LLC

Introduction

This, our second issue, is packed with information, thoughts, and ideas we hope you will find useful in the conduct of your business in the growing patent rich insurance industry.

In this issue **Phil Hargrove**, VP of the Intellectual Asset Management function for GE Employers Reinsurance Company, provides his perspectives on the growing use of patents in the insurance industry to protect intellectual property. He warns insurance company managers of the need to be aware of the risks and opportunities this change is creating.

Our mission is to provide our readers with useful information on how intellectual property in the insurance industry can be and is being protected – primarily through the use of patents. We will provide a forum in which insurance IP leaders can share the challenges they have faced and the solutions they have developed for incorporating patents into their corporate culture.

Please use the FEEDBACK link above to provide us with your comments or suggestions. Use QUESTIONS for any inquiries. To be added to the Insurance IP Bulletin e-mail distribution click on ADD ME. To be removed from our distribution click on REMOVE ME.

Thanks, Tom Bakos & Mark Nowotarski

Feature Article

Ignorance Will Be No Excuse

By: **Phil Hargrove**, Vice President, Intellectual Asset Management, GE Employers Reinsurance Company, Kansas City, MO

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The inaugural issue of the *Insurance IP Bulletin* identifies and defines many of the concepts and milestone events that have made patents in the insurance industry a topic of importance. Since the State Street Bank decision upholding patents on business methods, the growth rate for issued patents and applications filed for USPTO class 705/4 (Insurance) has grown at a compounded annual rate of more than 30% since 1998--more than triple the overall growth rate for all classes of patents. On a pure numeric basis, the number of issued patents remains small compared to other classes; however, thousands of patents are both issued and pending in the broader class 705, which includes all of financial services and software.

Patents are big business and a big business issue. An entire multi-billion dollar industry has emerged around patents. We're seeing the emergence of consultants to help craft a patent strategy and identify assets to protect, companies that specialize in searching for prior art or for clearance measures, firms to value and brokers to license patents as a source of revenue. We're also seeing more books, magazines and conferences on the subject ... and attorneys to

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draft and file patents ... and attorneys to prosecute those who infringe. The Justice Department has recently commissioned a study of the patent industry because it has become such a visible and important part of our economy. The Department figures patents contribute 5% to the GDP.

And, speaking of attorneys, the number of them specializing in patents has grown at an annual rate that exceeds the growth in patents filed and issued. For the insurance industry, any topic that attracts that kind of attention from the legal community is usually a leading indicator of trouble, with a capital \underline{T} and that rhymes with \underline{P} and that stands for Patent.

Every hour of every business day a patent infringement lawsuit is filed somewhere in the United States. According to a recent edition of the *Insurance Journal*, the average legal cost to defend against a claim of infringement is \$3 million, and that's if the defendant can prove it hasn't infringed. If there is willful infringement, treble damages can be awarded on top of whatever amount the court has assessed for the basic infringement. And that's all on top of the legal costs. To add insult to injury, the court may issue an injunction barring the continued use of the infringed patent claims and/or a company may have to negotiate a license fee to continue selling a product or performing a routine business process.

For an industry known for "me too" innovation, this is a trend that will have a major impact on the development of new products and services. Just ask Hartford Insurance. It recently paid \$80 million to settle a patent infringement and theft of trade secret lawsuit brought by Bancorp Services. Met Life and Sun Life are now in the crosshairs for infringing the same patent.

The effect of patent infringements on our industry is not limited to just those patents issued in the insurance class. At a high level, the processes of banks are similar to our own. We underwrite risks; they underwrite loans. The process is similar and the use of patented technology to assist these processes is growing throughout financial services. How different is the processing of premium payments from the processing of loan payments? The insurance industry is part of the broader financial services industry and one familiar with the processes used can find many similarities.

The \$520 million judgment against Microsoft for infringing a patent issued to the University of California and licensed to Eolas for certain features of a web browser may seem like a distant concern for the insurance industry. Software is typically protected by copyright and while cases of copyright infringement are growing primarily due to carelessness on the part of programmers, big software companies have had a tough time making their case. In the 80's, Apple tried and failed in its suit against Microsoft for the graphic user interface and Lotus unsuccessfully pursued Microsoft and Borland for the look and feel of electronic spreadsheets.

What if those companies had patents on key components of their software? Amazon was successful against Barnes & Noble for the "one-click" method because it had a patent. MercExchange was successful in its case against eBay for the "Buy It Now" feature because it had a patent. The use of the Internet is growing within our industry, along with the risk of infringing on someone else's patent. "Insure It Now" may seem like a great idea for your new

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customer website, but have you researched to make certain someone else doesn't have a patent on it? Claiming ignorance is no defense against a claim of infringement.

Many would question how innovation, insurance, and patents could possibly be uttered in the same breath. The good news is that there is a great deal of patented innovation occurring that affects our industry. The bad news is that very little of it is coming from insurance companies themselves.

Mark Nowotarski and Tom Bakos estimate that fewer than 30% of the patents issued or pending in the insurance class belong to insurance companies. Of the 70% remaining, individuals or small companies own most of them. History from other classes of patents indicates that these individually held patents pose the greatest threat. If you have a call center, odds are that you know or soon will know the infamous Katz patents. Who are the next Katzes in our industry? They are definitely out there.

Insurance is all about understanding and quantifying risk. There are even insurance companies that provide insurance coverage for various intellectual property risks, yet this may be a case of the shoemaker's kids going shoeless. There are very few within our industry that are fully aware of both the risks and opportunities for the industry itself with respect to patents and other forms of intellectual property.

There are a number of sources of information, such as this *Insurance IP Bulletin* that can help you learn about this important and growing trend in our industry. From the US Patent & Trademark Office website to search engines such as Google or Yahoo, there is a wealth of information available. While the sky may not be falling, there are definite signs of a brewing storm and now is the time to prepare.

Patent Watch

AIG joins the "Issued Patent Club"

AIG has joined the club of insurance and financial services organizations holding issued US patents. Their first internally generated patent, US 6,671,677, "Method and System for Reducing Mortgage Interest Rate and Mortgage Guaranty Insurance Premiums Associated with a Mortgage Loan", was issued in December of last year. This patent describes a new way of financing points in a mortgage without paying an increased mortgage insurance premium. The patent was filed by AIG member company United Guaranty Residential Insurance Company and protects some of the innovations underlying their RateXchange® insurance product.

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AIG's chairman, M.R. Greenberg, is a strong proponent of patents. He has encouraged all divisions and subsidiaries of AIG to protect their intellectual property. As of this writing, they have over 50 additional patents pending worldwide.

AIG's initiative in this area is indicative of changes occurring in the economic structure of the insurance industry. It both encourages and warns other insurance companies to take full advantage of patents to protect and cultivate their own innovations.

[Breaking News: AIG's second internally generated patent, US 6,772,128, "Nuclear Decommissioning Insurance Financial Product and Method", was just published on August 3. This patent describes a new method for insuring against the financial uncertainty of decommissioning nuclear power plants.]

Patent Tech

Broad Thinking - Yes, but will it fly?

The patent process, itself, ought to stir the inventor into thinking in broad terms about his or her invention. Inventors are granted exclusive rights to encourage them to share their inventive ideas so as to stimulate others to make further beneficial advances. What this means is that, if <u>you</u> the inventor don't think beyond the narrow confines of your inventive box, someone else will!

For example: The Wright Brother's patent application for airplane control mechanisms might have <u>only</u> referred to "wing warping" as a method for controlling airplanes in flight. After all, per all of the documentaries we have seen, that was the essence of how the control mechanism they were testing at Kitty Hawk worked.

Contrary to popular belief, the Wright brothers did not invent the airplane. There invention was an improvement of an existing concept. Their invention made that existing idea for a heavier than air flying machine useful. In fact, what they referred to as "aeroplanes" in their patent were actually a reference to what we would call the wings of a modern aircraft.

The object of the Wright brothers patent (US 821,393 issued May 22, 1906) was to control a flying machine in flight as stated in their patent application.

The objects of our invention are to provide means for maintaining or restoring the equilibrium or lateral balance of the apparatus, to provide means for guiding the machine both vertically and horizontally, and to provide a structure combining lightness, strength, convenience of construction, and certain other advantages which will hereinafter appear.

The patent describes how the aeroplanes (wings) are constructed and how "each aeroplane is twisted or distorted around a line ... so that each aeroplane surface is given a helicoidal warp or

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twist." Then, of course, the patent explains how this works on air flows to move the airplane about.

If the Wright brothers wrote their patent application to incorporate only the narrow "wing warping" process to bend the lateral edges of the aeroplanes that they were testing, they may have ended up being nothing more than a footnote in history and remained poor, frustrated bicycle mechanics.

But, for whatever reason, perhaps inspired by an astute patent attorney, the Wright brothers patent application described their control method more broadly by including in the description of the control mechanism the following wording:

We wish it to be understood, however, that our invention is not limited to this particular construction, since any construction whereby the angular relations of the lateral margins of the aeroplanes may be varied in opposite directions with respect to the normal planes of said aeroplanes comes within the scope of our invention.

Thus, the concept of moveable wing surfaces (equivalent to the ailerons of modern aircraft) was covered and the Wright brothers patent applied to all fixed wing aircraft ever flown. If they had not been inspired to move beyond the narrower "wing warping" claim, someone else would have probably improved their invention with the "moveable wing surface" method and trumped their patent.

So, the lesson is - get the most that you can out of your inventive processes. Look at the solutions you develop in their broadest possible terms. Look at them as another inventor would or get someone you trust to do that for you. And remember, your invention may be a solution to someone else's problem. Any use of your invention not contemplated in your application can become the property of someone else if they see it before you do.

Finding Innovation

Can You Patent an Insurance Product?

It might seem surprising that we should ask, "Can you patent an insurance product?", but the fact is, right now, in the United States, you can't. What you can patent is a business method that enables a new type of insurance policy or product. You cannot patent the product itself. This makes it somewhat awkward to talk about patents and insurance. To make the distinction that it is a business method and not the product itself that is patented, you may see statements like "patent protected insurance product" or "patented method of providing insurance" instead of simply "patented insurance product".

The inability to patent financial products directly makes it more challenging for a patent agent/attorney to serve their clients and for the clients, in turn, to get broadly effective patents

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on their inventions. They can't directly claim a type of insurance product that incorporates their inventive business method. Instead they have to carefully analyze the underlying technological processes (typically embedded in computer software) required to implement their inventions in insurance products and try to patent those.

An excellent example of a successful effort in this area is US 6,235,176, "Computer apparatus and method for defined contribution and profit sharing pension and disability plan". The inventor, Matt Schoen, invented a way to incorporate disability coverage into a defined contribution employee 401k plan. If the employee became disabled, the insurer would continue the employee's contributions. Matt did not and could not patent the disability product or policy itself. What he did patent was a computerized method for administering a large number of these policies. The patent was granted and Matt has since successfully licensed the patent to a third party. They, in turn, have brought a product enabled by the technological art disclosed in the patent to market.

The reason why financial products are not currently considered patentable by the US Patent Office is that they are not believed to be "statutory subject matter". The law, 35 U.S.C. 101, states that the <u>only</u> things you can get patents on are inventions that are either processes for doing something useful, a new composition of matter, a machine, or a manufactured item. A process for providing insurance is a process for doing something useful and the Court of Appeals for the Federal Circuit (effectively the supreme court for most patent cases) has ruled that it is therefore patentable. An insurance product, however, is considered by the US Patent Office to be a contract and not a "manufactured item" or any of the other three categories and hence is not patentable.

Many patent agents and attorneys disagree strongly with the Patent Office in this matter. Backed by their clients, they are working a number of rejected patents on financial products and insurance policies up through the appeals process. Elsewhere in this issue, for example, we mention that AIG just had a patent issue on a nuclear decommissioning insurance method (US 6,772,128 - see "AIG Joins the Issued Patent Club"). AIG's patent attorneys originally included in their patent application claims on the insurance policy itself. They even put a copy of the policy form right in their application (US 2003/0033171 A1). They weren't able to patent the insurance policy this time around, but they have since refilled the case and are trying again.

Of course, those familiar with the insurance business recognize that an insurance product is, essentially, an agreement between an insurance company and an insured. The insurance agreement is documented by the insurance policy. So, many other issues may be raised if it turns out that an "insurance policy" can be patented. There may be many consequences that we can only now imagine.

What do you think? Should the inventor of a new type of insurance product be allowed to have an exclusive right to that product via a patent? Please send comments to: lP@BakosEnterprises.com or to one of us individually (Tom - tbakos@BakosEnterprises.com or Mark - Mnowotarski@marketsandpatents.com

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Statistics

An Update on Current Patent Activity

Patent activity in USPTO class 705/4 provides a measure of invention in the insurance industry.

Patent applications have been published 18 months after their filing date only since March 15, 2001. Therefore, there are many pending applications not yet published. A conservative assumption would be that there are about 125 applications filed every 18 months in class 705/4. Therefore, there are, probably, about 550 class 705/4 patent applications currently pending, only 421 of which have been published.

Insurance Patents Issued by Year as of 8/11/04	
Class 705/4	
YEAR	#
2004	13
2003	23
2002	16
2001	21
2000	33
1999	38
1998	20
1978-1997	47
TOTAL	211

Insurance Patents Pending by Year Published as of 8/11/04		
Class 705/4		
YEAR	#	
2004	99	
2003	128	
2002	164	
2001	30	
TOTAL	421	

Because the pending patents total above includes <u>all</u> patent applications published since March 15, 2001, applications that have been issued will also appear in the issued patents totals.

Since the last issue of the *Insurance IP Bulletin* (June 15, 2004) two patents have been issued in class 705/4. One is the AIG patent (US 6,772,128, "Nuclear Decommissioning Insurance Financial Product and Method") mentioned in the *Patent Watch* section. The other was for a monitoring device which might have application in the health care field.

As an indication of continued increasing activity, however, there were 28 new published patent applications in class 705/4 in the past two months.

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Although patent applications often don't indicate assignments, one of the new published applications is assigned to GE Financial Assurance (now Genworth), 2004/0117289 - System and method for monitoring and processing trades. This invention is an automatic process (trade management system) for matching an insurers' actual asset purchases with its liabilities generated by new sales. It claims applicability for Life, annuity, LTCi coverages as well as automobile insurance and automobile warranties.

Another, 2004/153346 - Remote contents estimating system and method, is assigned to Allstate and is a new process for speedily settling a P&C claim.

The point is that some insurers are involved in protecting intellectual property they develop with patents.

Resources

These are links to web sites which contain information helpful to understanding intellectual property.

United States Patent and Trademark Office (USPTO) - http://www.uspto.gov

World Intellectual Property Organization (WIPO) - http://www.wipo.org/pct/en

Patent Law and Regulation - http://www.uspto.gov/web/patents/legis.htm