

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

By publishing a little later than our usual schedule we are able to close out 2007 with a complete 2007 issued patents and published applications table in the Statistics section. The editors were also able to enjoy a year-end holiday with a little less work and worry.

In this issue's feature article, *Designing Around a Threatening Patent*, Mark Nowotarski discusses how one might address a new patent which seems to threaten their own business activity. However, those of our readers who are considering protecting an invention they have made with a patent may learn something from the article about how to draft a stronger patent.

In our **Patent Q/A** we address a question regarding the current status of the Patent Reform Act of 2007. So far, in Congress there has been a lot of talk but little action. The bill has passed the House and is now being considered by the Senate. The House bill has a ban on "tax patents". The Senate bill has the same language. This ban could significantly impact insurance patents since many insurance inventions have positive tax consequences. Early 2008 may show progress on the Patent Reform Act front. We will keep you posted.

The Statistics section updates the current status of issued US patents and published patent applications in the insurance class (i.e. 705/4). We also provide a link to the *Insurance IP Supplement* with more detailed information on recently published patent applications and issued patents.

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

Thanks,
Tom Bakos & Mark Nowotarski

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

Feature Article

Designing Around a Threatening Patent (or, How I learned to Stop Worrying and Love the SOGRAT patent)¹

By: Mark Nowotarski

An important skill in an intellectual property based business is the ability to “design around” a threatening patent. A design around is a modification made to a patented invention so that most, if not all, of the benefits of the original invention are preserved, but the modification doesn’t infringe the claims of the issued patent.

The steps to a design around include:

1. Read the existing patent.
2. Analyze the claims to identify steps of each independent claim that can potentially be eliminated or changed.
3. Propose a way to eliminate or change said steps to create a new, non-infringing invention.
4. Verify that the non-infringing invention does not, in fact, infringe the existing patent.
5. File a patent application on the new invention.

To illustrate how this process can be applied to a real world example of an insurance patent, we will show how the steps could be applied to the infamous SOGRAT² patent, [US patent 6,567,790, “Stock Option Grantor Retained Annuity Trust”](#). The SOGRAT patent has recently become notorious in the estate planning profession due largely to the fact that the owner of the patent, Wealth Transfer Group LLC, sued an individual, [John W. Rowe](#), former CEO of Aetna, for infringing it. This lawsuit sent shock waves through the tax planning community since it appeared that patents could be used to block tax payers from minimizing their taxes and tax planners from giving the best possible tax savings advice to their clients. As a result, a number of powerful professional organizations, including the American Institute of Certified Public Accountants and the American Bar Association, have effectively lobbied Congress and the IRS to either ban patents like this, exempt tax planning professionals from the liability of infringing them, or heavily regulate their licensing. The SOGRAT patent has been characterized as a [tax patent](#) (or “tax planning patent”, or “tax strategy patent”). We need to be concerned about it, however, since it involves a novel use of annuities and life insurance policies. Hence it can also be considered an [insurance patent](#).

¹ With apologies to [Stanley Kubrick](#)

² SOGRAT is a [registered trademark](#) of the [Wealth Transfer Group](#).

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

Step 1: Read the patent

The specification of the SOGRAT patent discloses a method for passing stock options on to heirs using an annuity. This method has the potential for being tax efficient based on the IRS's current interpretation of gift tax regulations. The basic idea is that a donor funds a [Grantor Retained Annuity Trust](#) (or GRAT) with a combination of cash and stock options. The donor puts enough cash into the trust so that the initial annuity payments can be made with the cash and the stock options can remain in the trust for as long as possible. When the cash is used up, the remaining annuity payments are made with a portion of the stock options. Hopefully the stock options will have increased in value so that when the trust matures, there are stock options remaining which can be passed onto the beneficiary. The beneficiary is a family member of the donor. If the donor dies prior to the maturity date of the trust, then the assets are passed on to the beneficiary at that time.

The annuity payments are selected when the fund is established so that the cumulative value of said payments is equal to the calculated value of the stock options at trust inception plus the cash contribution at trust inception plus the anticipated earnings of the trust based on an assumed interest rate. The assumed interest rate is set equal to the federal midterm rate plus ½% at the time the fund is established. Thus, from the standpoint of the IRS, the future value of the trust at maturity is zero. The gift tax of the trust therefore is also zero. If the stock options in the SOGRAT appreciate faster than the assumed interest rate, then the assets of the trust will be positive at the end of the term and these are passed on to the beneficiary without being assessed a gift tax.

In order to determine the number of stock options that must be paid to the donor at each annuity payment, the stock options are valued "as each annuity payment is made".

Step 2: Analyze the claims to identify steps of each independent claim that can potentially be eliminated or changed.

A patent covers only what is in the claims.³ In order to infringe a claim the infringer must (if it is a method claim) perform all of the steps in the claim. If just one step is left out, the claim is not infringed. If none of the claims are infringed then the patent is not infringed.

There are two types of claims in a patent, independent and dependent. Independent claims stand on their own. Dependent claims "depend" upon earlier independent claims. Each dependent

³ Claims are numbered one sentence descriptions of the invention or inventions that a patent holder has exclusionary rights to. They are normally found as a list at the end of a US patent.

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

claim refers to at least one independent claim and incorporates all of the independent claim's steps into it.

In designing around a patent, you only have to focus on the independent claims. If you don't infringe any of the independent claims, you won't infringe any of the dependent claims.

Claim 1 of the SOGRAT patent is an independent claim. It reads:

1. A method for minimizing transfer tax liability of a grantor for the transfer of the value of nonqualified stock options to a family member grantee, the stock options having a stated exercise price and a stated period of exercise, the method performed at least in part within a signal processing device and comprising:
 - a. establishing a Grantor Retained Annuity Trust (GRAT);
 - b. funding said GRAT with assets comprising stock options, the stock options having a determined value at the time the transfer is made;
 - c. setting a term for said GRAT and a schedule and amount of annuity payments to be made from said GRAT; and
 - d. performing a valuation of the stock options as each annuity payment is made and determining the number of stock options to include in the annuity payment.

In order to design around this claim, one needs to find a way to either eliminate one of these steps or substitute a different step for one of these steps without unduly sacrificing the benefits of the invention. The critical skills are both technical (How can we do this?) and legal (How can we be sure we did this?).

It is essential to determine exactly what each word and phrase in a claim means in order to design around it. An inventor may give a word or phrase a particular meanings in the specification⁴ of the patent. If no meaning is given in the specification, then courts will give a word or phrase the meaning that is commonly used among professionals of ordinary skill in the art of the invention.

Consider step (d) of claim 1:

- d. performing a valuation of the stock options **as each annuity payment is made** and determining the number of stock options to include in the annuity payment. (emphasis added)

⁴ The specification of a patent is a written description of how to make and use the invention. It may include figures, tables, equations and text.

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

What does the phrase “as each annuity payment is made” mean? It’s not defined or used in the specification so that means we have to rely on the definition of those of ordinary skill in the art. An informal poll among members of the AICPA⁵ indicated that, at least for some accountants specializing in estate tax planning, “as each annuity payment is made”, means up to two months prior to said annuity payment being made. For the sake of this discussion, let’s accept that definition.

Step 3: Propose a way to eliminate or change said steps to create a new non-infringing invention.

Is there an acceptable or even beneficial way to manage a SOGRAT that it doesn’t involve performing a valuation of the stock options “as each annuity payment is made”? We leave that question to the inventiveness and creativity of our readers. But if someone does invent a way and if that way does not unduly sacrifice the benefits of a SOGRAT, then a new, potentially non infringing design around would have been made.

Let’s assume that a new method for managing a SOGRAT has been invented and doesn’t require step (d). If this new method is practical, and if the new method stands up to legal scrutiny, then at least claim 1 of the SOGRAT patent will have been designed around. This step must then be repeated for all of the other independent claims of the patent.

Fortunately for this example, all of the independent claims of the SOGRAT patent have the equivalent of step (d). If the design around for step (d) works for claim 1, then the design around for step (d) may work for the other independent claims as well.

Step 4: Verify that the non-infringing invention does not, in fact, infringe the patent.

In order to determine if the new invention doesn’t infringe the existing claims of a given patent, it’s necessary to get a legal “infringement opinion”. An experienced patent attorney⁶ is presented with the proposed new invention and a copy of the patent that is being designed around. The attorney is then asked, “Does this new invention infringe the patent?” The patent attorney will then study both the invention and the patent and supply an infringement opinion. If the infringement opinion says “yes, it does infringe” then it’s back to the drawing board. If the opinion says “no, it doesn’t infringe”, then it’s clear sailing.

⁵ American Institute of Certified Public Accounts

⁶ Only an attorney can provide an infringement opinion. A patent agent cannot. The reason is that the attorney will be opining on what the outcome of a lawsuit in Federal District Court would be. Patent agents can only give opinions on what the outcome of a proceeding before the USPTO would be.

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

Chances are, however, the infringement opinion will say “it depends”. The opinion will lay out certain interpretations of the claims that could “read on” the new invention (and hence infringe the patent). It will also give an assessment of the likelihood of a jury in a patent trial accepting these interpretations and may discuss counter arguments that could be presented to show that the new invention does not infringe.

It is then up to the appropriate business manager to make the decision of whether or not the risk of provoking a patent infringement lawsuit is worth the reward of bringing the new, presumably non infringing invention to market. For example, if the design around relied on valuations being done three months before each annuity payment is made instead of up to two months, then the likelihood of provoking a patent infringement lawsuit might still be high and the risk might not be worth the reward. If, on the other hand, the design around relied on valuations being done more than a year before each annuity payment is made then the likelihood of provoking a patent infringement lawsuit could be much lower and the risk might then be worth the reward.

Step 5: File a patent application on the new invention.

If the design around is a new invention in and of itself, then it should be considered for patent protection. It’s quite possible that the design around has important benefits that the earlier patented invention does not have. These benefits could lead to an even larger market for the design around than for the earlier invention. With a patent in hand, the inventor can protect the new intellectual property he or she has created.

If the design around still might be considered to infringe the threatening patent, then having a patent on it may allow both parties to cross license their patents to each other. They then can bring their respective products to market to the exclusion of other competitors. Thomas Edison did this with his light bulb patent. Both he and his arch rival [Joseph Swan](#) were locked in a fierce patent battle over who invented the light bulb. Edison’s original patent covered a method for making the light bulb filament. Swan’s original patent, filed only five months later, covered how to make an air tight seal around the wires that went into the bulb. Both inventions were important for making practical light bulbs. Eventually Edison and Swan settled their dispute by cross-licensing their respective patents to each other. They then formed a joint venture to bring their light bulbs to market. If either one hadn’t patented his invention, they might not have been able to form the joint venture.

Conclusion:

The ability to design around a patent is a critical skill in any industry where patented inventions are made, used or sold. A design around is performed by reading the threatening patent, analyzing the claims, finding one or more steps of each claim that can be eliminated or modified,

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

inventing an alternative step, getting a legal opinion to make sure that the new alternative does not infringe, and, optionally, filing a patent application on the new alternative. Even patents as seemingly formidable as the SOGRAT patent may be vulnerable to a design around. Design arounds can lead to better inventions, the avoidance of future lawsuits and the establishment of very profitable cross licenses or joint ventures.

Meeting Announcement

A session on new patented or patent pending retirement income products has been added to the upcoming RIIA meeting, [Managing Retirement Income Conference](#), to be held at the Doral Resort Golf Resort and Spa in Miami Florida, **February 13 – 18, 2008**. Mark Nowotarski will be hosting a panel of inventors and IP attorneys who will discuss the challenges and successes they've had in bringing new retirement income inventions to market. Q&A will follow.

The panelists include:

- Chuck Robinson, SVP Investment Products & Services, Northwestern Mutual Life Insurance Company
- John Bevacqua, Principal Deloitte Consulting
- Matt Schoen, Managing Principal, Private Placement Insurance Products, LLC
- Matthew Reece, Counsel Pepe & Hazard LLP.

Information and Registration can be found at:

<http://www.iirusa.com/retirement/eventhome/35279.xml>

To obtain a “moderator referral” discount, please contact Mark Nowotarski at (203) 975-7678.

Patent Q & A

Patent Reform Act of 2007

Question: What's happening with the Patent Reform Act of 2007?

Disclaimer: *The answer below is a discussion of typical practices and is not to be construed as legal advice of any kind. Readers are encouraged to consult with qualified counsel to answer their personal legal questions.*

Answer: Well, not much right now but there are some significant changes proposed and it is worth paying attention to.

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

Details: Here's what's happened. The Patent Reform Act of 2007 was introduced into the House (H.R. 1908) and the Senate (S.1145) on April 18, 2007. The House version passed on September 7, 2007. The Senate version, which was identical when introduced, is awaiting action. The Senate bill has been reported out of the Senate Judiciary Committee with some changes. Further action in the Senate is expected in early January, 2008.

Both the House and Senate versions have been amended identically to make "tax planning inventions" *unpatentable subject matter*. See the Senate version of this amendment at: [S 2369](#).

Per the amendment a "tax planning invention" means "a plan, strategy, technique, scheme, process, or system that is designed to reduce, minimize, avoid, or defer, or has, when implemented, the effect of reducing, minimizing, avoiding, or deferring, a taxpayer's tax liability ..." The amendment specifically excludes tax preparation software or other tools used solely to prepare tax returns.

Of course, the definition, even though it may seem precise, is broad enough under some interpretations to include any process involving insurance since life and annuity insurance products enjoy a tax deferral advantage. It is expected that some work will need to be done on the language to focus in on only the SOGRAT type patents (see the feature article) which are, apparently, the intended target of this amendment.

In addition, the Internal Revenue Service has [published regulations](#) that will add "patented transactions" to the category of reportable transactions. The definition of a "patented transaction" is "a transaction for which a taxpayer pays (directly or indirectly) a fee in any amount to a patent holder or the patent holder's agent for the legal right to use a tax planning method that the taxpayer knows or has reason to know is the subject of the patent." This regulation also specifically excludes patented tax preparation software. It may, however, be interpreted broadly enough to include patented insurance design concepts which only incidentally have the effect of reducing or deferring taxes because they inherit the tax deferral advantage enjoyed by all life and annuity insurance products.

See the [June 15, 2007](#) issue of the Insurance IP Bulletin for a summary of other patent reforms in the Patent Reform Act of 2007.

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

Statistics

An Update on Current Patent Activity

The table below provides the latest statistics in overall class 705 and subclass 4. The data shows issued patents and published patent applications for this class and subclass.

Issued Patents as of 12/25/07		
	Class 705	Subclass 4
YEAR	#	#
2007	2,062	43
2006	2,223	44
2005	1,453	30
2004	998	23
2003	969	21
2002	887	15
2001	880	19
2000	1,062	29
1999	1,005	36
1998	745	20
1978-1997	2,778	47
1976-1977	80	0
TOTAL	15,142	327

Published Patent <u>Applications</u> as of 12/27/07		
	Class 705	Subclass 4
YEAR	#	#
2007	6,989	183
2006	6,115	169
2005	6,300	148
2004	5,590	156
2003	6,009	128
2002	6,135	164
2001	1,326	30
TOTAL	38,464	978

Class 705 is defined as: DATA PROCESSING: FINANCIAL, BUSINESS PRACTICE, MANAGEMENT, OR COST/PRICE DETERMINATION.

Subclass 4 is used to identify claims in class 705 which are related to: *Insurance* (e.g., computer implemented system or method for writing insurance policy, processing insurance claim, etc.).

Issued Patents

A total of 43 patents have been issued in class 705/4 in 2007- only one short of the 44 issued during 2006.

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

Patents are categorized based on their claims. Some of these newly issued patents, therefore, may have only a slight link to insurance based on only one or a small number of the claims therein.

The [Resources](#) section provides a link to a detailed list of these newly issued patents.

Published Patent Applications

A total of 183 patent applications were published during 2007 class 705/4 indicating a continued high level of patent activity in the insurance industry.

The [Resources](#) section provides a link to a detailed list of these newly published patent applications.

A Continuing reminder -

Patent applications have been published 18 months after their filing date only since March 15, 2001. Therefore, there are many pending applications that are not yet published. A conservative estimate would be that there are, currently, close to 250 new patent applications filed every 18 months in class 705/4.

The published patent applications included in the table above are not reduced when applications are either issued as patents or abandoned. Therefore, the table only gives an indication of the number of patent applications currently pending.

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

Resources

Recently published U.S. Patents and U.S. Patent Applications with claims in class 705/4.

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

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

United States Patent and Trademark Office (USPTO): *Patent Application Information Retrieval* - <http://portal.uspto.gov/external/portal/pair>

Free Patents Online - <http://www.freepatentsonline.com/>

Provides free patent searching, with pdf downloading, search management functions, collaborative document folders, etc.

US Patent Search - <http://www.us-patent-search.com/>

Offers downloads of full pdf and tiff patents and patent applications free

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

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

Here is how to call the USPTO Inventors Assistance Center:

- Dial the USPTO's main number, 1 (800) 786-9199.
- At the first prompt press 2.
- At the second prompt press 4.
- You will then be connected to an operator.
- Ask to be connected to the Inventors Assistance Center.
- You will then listen to a prerecorded message before being connected to a person who can help you.

The following links will take you to the authors' websites

Mark Nowotarski - Patent Agent services – <http://www.marketsandpatents.com/>

Tom Bakos, FSA, MAAA - Actuarial services – <http://www.BakosEnterprises.com>