

**PROVING DIRECT INFRINGEMENT OF
SOFTWARE AND BUSINESS METHOD PATENT CLAIMS
INVOLVING MULTIPLE ACTORS**

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INTRODUCTION: This paper has been created for the Intellectual Property Owners Association Software and Business Methods Committee to provide background to IPO members regarding litigating software and business method patents. It should not be construed as providing legal advice or as representing the views of IPO.

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In order to prove infringement under any theory permitted by 35 U.S.C. § 271, the patentee must prove direct infringement. *Dynacore Holdings Corp. v. U.S. Philips Corp.*, 363 F.3d 1263, 1272 (Fed. Cir. 2004). This typically requires a showing that *a single entity* practices each and every step or element of the claimed method or apparatus. *BMC Resources, Inc. v. Paymentech, L.P.*, 498 F.3d 1373, 1380 (Fed. Cir. 2007) (*citing Warner-Jenkinson Co., Inc. v. Hilton Davis Corp.*, 520 U.S. 17, 40 (1997)). Therefore, even though 35 U.S.C. § 271(b) and (c) allow a patentee to recover from a party that is an indirect infringer if that party supplied a material portion of the patented invention or induced infringement, typically the patentee must still prove that a single entity directly infringes. Software and business method patents pose a special problem in this regard because a method or process patent can often be practiced without any single entity performing each of the steps necessary to completely practice the claim.

A. THE *BMC RESOURCES* STANDARD FOR JOINT INFRINGEMENT

The Federal Circuit recently addressed this issue in *BMC Resources*. BMC's patents involved a business method for debit bill payment involving the combined action of four participants. *BMC Resources*, 498 F.3d at 1375. Paymentech was granted summary judgment of non-infringement by the district court because it was only one of the four necessary participants in the claimed method, and therefore could not be a direct infringer. The Federal Circuit affirmed the grant of summary judgment. Although the Court took note of a potential "loophole" that would permit a party to avoid liability by "having a third party carry out one or more of the claimed steps on its behalf," it dismissed this concern in view of case law imposing "vicarious liability" on a party for the acts of another where the circumstances show that the liable party

was the “mastermind” and “controlled the conduct of the acting party.” *Id.* at 1379, 1381. The Court therefore adopted a standard “requiring control or direction for a finding of joint infringement.” *Id.* at 1381. The Federal Circuit recognized that the “control or direction” standard it was adopting might allow parties “to enter into arms-length agreements to avoid infringement,” but reasoned that “expanding the rules of direct infringement to reach independent conduct of multiple actors would subvert the statutory scheme for direct infringement.” *Id.* at 1381.

In applying the standard to the facts in the case, the Court held that BMC Resources’ proffered evidence that Paymentech had “some relationship” with, and provided data to, the debit networks, without any evidence that Paymentech also provided “instructions or directions regarding the use of those data,” was inadequate to create a genuine issue of fact as to whether Paymentech “controls or directs the activity of the debit networks” *Id.* The Court further noted that the evidence regarding Paymentech’s “direction or control” of the accused financial institutions “was even scarcer” as there was no evidence “even of a contractual relationship” between Paymentech and those financial institutions. *Id.* at 1382.

The *BMC Resources* opinion clearly establishes that, on the one hand, a party cannot avoid infringement “simply by contracting out steps of a patented process to another entity” but that, on the other hand, “independent conduct of multiple actors” via “arms-length cooperation” will not support an infringement claim. *Id.* at 1381. However, the Federal Circuit left for subsequent courts to determine what types of conduct falling between those two ends of the liability spectrum would constitute “direction or control” sufficient to establish liability for joint-direct infringement.

B. SUBSEQUENT APPLICATION OF THE *BMC RESOURCES* STANDARD

In *Gammino v. Cellco Partnership*, a payphone operator, which purchased telephone services from local service providers, was accused of infringing patents for an international call blocking process. 527 F. Supp. 2d 395 (E.D. Pa. 2007). The asserted claim required performance of a step that the un rebutted evidence showed was performed, if at all, by the local providers -- not the payphone operator. While the payphone operator did have a contractual relationship with the local service providers, there was no evidence that the operator knew of the providers' methods for blocking international calls. *Id.* at 398. The district court granted summary judgment of no direct infringement because, in its view, the payphone operator could not have "controlled" the local providers if it "did not even know the providers' methods." *Id.*

In *TGIP, Inc. v. AT&T Corp.*, TGIP alleged that AT&T was infringing two patents related to activation and use of prepaid calling cards. 527 F. Supp. 2d 561 (E.D. Tex. 2007). AT&T moved for judgment as a matter of law on the basis that other entities provided the activation platform and unaffiliated retailers provided the data terminals, both of which performed steps necessary to the infringement of the patents. *Id.* at 577. The Court denied the motion because TGIP presented sufficient evidence to survive summary judgment by showing that the third parties providing the activation platforms "acted on behalf of AT&T" and that AT&T "provided specifications to each of its retailers directing the retailers on the processes for sending an activation message to AT&T," including a required message format "necessary in order for AT&T to provide its services to retailers." *Id.* at 578.

In *Zinus, Inc. v. Simmons Bedding Co.*, the patents at issue were directed to a method for packaging a mattress in a containment sleeve. No. C-07-3012 PVT, 2008 WL 682858 (N.D. Cal. Mar. 11, 2008). The defendant allegedly practiced all of the steps of the patented process with the exception of the last two, which entailed "removing" a mattress from a containment sleeve

and “allowing” it to return to an uncompressed state -- steps carried out by the customer after the product was purchased. *Id.* at *3. Purportedly applying the test from *BMC Resources*, the district court equated the “control” test to traditional causation. According to the Court: “An accused infringer may be found to have ‘caused to be performed’ a step of the patented method, the other steps of which it has itself performed, where it provided the third party with instructions or directions regarding how to perform the missing step.” *Id.* at *2. The Court therefore denied defendant’s motion for summary judgment, concluding that the jury could find, based on the instructions provided by the defendant, that the defendant had caused to be performed the final steps of the method. *Id.* at *4.

C. *MUNIAUCTION* FURTHER LIMITS THE “CONTROL OR DIRECTION” TEST

The Federal Circuit spoke again on the joint-direct infringement test in *Muniauction, Inc. v. Thomson Corp.*, 532 F.3d 1318 (Fed. Cir. 2008). The patent at issue involved a method for an electronic auction, the first step of which was performed by a bidder while the remainder of the steps were carried out by an auctioneer system. *Id.* at 1328-29. At the conclusion of trial, the district court gave the jury an instruction regarding joint infringement that asked the jury to consider whether there was “one party teaching, instructing, or facilitating the other party’s participation in the electronic auction process.” *Id.* at 1329. The jury thereafter returned a verdict of infringement against the auctioneer-defendant. The Federal Circuit, applying the test from *BMC Resources*, reversed. The Court first held that “none of the questions identified by the jury instruction are relevant to whether [defendant] satisfies the ‘control or direction’ standard.” *Id.* at 1330. It held that the auctioneer’s controlling access to its system and instructing bidders on use of its system, including how to perform the initial step of the claimed method, “is not sufficient to incur liability for direct infringement.” *Id.* The Court went on to note that the

defendant “neither performed every step of the claimed methods nor had another party perform steps on its behalf” and there was no identified legal theory “under which [defendant] might be vicariously liable for the actions of the bidders.” *Id.*

The Federal Circuit’s holding in *Muniauction* appears to make it more difficult for patentees to prove infringement by joint activity. Arguably most surprising is the Court’s statement that “instructing” another party regarding their activities is not “relevant” to the control or direction test. It therefore appears that patentees must now prove that the “mastermind” of the infringing activities arranged for the other actor or actors to perform the claimed steps “on its behalf” or is otherwise vicariously liable for the actions of the other actors. Notably, this modified test calls into question the results in *TGIP* and *Zinus*, because in neither case were all of the other necessary actors (*i.e.* the retailers in *TGIP* and the customers in *Zinus*) performing steps “on behalf of” the accused “mastermind,” and the courts in both cases improperly (in retrospect) relied on “instructions” provided by the alleged mastermind to the other actors as evidence of “control or direction.”

D. SUBSEQUENT TREATMENT OF *MUNIAUCTION* IN THE DISTRICT COURTS

In *Global Patent Holdings LLC v. Panthers BRHC LLC*, the district court relied on *Muniauction* to grant defendant’s motion to dismiss plaintiff’s complaint at the pleading stage. No. 08 -80013-CIV, 2008 WL 3833219 (S.D. Fla. Aug. 13, 2008). The asserted claim entailed a method of interacting with a remote web-server, and required the joint action of a website-operator and users visiting the website. Plaintiff alleged that defendant exerted the necessary control because its website stored HTML and Javascript code that, when transmitted to and executed on the user’s computers, necessarily practiced the claim. *Id.* at *1. The district court, after analyzing the Federal Circuit’s holding in *BMC Resources* and *Muniauction*, concluded that

to attribute the actions of third parties to the defendant, those parties “must perform the steps of the patented process by virtue of a contractual obligation or other relationship that gives rise to vicarious liability.” *Id.* at *3. On the facts alleged, the Court concluded that because there would be no infringement if no user ever visited defendant’s website, and because there was no allegation that the users were “contractually bound” to visit defendant’s website or were defendant’s “agents,” the users could not be acting under the “direction or control” of the defendant as a matter of law. *Id.* Notably, had these allegations been evaluated against the “causation” test articulated in *Zinus*, the result would likely have been quite different, because plaintiff alleged that defendant’s activities (generating and transmitting code to users) caused the asserted claim to be practiced, without further intervention of the users.

In *Emtel, Inc. v. Lipidlabs, Inc.*, the district court granted defendant’s motion for summary judgment of non-infringement. 583 F.Supp.2d 811, 814-815 (S.D. Tex. 2008). The patent at issue required the joint action of a videoconference operator and physicians or other medial personnel. Although the defendant (the videoconference operator) did have a contractual relationship with the physicians related to the use of the videoconference system, the district court concluded that the contractual relationship did not rise to the level that the defendant could be said to have controlled the physicians in their “performance of the infringing steps” so that the physicians were carrying out those steps “as the defendant’s agent.” *Id.* at 839.

The result in one other post-*Muniauction* district court case is not as bleak for software and business method patentees. In *Rowe Int’l Corp. v. Ecast, Inc.*, No. 06 C 2703, 2008 WL 4133516, at *2 (N.D. Ill. Aug. 25, 2008), the Court found that there was evidence that defendant had sufficient contacts with the other necessary joint-actors to raise a genuine issue of fact as to whether defendant controlled or directed those entities’ activities. In that case, there was some

evidence that the various actors considered themselves “partners” in manufacturing and selling the patented invention. *Id.* at *4.

**E. THE IMPORTANCE OF PROPER METHOD CLAIM DRAFTING
FOLLOWING *BMC RESOURCES* AND *MUNIAUCTION***

The Federal Circuit’s rulings in *BMC Resources* and *Muniauction* make the patentee’s task of proving infringement of a method claim challenging. However, the courts have noted that this problem can be addressed by the patent draftsman. As the *BMC Resources* opinion notes: “[t]he concerns over a party avoiding infringement by arms-length cooperation can usually be offset by proper claim drafting. A patentee can usually structure a claim to capture infringement by a single party.” *BMC Resources*, 498 F.3d at 1381. Indeed, the defendant in the *Emtel* case made a point of showing the court how the patentee could have drafted its claim to solely cover the defendant’s activities. *Emtel*, 583 F.Supp.2d at 840. This argument was referred to by the Court in its opinion, and likely helped convince the Court that the result of dismissal was not an inequitable one. *Id.* Accordingly, when drafting software/business method patent claims, the draftsman should ensure the claim will read on the activities of only a single infringing entity whenever possible. On the other hand, when accused of infringement of a software/business method patent, the defendant should carefully investigate whether it practices all of the elements of the claim, or whether instead an entity outside its “direction or control” (such as a downstream entity) actually performs at least one of the claimed steps.