

2. Patent No. 5,970,479 (“the ’479 patent”) is entitled “Methods and Apparatus Relating to the Formulation and Trading of Risk Management Contracts.” (*See Answer and Countercl., Countercl. ¶¶ 21, 42; Ex. 1, ’479 patent.*)¹

3. The application that led to the ’479 patent was filed on May 28, 1993, and the patent issued on October 19, 1999. (*See Ex. 1, ’479 patent.*)

4. In this litigation, Alice is only asserting claims 33 and 34 of the ’479 patent, which are the only claims of that patent directed to the exchange of an obligation. (Docket No. 27 Alice Mem. 4-5; Ex. 1, ’479 patent, claims 33-34.)

5. Patent No. 6,912,510 (“the ’510 patent”) is entitled “Methods of Exchanging an Obligation.” (*See Answer and Countercl., Countercl. ¶¶ 28, 49; Ex. 2, ’510 patent.*)

6. The application that led to the ’510 patent was filed on May 9, 2000, and the patent issued on June 28, 2005. (*See Ex. 2, ’510 patent.*)

7. Patent No. 7,149,720 (“the ’720 patent”) is entitled “Systems for Exchanging an Obligation.” (*See Answer and Countercl., Countercl. ¶¶ 35, 56; Ex. 3, ’720 patent.*)

8. The application that led to the ’720 patent was filed on December 31, 2002, and the patent issued on December 12, 2006. (*See Ex. 3, ’720 patent.*)

9. Claims 33 and 34 of the ’479 patent, and claims 1-75 of the ’510 patent, claim purported methods for exchanging an obligation between parties to a transaction. (*See Ex. 10, Hughes Decl. ¶¶ 27-30; Ex. 1, ’479 patent, claims 33, 34; Ex. 2, ’510 patent, claims 1-84.*)

10. Claims 1-84 of the ’720 patent claim “data processing” systems for exchanging an obligation. (*See Ex. 10, Hughes Decl. ¶¶ 27-30; Ex. 3, ’720 patent, claim 1-84.*)

¹ “Ex. __” is used herein to refer to the exhibits to the Declaration of Abigail Langsam, submitted herewith.

11. In a memorandum to the Court dated May 19, 2008, (the “Alice Mem.”), Alice summarized the inventions claimed in its patents as follows:

Mr. Shepherd conceived an electronic settlement mechanism capable of allowing parties to exchange obligations in a risk-free manner because both sides of a trade would be settled simultaneously and irrevocably—removing the risk that one party would perform and the other abscond.

(Alice Mem., at 4-5.)

12. In the Alice Mem., Alice summarized the ’479, ’510 and ’720 patents as follows:

Mr. Shepherd pursued a range of patents for methods and systems in both trading and settlement, including U.S. Patent Nos. 5,970,479 (“the ’479 Patent”), 6,912,510 (“the ’510 Patent”) and 7,149,720 (“the ’720 Patent”) and commenced development of the software and business processes for commercializing his inventions in the early 1990s. Two of these patents (the ’510 and ’720 patents), which are now held by Alice (a corporation in which Mr. Shepherd has an indirect 50% interest), describe a method and system for exchanging obligations between parties . . .

(Alice Mem., at 5.)

13. In the Alice Mem., Alice summarized the inventions claimed in its patents as follows:

A simplified example illustrates how use of Mr. Shepherd’s invention overcomes foreign currency exchange settlement risk. Assume a bank in the United States wants to exchange \$1,000,000 with a bank in Japan for an equivalent amount of Yen. Traditionally, this exchange was fraught with risk because the exchange involved two independent payments that did not occur simultaneously. The U.S. bank would have to send \$1,000,000 to the Japanese bank’s U.S. branch or agent (called a nostro agent), and the Japanese bank would send the Yen to the U.S. Bank’s Japanese branch or agent. However, the exchange could not occur simultaneously because they involved different central banks in different time zones (transfers of funds between banks are legally final and irrevocable when the funds are transferred by a country’s central bank); the two payments that comprise the exchange were thus independent. If the Japanese bank paid first in this example (as is typically the case because Japan is approximately twelve hours “ahead” of the U.S. based on time zones), it had no guarantee that the U.S. bank would have the means to honor its commitment and pay the \$1,000,000. Should the U.S. bank become insolvent before paying, the Japanese bank would lose the Yen equivalent of \$1,000,000 it had paid. This risk is commonly referred to as “Herstatt risk,” named after the German bank Herstatt, which became insolvent in

1974 and, through its agents, failed to pay the U.S. dollar side of foreign currency exchanges it had agreed to pay after having received its counterparties' money.

(Alice Mem., at 5-6.)

14. In the Alice Mem., Alice stated the following with respect to the invention claimed in the '479, '510 and '720 patents:

In the Shepherd invention, the key to eliminating the risk is creating a supervisory institution to execute the payments between the parties, by maintaining an account for each party (*i.e.*, bank) that is independent of the parties' own central bank accounts.

(Alice Mem., at 6.)

15. In the Alice Mem., Alice summarized the inventions claimed in its patents using the following example:

[S]uppose CitiBank ("Citi") maintains an account with the FRBNY and Mizuho Corporate Bank ("Mizuho") maintains an account with the Bank of Japan. Both central banks are referred to in Alice's patent claims as "exchange institutions." Citi and Mizuho also have multi-currency accounts with the supervisory institution ("SI accounts").

The supervisory institution waits for a transaction to be received (*i.e.*, Citi wants to exchange \$1,000,000 for an equivalent amount of Yen from Mizuho). After ensuring that the parties have adequate value in their respective SI accounts, the supervisory institution adjusts these accounts to reflect the exchange. It then instructs the exchange institutions (*i.e.*, the central banks) to adjust Citi's and Mizuho's central bank accounts, respectively, in accordance with the adjustment made to the SI accounts it maintains. Most importantly, the adjustment of Citi's and Mizuho's accounts at the supervisory institution and the instruction from the supervisory institution to the FRBNY and the Bank of Japan are irrevocable and the instruction, once received, must be honored by both central banks. In this manner, the exchange occurs simultaneously and cannot be undone by either party. As a result, if Citi were to go bankrupt after the SI accounts were adjusted, Mizuho would still receive payment because the transaction is irrevocable.

(Alice Memo., at 7.)

16. All of the Alice patent claims at issue in this litigation require that "accounts" or "shadow records" are maintained by an entity or system separate from accounts or records

maintained by another entity. (*See* Ex. 1, '479 patent, claim 33; Ex. 2, '510 patent, claims 1, 27, 61, 65, 68; Ex. 3, '720 patent, claims 1, 28, 60, 68, 80.)

17. All of the Alice patent claims at issue in this litigation require that information about a transaction or exchange obligation is received by the entity or system that maintains the accounts/shadow records. (*See* Ex. 1, '479 patent, claim 33; Ex. 2, '510 patent, claims 1, 27 61, 65, 68; Ex. 3, '720 patent, claims 1, 28, 60, 68, 80.)

18. All of the Alice patent claims at issue in this litigation require the accounts/shadow records to be mathematically tested in light of the transaction and adjusted according to an algorithm. (*See* Ex. 1, '479 patent, claim 33; Ex. 2, '510 patent, claims 1, 27 61, 65, 68; Ex. 3, '720 patent, claims 1, 28, 60, 68, 80.)

19. All of the Alice patent claims at issue in this litigation require an "instruction" to be generated or provided to adjust the accounts or records at another institution according to the adjustment of the accounts/shadow records, where the instruction is an "irrevocable, time-invariant obligation" on the other institution. (*See* Ex. 1, '479 patent, claim 33; Ex. 2, '510 patent, claims 1, 27 61, 65, 68; Ex. 3, '720 patent, claims 1, 28, 60, 64, 68, 80.)

20. During prosecution of the application that led to the '510 patent, the U.S. Patent Office ("PTO") found that there was no patentable distinction between claim 33 of the '479 patent and the independent claims of the application, and rejected the independent claims under the doctrine of double patenting. (*See* Ex. 4, Office Action, dated Sept. 3, 2003 at 5-6.)

21. Alice did not object to the PTO examiner's double patenting rejection, and instead executed a "terminal disclaimer" agreeing that the claims of the '510 patent would expire at the same time as those of the '479 patent. (Ex. 5, Amendment and Reply Under 37 C.F.R. § 1.111, dated October 31, 2003.)

22. The word “electronically” was added to modify “adjusting” in each independent claim of the ’510 patent during prosecution of the application that led to the patent, when the examiner rejected the original claims after finding that they were “directed to non-statutory subject matter” under Section 101 because they “lack[ed] any specific technology.” (Ex. 4, Office Action, dated September 3, 2003 at 3).

23. In a subsequent interview with the patentee, the examiner stated that the independent claims of the ’510 patent were “directed to an abstract idea and were therefore unpatentable.” (Ex. 5, Amendment and Reply Under 37 C.F.R. § 1.111, dated October 31, 2003 at 22.)

24. The examiner allowed the independent claims of the ’510 patent after the patentee agreed to add the word “electronically,” because he believed that the use of this term would bring the claims within the “‘technological’ arts.” (Ex. 5, Amendment and Reply Under 37 C.F.R. § 1.111, dated October 31, 2003 at 22.)

25. The ’720 patent differs from the ’479 and ’510 patents in that each of its independent claims is expressly directed to a “data processing system” comprised of “a data storage unit” and “a computer coupled to said data storage unit.” (*See* Ex. 3, ’720 patent at claims 1, 28, 60, 64, 68 and 80.)

26. In claim 68 of the ’720 patent (*see* Table 1) the “data storage unit” stores “information about a first account for a first party, independent from a second account maintained by a first exchange institution.” (*See* Ex. 3, ’720 patent at claim 68.)

27. The “computer, coupled to said data storage unit” is configured to carry out the method claimed in claim 68 of the ’510 patent. (*See* Ex. 3, ’720 patent at claim 68.)

28. Claim 1 of the '720 patent claims a data processing system configured to perform the method of claim 1 of the '510 patent. (*See* Ex. 3, '720 patent at claim 1; Ex. 2, '510 patent at claim 1.)

29. The systems of claim 1, 28, 60 and 68 of the '720 patent are configured to perform the methods of claim 1, 27, 61 and 68 of the '510 patent, respectively. (*See* Ex. 3, '720 patent at claims 1, 28, 60 and 68; Ex.2, '510 patent at claims 1, 27, 61 and 68.)

30. The systems of claim 64 and 80 of the '720 patent are configured to perform the method of claim 65 of the '510 patent. (*See* Ex. 3, '720 patent at claims 64, 80; Ex.2, '510 patent at claim 65.)

31. During prosecution of the '720 patent, the claims of the '720 patent were initially rejected for double patenting over each of the claims of the '510 patent. (Ex. 7, Office Action, dated Dec. 28, 2005 at 2.)

32. The Examiner stated, "Although the . . . claims are not identical [to those in the '510 patent], they are not patentably distinct . . . because [the claims of the '720 patent] are the same method for intended use as claims 1-75 of [the '510 patent]." (Ex. 7, Office Action, dated Dec. 28, 2005 at 2.)

33. The Examiner noted that "[t]he additional limitation disclose[d] by [the application that led to the '720 patent] is 'a data processing system and a data storage unit' while all the other limitations in [the application claims] are the same as claims 1-75 of [the '510 patent]." (Ex. 7, Office Action, dated Dec. 28, 2005 at 2.)

34. The claims were allowed only after Alice executed a terminal disclaimer so that the claims of the '720 patent would expire at the same time as those in the '510 patent. *See* Ex. 5,

Amendment and Reply Under 37 C.F.R. § 1.111, dated Jan. 27, 2006 at 50; Ex. 8, Terminal Disclaimer To Obviate A Double Patenting Rejection Over A Prior Patent, dated Jan. 27, 2006.

35. The three Alice patents, in addition to 12 independent claims, also include 149 independent claims. The dependent claims include the following limitations on the type of obligation or transaction on which the invention may be used, on the nature of the exchange institution, on the nature of the parties, on the “irrevocable, time-invariant” instruction, and on the type of data recorded in the account or shadow record.

	Dependent Claims		
	'479 Patent	'510 Patent	'720 Patent
Limitations on type of exchange “obligation” or “transaction”			
“arises out of” a “share price”		2	2
“arises out of” or “involves” a “weather event”		3, 41	3, 42
“arises out of” or “involves” a “market event”		4, 42	4, 43
“involves” the “transfer of shares in financial or physical assets”		5	5
“involves” a “wager”		6, 43	6, 44
“involves” the “transfer of a commodity”		7	7
“arises out of” or “involves” “money for goods, services, promises, credits or warrants”		8, 44	8, 45
“arises out of” or “involves” “currency”		18, 54, 72	18, 54, 70, 74
“arises out of” a “collateralization payment”		21, 40	21, 41
relates to “acquir[ing] an item from” another party”			27, 59, 67, 79, 84
Limitations on “irrevocable, time invariant” instruction			
“period of time” for which instruction is provided is a “part of a day”		9, 53, 67	9, 53, 66, 77
based on “netted” transactions	34	11, 52, 75	11, 55, 78
provided at “an end of a processing cycle”		64	63
“generated at the end of a day”			82
Limitations on algorithm or test for adjusting accounts or shadow records			
applied to transaction in “chronological order”		10, 62	10, 61
includes “debiting and/or crediting . . . shadow		39	40

record based on . . . transaction”			
includes obtaining a balance for shadow records from exchange institution		22, 48, 63, 66	22, 49, 62, 65, 81
“adequate value” requires that the first and third accounts have “a positive balance”		74	76
Limitations on the “exchange institution”			
“credit card company”		12, 45	12, 46
“debit card company”		13, 46	13, 47
“bank”		14, 55	14, 56
“central bank”		15, 56, 69	15, 57, 69
“guarantor”		16	16
“party offering credit”		17, 47	17, 48
exchange institutions operate in “different time zone[s]”		19, 25, 50, 59	19, 24, 51, 71
exchange institutions have “different account processing cycle[s]”		20, 26, 51, 57, 60	20, 25, 52, 58
“non-bank clearing house or depository”		23, 73	26, 75
supervisory institution and exchange institution “legally and/or geographically domiciled in different countries”		37	38
exchange institutions are different		24, 49, 58	23, 50
“first exchange institution and . . . second exchange institution are the same”		70	72
Limitations on the exchange institution “account” or “record”			
pertains to “shares in financial or physical assets”		28	29
pertains to “participation rights in wagers”		29	30
pertains to “goods”		30	31
pertains to “services”		31	32
pertains to “central bank exchange settlement account deposits”		32	33
pertains to “financial instrument deposits”		33	34
pertains to “credit extended to/from a party or to/from a guarantor”		34	35
includes an “overdraft or line-of-credit” with an exchange institution		35	36
“second account and . . . fourth account are the same account”		71	73
“first account holds funds for . . . first party and . . . second party”			83
Limitations on the “parties”			
“first party holds one or more accounts with more		36	37

than one exchange institution”			
one “party is a buyer” and the other “party is a seller”		38	39

(See Ex. 1, '479 patent at claim 34; Ex. 2, '510 patent at claims 2-26, 28-60, 62-64, 66-67, 69-75; Ex. 3, '720 patent at claims 2-27, 29-59, 61-63, 65-67, 69-79, 81-84.)

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Respectfully submitted,

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