

Patents: *Help or Hindrance?*

As I sat in the witness stand, I started to realize just how difficult my task had become. I had been hired by the defendant in a patent-infringement lawsuit to be the leading expert witness. It was a case involving a fairly basic online mortgage technology application. I assumed it was an easy case, as what was patented was so obvious to anyone “skilled in the art.” In other words, if you work in the mortgage technology field, you would have easily created a technology solution that this patent covered.

The jury endured two weeks of testimony. I had about eight hours of this time to persuade them that the patent in question was both invalid (because of obviousness and prior art) and didn’t apply to my clients’ technological solutions. I failed, and we failed, to do either.

The issue seemed so crystal-clear to me, but the opposing counsel performed an amazing feat of making it seem so complicated and unique. The jury found for the plaintiff on all counts, and then it really hit me about just how hard it is to educate a jury about mortgage technology.

We—the defendant, his legal team and myself—spent years preparing for this two-week trial. The very best law firms were hired, and probably millions of dollars were spent on the defense. I don’t think much more could have been done. When it comes to a jury understanding the complex world of mortgage technology, there really isn’t an easy way to educate them quickly enough. It was akin to rolling the dice to determine the winner. The verdict made me realize what a perilous world patent law is for our industry.

More recently, seven different financial industry trade groups (including the Mortgage Bankers Association [MBA]) called on Fannie Mae to abandon a recently obtained patent on mortgage technology. I have reviewed this patent myself, and can understand why Fannie Mae is being brought to task on this issue. The patent, U.S. Patent No. 7089503, was granted Aug. 8, 2006.

Its abstract describes the patent as: “A computerized mortgage loan system and process to enable borrowers to design mortgage loans that meet their particular individual needs and financial goals, and that can be adapted to fit changing needs and goals. . . . The loan requirements of the borrower are obtained and applied to a set of rules for combining loan product features. One or more loan recommendations are determined and presented to the borrower. The loan recommendations include customized combinations of loan features

decision and obtaining pricing from a lender. In my review of some of these patents, I would guess that many, if not most, online mortgage Web sites in use today violate at least one patent. Enforcement of such patents has been slow in coming, but already there are several lawsuits in the works. They typically start with the firms that have deeper pockets, but even small firms could soon be receiving “cease and desist” orders.

Think about what mortgage brokers have done for decades. They take an application,

There are a large number of firms within our industry that have obtained patents covering almost every conceivable area.

based on the loan requirements of the borrower and the rules.”

Many of us in the industry could see how even some of the existing systems could be described this way. Many of us might also feel that such a system would be an obvious advancement over most of the systems that exist today. Looking further out, it’s very conceivable that almost all future loans would be done this way. I remember talking with many lenders, long before the 2002 application date of this patent, about such a system.

It’s possible that Fannie Mae doesn’t plan to protect its patent or enforce royalty payments. However, if it desired, Fannie could force infringing systems to stop being used under the threat of a lawsuit.

And Fannie Mae is by no means alone in its quest for patents. There are a large number of firms within our industry that have obtained patents covering almost every conceivable area. For example, there are patents for taking an online loan application on the Internet, rendering a credit

obtain credit and other information, and then shop the loan among multiple lenders. It would be common sense, with the advent and growth of the Internet, to automate this process. Yet, there are patents that cover this very process. In my view, it doesn’t seem right that a patent could be granted for something so obvious. Many technology firms have built such a solution over the last 10 years, and they probably don’t realize that they could potentially be liable for a substantial sum in royalties.

In 1982, I founded Contour Software Inc., which for a number of years was viewed as the leading loan origination system by market share. Many of our products were innovative, and probably could have been patented. Contour was among the first to develop many innovations such as laser-printed mortgage forms, tracking systems, credit-report interfaces, production systems, online imaged loan files, PC-based fax systems, mortgage-related voice-response systems and so on.

We could have applied for 25 or more

patents, based on my understanding of the law, but chose not to. For me, so many of these innovations were obvious to one skilled in the art of mortgage technology. They are the natural evolution of systems and processes. As one system is developed and perfected, it naturally leads to a more

One problem with the way the system works is that although only the original inventor of an innovation should be entitled to a patent, in practice the first person to apply is sometimes granted a patent on a process that may have already been in use by others. Further, it is very

contingency basis. Thus, the patent holder has almost no risk in going to court. These law firms specialize in prosecuting patent infringers, and have become very adept at bringing a jury to their side.

For many mortgage technology firms, the cost to defend themselves against a patent-infringement case is astronomical. They could be forced to change their products and/or settle the case regardless of what's right or wrong on the merits.

Now, I'm not opposed to patents in general. If someone spends years coming up with a cure for a specific cancer, he or she should be able to earn profits through the sale of the resulting drug. However, in the mortgage technology industry and in all the patents I've reviewed, I've yet to find one that wasn't significantly obvious to one skilled in the art of mortgage technology.

The question I ponder is this: Is the patent process a help or a hindrance to our industry? Do we find that because of the patent process, mortgage technology firms invest more in their research and development (R&D)? I work with dozens of such firms in my consulting practice, and have not seen a firm that considers the ability to obtain a patent to be highly important to its success. Just as with Contour, I don't see firms that increase their investment in technology because the process can be patented.

What's important is that today's mortgage technology firms must be more aware than ever about current patents and how their solutions might infringe. Searching the U.S. Patent and Trademark Office Web site (www.uspto.gov/patft/index.html) for patents related to "mortgage loan application" currently yields 17 different patents. Many of us would be surprised by how many patents have already been granted around mortgage technology. It's also surprising to what degree they cover such basic solutions in our industry. My advice is this: Beware of getting caught in the trap of unintended patent infringement. What you don't know can end up hurting you.

Scott Cooley is an independent mortgage technology consultant, analyst and author based in Los Gatos, California. He can be found at www.scooley.com.

Some of the patent-related lawsuits come from failed dot-com companies where the patent is the only remaining asset.

advanced innovation. In fact, as I think of all the most advanced innovations in the industry, there were typically multiple companies developing them simultaneously.

In 1991, Contour developed what I believe was the first interface from a loan origination system (LOS) to a credit-reporting company, where the credit data would populate the loan application. If we had sought a patent on this invention, we likely could have earned a dollar or so for each credit report pulled in the industry even to the present day. Almost all credit-report data retrieved today are sent back to the LOS to populate the loan application.

As I look back, I lost out on earning potentially countless millions in royalty payments—and yet if I had done so it wouldn't have been good for anyone else. Further, such a patent would have enriched only me, and wouldn't have created more innovation. I would even argue that it would have hindered innovation among many firms, as such a feature became a building block to the automated underwriting systems in use today. I also could have used such a patent to hurt my competitors, which is often the reason that many apply for a patent in the first place. The industry is better off because of the invention and because it wasn't patented. No doubt though, others would have invented it shortly afterward if we hadn't. It was a common-sense advancement in origination technology.

difficult to challenge a patent once it is granted. For example, even though many firms developed online loan applications, only the first firm to file the patent would own it—that is, unless the process was described in an article or otherwise released publicly.

In my patent work, I researched hundreds of articles and found many that both described the patent in question and were published prior to the first patent-filing date. Typically, that would constitute prior art and invalidate the patent. The problem was that the articles must be very detailed—almost to the point of being a patent application. Few authors would ever write an article describing a technology in such a way that it could invalidate a future patent filing. The hurdle to jump is quite high.

Further, and more important, the jury has to believe that the articles describe the patent explicitly. In the case I was involved with, it seemed easy for the plaintiff's attorneys to explain how the article doesn't come close to describing the patent. For the nurse, homemaker, contractor and other jury members, it was "all Greek to them."

Some of the patent-related lawsuits come from failed dot-com companies where the patent is the only remaining asset. Others come from law firms that buy the patent as an asset. There are many law firms that will take a patent case on a