

**IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TEXAS
TYLER DIVISION**

H&R BLOCK TAX SERVICES, INC. ,

v.

**JACKSON HEWITT TAX
SERVICE, INC.**

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No. 6:08cv37 LED-JDL

JURY DEMANDED

**REPORT AND RECOMMENDATION OF
UNITED STATES MAGISTRATE JUDGE**

Before the Court is Defendant Jackson Hewitt Tax Service Inc.'s ("Jackson Hewitt") Motion for Summary Judgment of Invalidity of All Asserted Patent Claims (Doc. No. 53). A response and reply were filed (Doc. Nos. 65 & 68), as well as supplemental briefing from both parties (Doc. Nos. 84, 86, & 87).

The Court withdraws its previous Report and Recommendation ("R&R") (Doc. No. 108) in light of the Supreme Court's decision in *Bilski v. Kappos* and substitutes this R&R in its place. Upon review of the parties' arguments, objections to the prior R&R, and the Supreme Court's decision in *Bilski*, the Court **RECOMMENDS** that Jackson Hewitt's Summary Judgment of Invalidity of All Asserted Patent Claims (Doc. No. 53) be **GRANTED-IN-PART** and **DENIED-IN-PART**. The Court further **RECOMMENDS** that U.S. Patent No. 7,127,425 be found invalid.

BACKGROUND

On February 8, 2008, H&R Block filed suit against Jackson Hewitt, alleging infringement of U.S. Patent Nos. 7,072,862 ("the '862 patent") and 7,177,829 ("the '829 patent"). (Doc. No. 1). Jackson Hewitt subsequently counterclaimed, seeking declaratory judgments of non-infringement and invalidity of each patent. (Doc. No. 14). On November 14, 2008, Plaintiff amended its complaint to include U.S. Patent No. 7,127,425 ("the '425 patent") (Doc. No. 32), and Jackson

Hewitt again counterclaimed for declaratory judgments of non-infringement and invalidity (Doc. No. 47).

Prior to the Supreme Court's review of *In re Bilski*, 545 F.3d 943 (Fed. Cir. 2008), the Court issued two R&Rs regarding the validity of the patents at issue. (Doc. Nos. 108 & 113). On November 10, 2009, the Court issued a R&R recommending that Jackson Hewitt's Motion for Summary Judgment of Invalidity of All Asserted Patent Claims (Doc. No. 53) be granted-in-part and denied-in-part. (Doc. No. 108). The Court recommended (1) invalidating the '862 patent because it claimed unpatentable subject matter; (2) upholding the validity of the '829 patent because it passed the machine-or-transformation test; and (3) invalidating the '465 patent because it claimed unpatentable subject matter while also failing the machine-or-transformation test. H&R Block filed objections on August 5, 2010.¹ (Doc. No. 118).

The Court then issued another R&R, which recommended denying Jackson Hewitt's Motion for Summary Judgment of Invalidity Under 35 U.S.C. § 112 ¶ 2. (Doc. No. 113). The Court did not analyze the '465 and '862 patents, having already recommended invalidating those patents. Instead, the Court concentrated on the validity of the '829 patent, finding that the phrases in dispute were not indefinite. Jackson Hewitt filed objections on August 5, 2010.² (Doc. No. 119).

The Court also held a *Markman* hearing on October 1, 2009. The Claim Construction Memorandum Opinion and Order construing terms in the '829 patent³ (Doc. No. 112) issued on December 8, 2009.

¹ After the case was stayed pending the outcome of *Bilski v. Kappos*, the Court held a status conference on July 13, 2010, where it directed the parties to file any objections to the R&Rs issued prior to the stay.

² These objections were filed as a result of the status conference proceedings.

³ The parties briefed terms from all three patents at issue.

At the request of both parties, the Court administratively closed the case on December 10, 2009 pending the appeal of *In re Bilski* in order to better address the invalidity issues regarding the '862, '829 and '425 patents. (Doc. No. 114). After the Supreme Court issued its decision in *Bilski v. Kappos*, 130 S.Ct. 3218 (2010), on June 28, 2010, the Court held a status conference (Doc. No. 116) where it ordered supplemental briefing on the *Bilski* issues in light of the Supreme Court's recent decision. Briefing completed on September 13, 2010. (Doc. Nos. 120, 123, 126 & 127).

LEGAL STANDARD

“Summary judgment is appropriate in a patent case, as in other cases, when there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law.” FED. R. CIV. P. 56(c); *Nike Inc. v. Wolverine World Wide, Inc.*, 43 F.3d 644, 646 (Fed. Cir. 1994); *see also Celotex Corp. v. Catrett*, 477 U.S. 317, 323-25 (1986). A “genuine issue” of material fact exists when a fact requires resolution by the trier of fact and a reasonable jury could resolve a factual matter in favor of the non-movant. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248-49 (1986). When ruling on a motion for summary judgment, the court is required to view all justifiable inferences drawn from the factual record in the light most favorable to the non-moving party. *Id.* at 255.

A patent is presumed valid. 35 U.S.C. § 282; *KSR Int'l Co. v. Teleflex, Inc.*, 550 U.S. 398, 412 (2007). This presumption may be overcome only by clear and convincing evidence. *Takeda Chem. Indus., Ltd. v. Alphapharm Pty., Ltd.*, 492 F.3d 1350, 1355 (Fed. Cir. 2007). “Whether a claim is drawn to patent-eligible subject matter under § 101 is a threshold inquiry” and an issue of law. *In re Bilski*, 545 F.3d 943, 950-51 (Fed. Cir. 2008) (en banc), *aff'd sub nom. Bilski v. Kappos*, 130 S.Ct. 3218 (2010). “Section 101 emphasizes that ‘any’ subject matter in the four independent

categories [process, machine, manufacture, or composition of matter] and ‘any’ improvement in that subject matter qualify for protection.” *Research Corp. Technologies, Inc. v. Microsoft Corp.*, --- F.3d ----, 2010 WL 4971008, at *6 (Fed. Cir. Dec. 8, 2010). Fundamental principles such as “[p]henomena of nature, though just discovered, mental processes, and abstract intellectual concepts are not patentable, as they are the basic tools of scientific and technological work.” *Gottschalk v. Benson*, 409 U.S. 63, 67 (1972); *see also Diamond v. Chakrabarty*, 447 U.S. 303, 309 (1980) (listing three exceptions to patentability: “laws of nature, physical phenomena, and abstract ideas.”). But application of an abstract principle may be patentable. *Diamond v. Diehr*, 450 U.S. 175, 187 (1981). Courts, however, may not categorically reject subject matter “because it finds that a claim is not worthy of a patent.” *Research Corp.*, 2010 WL 4971008, at *6.

In *Bilski v. Kappos*, the Supreme Court characterized the machine-or-transformation test as “a useful and important clue, an investigative tool, for determining whether some claimed inventions are processes under § 101.” *Bilski*, 130 S.Ct. at 3227. In addition, the machine-or-transformation test may be a “key indicator of patentability.” *Ultramercial, LLC v. Hulu, LLC*, 2010 WL 3360098, at *3 (C.D. Cal. Aug. 13, 2010).

The machine-or-transformation test is subject to two considerations: first, the machine or transformation “must impose meaningful limits on the claim’s scope,” and second, the machine or transformation “must not merely be insignificant extra-solution activity.” *In re Bilski*, 545 F.3d at 961-62. The imposition of meaningful limits prevents claims from preempting “all uses of a fundamental principle in all fields and . . . all uses of the principle in only one field.” *Id.* at 957. The prohibition against tying a claim to an extra-solution machine or transformation protects against subversion of the patent system by clever draftsmen. *Id.* (citing *Parker v. Flook*, 437 U.S. 548, 590

(1978)). “[A] claim that is tied to a particular machine or brings about a particular transformation of a particular article does not pre-empt all uses of a fundamental principle in any field but rather is limited to a particular use, a specific application.” *Id.*

To pass the transformation prong of the test, the claimed process must transform a particular article. *In re Bilski*, 545 F.3d at 961-62. “This transformation must be central to the purpose of the claimed process.” *Id.* at 962. Traditionally, an article may be a physical object or substance. *Id.* In modern applications, an article may be electronic signals or electronically-manipulated data if the data represents physical and tangible objects. *Id.* at 962-63. When a process transforms qualified data, transformation of the underlying physical objects is not necessary. *Id.* at 963. “[T]ransformations or manipulations simply of public or private legal obligations or relationships, business risks, or other such abstractions cannot meet the test because they are not physical objects or substances, and they are not representative of physical objects or substances.” *Id.*

Similarly, a process is sufficiently tied to a particular machine when that machine is central to the purpose of the claimed process. *Cf. In re Bilski*, 545 F.3d at 962 (holding a transformation “must be central to the purpose of the claimed process.”). “Integral use of a machine or apparatus to achieve performance of the method weighs toward eligibility, as compared to where the machine or apparatus is merely an object on which the method operates, which weighs against eligibility.” INTERIM GUIDANCE FOR DETERMINING SUBJECT MATTER ELIGIBILITY FOR PROCESS CLAIMS IN VIEW OF *BILSKI V. KAPPOS*, 75 Fed. Reg. 43,922, 43,925 (July 27, 2010) (“INTERIM GUIDANCE”).

However, the machine-or-transformation test is not the exclusive test for patentability, *Bilski*, 130 S.Ct. at 3227, nor is it outcome determinative. *See Prometheus Laboratories, Inc. v. Mayo Collaborative*, --- F.3d ----, 2010 WL 5175124, at *7 (determining whether the patent at issue

claimed natural phenomena despite having already determined the claims passed the machine-or-transformation test). Instead, the eligibility inquiry refocuses on § 101. *Research Corp.*, 2010 WL 4971008, at *7. The § 101 analysis applies equally to machine or process claims: “[T]he Supreme Court’s decisions in *Diehr*, *Benson*, and *Flook*, all of which involved method (i.e., process) claims, have provided and supported the principles we apply to both machine- and process-type claims.” *AT&T Corp. v. Excel Commc’ns, Inc.*, 172 F.3d 1352, 1358 (Fed. Cir. 1999), *abrogated by In re Bilski*, 545 F.3d 943 (Fed. Cir. 2008); *see also Flook*, 437 U.S. at 590 (“The concept of patentable subject matter under § 101 is not ‘like a nose of wax which may be turned and twisted in any direction.’”) (citations omitted). Thus, it seems that although a patent may fail the machine-or-transformation test, claims may nonetheless be directed toward patentable subject matter. *See Bilski*, 130 S.Ct. at 3227-3228 (analyzing the concept of hedging risk under an “abstract idea” regime of *Benson*, *Flook* and *Diehr* rather than applying the machine-or-transformation test). Similarly, even if the process claims pass the machine-or-transformation test, the Court must decide whether the patent is nonetheless directed toward claiming an abstract idea. *See id.* at 3229-3231; *Research Corp.*, 2010 WL 4971008, at *7; *Ultramercial*, 2010 WL 3360098, at *6. Therefore, even though the outcome of an application of the machine-or-transformation test is an “important clue” to determine patentability, courts should also engage in a discussion of whether the patent is directed toward an abstract idea or any of the other exceptions to patentability. *See Ultramercial*, 2010 WL 3360098, at *3-*6 (analyzing the patent at issue under the machine-or-transformation test and the abstract idea construct).

In addressing what is “abstract,” the Federal Circuit has not defined the concept “beyond the recognition that this disqualifying characteristic should exhibit itself so manifestly as to override the

broad statutory categories of eligible subject matter and the statutory context that directs primary attention on the patentability criteria of the rest of the Patent Act.” *Research Corp.*, 2010 WL 4971008, at *7. However, even if an invention is not “so manifestly abstract,” the patent may lack “sufficient concrete disclosure to warrant a patent.” *Id.* at *8.

DISCUSSION

As stated above, this case was stayed until the Supreme Court decided *Bilski v. Kappos*, 130 S.Ct. 3218 (2010). For the purposes of this discussion, it is helpful to review the Supreme Court precedent that aided the Court in determining whether the patent at issue in *Bilski* fell outside the scope of § 101 for claiming an abstract idea.

In deciding *Bilski*, the Supreme Court turned to *Benson*, *Flook*, and *Diehr* for guidance. 130 S.Ct. at 3229. In *Benson*, the Court held that a patent claiming a method to convert binary-coded decimal numerals into pure binary numerals was not patent-eligible, stating the application was not a “process,” but rather an unpatentable abstract idea. *Benson*, 409 U.S. at 64-67. Even though the claim recited “a general-purpose digital computer,” the Court did not take the opportunity to determine whether the algorithm was tied to a particular machine, observing instead that the practical effect of the claim would be to wholly preempt the use of the formula. *Id.* at 65, 71-72.

In *Flook*, the Court considered a patent “where the ‘only innovation was reliance on a mathematical algorithm.’” *Bilski*, 130 S.Ct. at 3230 (citing *Flook*, 437 U.S. at 585-586). Unlike *Benson*, the patent confined the use of the mathematical algorithm to a specific industry. *Id.* at 589-90. The Court, however, deemed the patent unpatentable under § 101 because the algorithm was assumed to be within the prior art and therefore, the patent contained no patentable invention. In *Diehr*, the Court explained that *Flook* represents the idea that abstract concepts cannot become

patentable simply because the patent application limits the use of the formula to a particular field or adds “insignificant postsolution activity.” *Diehr*, 450 U.S. at 191-92.

On the other end of the spectrum, the Court in *Diehr* upheld the patentability of a computerized process that used a mathematical formula. *Diehr*, 450 U.S. at 192-93. The Court reasoned the patent did not wholly preempt the formula’s use because the patent claimed an industrial process for molding rubber, rather than the formula itself. *Id.* The formula claimed was confined to use in the process of curing rubber, and other uses of the formula were not claimed. *Id.* at 187. The Court stated: “[A]n *application* of a law of nature or mathematical formula to a known structure or process may well be deserving of patent protection.” *Id.* at 187.

A reading of Supreme Court precedent leads this Court to apply a “meaningful limits” test. The Supreme Court rejected the patent in *Bilski* because to allow patentability of hedging risk would effectively “pre-empt use of this approach in all fields.” 130 S.Ct. at 3231. According to the Federal Circuit, a patent claiming an abstract idea, rather than a particular application of the principle, preempts “all uses of a fundamental principle in all fields and pre-empt[s] . . . all uses of the principle in only one field” when the patent is “not limited.” *In re Bilski*, 545 F.3d at 957 (citing *Diehr*, 450 U.S. at 193, n.14). “[M]eaningful limits on the claim’s scope . . . impart patent-eligibility.” *Id.* at 961 (citing *Benson*, 409 U.S. at 71-72).

I. The ‘862 Patent⁴

H&R Block asserts that Jackson Hewitt infringes “one or more claims” of each of the ‘862, ‘829, and ‘425 patents. (Doc. No. 32).

⁴ Although disputed terms contained within the ‘862 patent were briefed in the parties’ claim construction briefing (Doc. Nos. 85, 93, 98 & 102), the Court did not construe these terms, having previously found the ‘862 patent to be invalid prior to the *Markman* hearing.

The '862 patent is entitled "Spending Vehicles for Payments." The claimed invention "relates generally to a system and method for distributing payments to individuals and, more particularly, to a system and method for allocating a portion or all of an individual's payment into a spending vehicle." '862 patent at 1:6-9. The '862 patent consists of one independent claim and two dependent claims. The independent claim reads:

A computerized system for distributing spending vehicles comprising:

a payment due from a governmental entity;

an assignable right to receive said payment from said governmental entity, said assignable right held by an individual;

a spending vehicle offered by a third party sponsor to said individual in exchange for at least a portion of said individual's right to receive said payment due;

an assignment of at least a portion of said individual's right to receive said payment to said third party sponsor in exchange for said spending vehicle;

wherein information associating said payment with said spending vehicle from said third party sponsor is stored in and retrieved from a computer to facilitate processing of said spending vehicle and said spending vehicle is issued to said individual in an amount for spending by said individual of said at least a portion of said payment, said governmental entity is electronically notified to transfer said at least a portion of said payment to said third party sponsor, and said at least a portion of said payment is received by said third party sponsor.

'862 patent at 6:56-7:12 (Claim 1).

A. The Parties' Supplemental Contentions

Jackson Hewitt contends that the claims of the '862 patent are invalid under 35 U.S.C. § 101 because the claims are very similar to the invalidated claims in *Bilski*. DFT'S SUPP. BRIEF (Doc. No. 120) at 18. Specifically, the '862 patent claims, and the rejected *Bilski* claims, are directed to financial relationships, which are abstract ideas. *Id.* Jackson Hewitt further contends that the

computer claimed in the '862 patent merely stores and retrieves data, thereby making it an insignificant extra-solution component that does not meet the requirements of patentability under *Flook*. *Id.* at 19. Moreover, Jackson Hewitt contends the invention claimed in the '862 patent merely limits the invention to the field of "government payments," which is unacceptable under the Supreme Court's decision in *Bilski*. *Id.*

H&R Block responds by stating that *Bilski* allows specific applications of business concepts that do not preempt uses of the concept in other fields. PLTFF'S SUPP. RESPONSE (Doc. No. 123) at 2. Moreover, H&R Block asserts the '862 is patentable because the claims provide meaningful limits on the exchange of financial products. *See id.* at 8-10. First, H&R Block argues the '862 patent limits the entities eligible to exchange financial products, namely "individuals." *Id.* at 8. Second, the financial product is limited to a spending vehicle that must be offered by a third party sponsor. *Id.* Third, the '862 patent is limited by the computer disclosed in the disputed claims, and the system must be "capable of notifying a government entity to transfer payment so that [the] third party sponsor may receive the payment." *Id.* at 9. Finally, H&R Block contends these limits do not preempt the use of exchanging financial products in other fields of use. *Id.* at 10. For example, H&R Block asserts that the '862 patent leaves the door open for the issuance of spending vehicles that are not linked to government payments; financial products that are not used for spending, such as stock certificates; and the distribution of spending vehicles without electronically notifying the government. *Id.*

B. The '862 Claims Apply a Meaningful Limit, Making the Claims Patentable

In rejecting the claims in *Bilski*, the Supreme Court stated that hedging risk, the concept recited in the patent, was a "fundamental economic practice." *Bilski*, 130 S.Ct. at 3231. Moreover,

allowing the “petitioners to patent risk hedging would pre-empt use of this approach in all fields, and would effectively grant a monopoly over an abstract idea.” *Id.* Claim 1 of the *Bilski* patent describes steps to hedge risk: 1) trading commodities with a consumer based on historical averages; 2) identifying alternate consumers with the opposite position as those consumers identified in step 1; and 3) initiating transactions between the consumers identified in step 2 to balance, or hedge, the risk assumed in the trades of step 1. *Id.* at 3223-24. The dependent claims of the patent went on to describe the application of the above transactions to the energy market. *Id.* at 3224.

Although an abstract intellectual concept—collateralized loans⁵—certainly underlies the ‘862 patent, it differs in important ways from the patent at issue in *Bilski*. Where the *Bilski* patent’s independent claims disclosed the abstract idea of hedging, independent Claim 1 of the ‘862 patent describes a particular *application* of an abstract idea, particularly, the application of collateralized loans to the field of assignable government payments in exchange for something of value. *See Diehr*, 450 U.S. at 187 (approving the patentability of the application of an abstract idea).

Limiting the concept of collateralized loans to the specific field of assignable government payments in exchange for something of value is not merely a field of use limitation prohibited by *Flook*. The ‘862 patent imposes a meaningful limit that prevents the preemption of all uses of collateralized loans in the field. *See In re Bilski*, 545 F.3d at 957. Particularly, the ‘862 patent limits the invention by disclosing a “spending vehicle.”⁶ The ‘862 patent clearly provides that a spending

⁵ The Court uses the term *collateralized loans* to describe a financial relationship where one party gives something of value in exchange for an expectation to receive something of value in the future.

⁶ The Court construed the term “spending vehicle” in its Claim Construction Memorandum Opinion and Order (Doc. No. 112) regarding the ‘829 patent. The Court construed the term as “a financial product, but not cash, used for purchasing something of value.” (Doc. No. 112) at 7.

Because the parties briefed the term “spending vehicle” for the ‘862 and ‘829 patents together, the Court construes “spending vehicle,” with regard to the ‘862 patent, as “a financial product, but not cash, used for

vehicle is an “[a]lternative to cash payments,” thereby limiting the applicability of the ‘862 patent to the use of *non-cash* collateralized loans in the field of assignable government payments in exchange for something of value. *See* ‘862 patent at 1:30-54.

Contrary to Jackson Hewitt’s arguments, the spending vehicle limitation is not a token or accessory. *See* DFT’S SUPP. REPLY (Doc. No. 126) at 3-4 (characterizing H&R Block’s limitation arguments as extra-solution activities). In *Ultramercial*, the court analyzed the patentability of an invention that claimed a method for distributing copyrighted products over the internet. *Ultramercial*, 2010 WL 3360098, at *1. After determining the invention failed the machine-or-transformation test, the court determined the patent at issue disclosed an abstract idea. *Id.* at *6. In rejecting the claims, the court stated that the patent lacked meaningful limits: “That the exchange (advertisement for media) is carried over the Internet, through a facilitator, using passwords and activity logs, does not limit the patent in a meaningful way.” *Id.* The court stated that these token limitations did not prevent the preemption of using advertisements as an exchange or currency in other fields.⁷ *See id.* at *6-*7.

Unlike the proposed limits in *Ultramercial*, the disclosed spending vehicle is a meaningful limitation. The spending vehicle limitation leaves the door open for cash-collateralized loans to be applied to all forms of government payments (*e.g.*, Social Security checks, 401(k) distributions, dividend payments, tax refunds, payroll checks or deposits, private payment arrangements, etc.), ‘862 patent at 1:45-48, because the type of loans claimed in the ‘862 patent are limited to the use of

purchasing something of value.”

⁷ The Court wonders whether it would have been more accurate to say that if the court were to allow the applicant to patent the concept with these token limits, the use of the concept would be preempted in one field, *i.e.*, the Internet, instead of all fields, *i.e.*, outside the context of the Internet.

spending vehicles rather than cash: “[A]n individual . . . may choose to receive in place of the payment a spending vehicle . . . instead of receiving a regular payment by check or cash or direct deposit.” ‘862 patent at 1:30-54. Thus, the spending vehicle limitation is meaningful because it does not preempt all uses of collateralized loans in the particular field of assignable government payments in exchange for something of value.⁸

Accordingly, the Court finds that the claims of the ‘862 patent imposes a meaningful limit, and therefore, the ‘862 patent is valid under 35 U.S.C. § 101.

II. The ‘829 Patent

The ‘829 patent is entitled “Tax Refund System.” The claimed invention “relates generally to a system for distributing tax refunds to taxpayers and, more particularly, to a system for reallocating some or all of a taxpayer’s tax refund into a spending vehicle.” ‘829 patent at 1:6-10.

The ‘829 patent has one independent claim and five dependent claims. The independent claim reads:

A method of providing at least a portion of an income tax refund amount to a taxpayer through a spending vehicle, comprising:

arranging, among an electronic tax preparation system and a third party spending vehicle provider, to offer at least one spending vehicle to said taxpayer, said spending vehicle redeemable only at a retailer designated by the arrangement;

preparing a tax return by or for said taxpayer using said electronic tax preparation system;

obtaining tax return data from said electronic tax preparation system, said tax return data comprising an anticipated income tax

⁸ With respect to H&R Block’s argument that the computer poses meaningful limits, the Court disagrees. The computer component is not a particular, special-purpose machine; it is capable of no more than storing and retrieving data memorializing associations. If an extra-solution step is insufficient to render an otherwise unpatentable process claim valid, then by analogy, an extra-solution component is insufficient to render an otherwise unpatentable “system” claim valid. *Cf. In re Bilski*, 545 F.3d at 961-63 (concluding that data gathering steps are insignificant extra-solution activity). Thus, the addition of a generic computer—capable of only storing and retrieving data associating payments with spending vehicles—to the claimed system fails to impose meaningful limits on Claim 1.

refund amount from said taxing authority payable to said taxpayer;
selecting by said taxpayer said at least one spending vehicle from a plurality of spending vehicles offered by said third party spending vehicle provider;
executing at the time of preparation of said tax return using said electronic tax preparation system an agreement related to said spending vehicle in which said taxpayer agrees to assign at least a portion of said income tax refund amount to said third party spending vehicle provider and said third party spending vehicle provider agrees to accept said assignment and provide said selected spending vehicle to said taxpayer and to accept an associated risk for non-payment of said portion of said income tax refund, wherein said agreement does not involve issuing a loan or credit to said taxpayer and wherein said taxpayer and said spending vehicle provider obligations occur upon submission of said tax return to said taxing authority;
transferring electronically said at least a portion of said income tax refund amount to an account for said third party spending vehicle provider; and
issuing said selected spending vehicle to said taxpayer, said selected spending vehicle having a prepaid value greater than said assigned at least a portion of said tax refund and said taxpayer redeems said selected spending vehicle at said designated retailer to purchase products or services.

‘829 patent at 5:37-6:28 (Claim 1).

A. The Parties’ Supplemental Contentions

Jackson Hewitt essentially argues that the Court’s application of the machine-or-transformation test in its previous R&R was erroneous. *See* DFTS’ SUPP. BRIEF AT 10-11. Jackson Hewitt cites *Diehr*, stating that “[i]n determining the eligibility of [a] claimed process for patent protection under § 101, [the] claims must be considered as a whole,’ and not dissected into separate elements.” *Id.* at 10 (citing *Diehr*, 450 U.S. at 188; *Bilski*, 130 S.Ct. at 3229-31; *Flook*, 437 U.S. at 594). Thus, Jackson Hewitt argues that although the Court found one component of the ‘829 patent passed the machine-or-transformation test, the claimed invention, as a whole, is unpatentable. *Id.* at 11. Jackson Hewitt further argues that the claims of the ‘829 are directed toward financial

relationships and legal obligations, just like the ‘862 and ‘425 patents, which the Court found to be invalid in its prior R&R. *Id.* (citing (Doc. No. 108)). In addition, Jackson Hewitt analogizes the claims of the ‘829 to those found invalid in *Bilski*. *Id.* at 11-12.

Finally, Jackson Hewitt claims the computer the Court previously tied to the claims of the ‘829 does not actually meet the machine-or-transformation test. *Id.* at 12. Jackson Hewitt asserts that neither party argued that “the ‘executing’ step requires the use of the ‘electronic tax preparation system’ or any particular computer.” *Id.* at 13. Jackson Hewitt contends it is undisputed that a computer is not needed to perform the “executing” step claimed in the ‘829 patent. *Id.* at 13. According to Jackson Hewitt, the electronic tax preparation system that performs the “executing” step is merely a “general purpose electronic system programmed in some unspecified manner, which is insufficient to meet the machine-or-transformation test.” *Id.* at 15.

H&R Block responds by claiming the Court has already determined that the ‘829 patent passes the machine-or-transformation test, and that *Bilski* did not change the applicability of the test. PLTFF’S SUPP. RESPONSE AT 10. Therefore, according to H&R Block, the issue need not be revisited. *Id.* at 12. Furthermore, H&R Block attacks Jackson Hewitt’s characterization of *Diehr*, stating that the patents in *Flook* and *Diehr* claimed algorithms, and the Supreme Court had to determine whether these algorithms were the sole novel feature of the invention. *Id.* at 11. According to H&R Block, because it “does not contend that some abstract idea is its sole innovation,” the machine-or-transformation test, as already applied, falls in line with Supreme Court precedent. *Id.* In addition, H&R Block reiterates the arguments made concerning meaningful limits on the ‘862 patent, stating the ‘829 patent provides the same meaningful limits on the application of a business concept. *Id.* at 8.

B. The ‘829 Patent Fails the Machine-Or-Transformation Test

The ‘829 claims recite a method utilizing an “electronic tax preparation system.” ‘829 patent at 5:40. H&R Block argues this requires the use of a computer, which is a machine central to the claimed method. (Doc. No. 65) at 17. The Court must determine whether this recitation of a computer meets the machine-or-transformation test. *In re Bilski*, 545 F.3d at 961. To meet the machine prong of the test, the computer must “impose meaningful limits on the claim’s scope.” *Id.* (citing *Benson*, 409 U.S. at 71-72).

In the original briefing, the parties dispute the scope of the computer’s involvement in the claimed process. Jackson Hewitt describes the computer’s two functions as 1) data gathering, including preparing a tax return, obtaining tax return data, and providing the taxpayer with the option to select a spending vehicle; and 2) electronically transferring a portion of the refund to a spending vehicle provider. (Doc. No. 53) at 25. H&R Block states the “computer is used to prepare and relay a tax return with an anticipated refund amount, and to electronically transfer a portion of the tax refund into an account for the third party sponsor of a spending vehicle.” (Doc. No. 65) at 20.

The Court sees no difference in the parties’ explanation of the computer recited in Claim 1 of the ‘829 patent. Looking at the claim language, the Court identifies computer involvement only in the steps of 1) preparing a tax return and 2) obtaining tax return data, ‘829 patent at 5:45-6:2, which are insignificant extra-solution activity. *See In re Bilski*, 545 F.3d at 963 (“adding a data gathering step to an algorithm is insufficient to convert that algorithm into a patent-eligible process”); *see also In re Grams*, 888 F.2d 835, 840 (Fed. Cir. 1989) (finding step of deriving data for use in an algorithm insufficient to render the process patentable). Preparing, calculating, and obtaining a tax refund simply amount to a data gathering step. Therefore, the computer is

insufficient to satisfy the machine prong of the machine-or-transformation test.

As for the transformation prong of the test, the '829 patent also fails. All the steps claimed in independent Claim 1 of the '829 patent involve manipulating data that represent legal obligations and relationships. *See In re Bilski*, 545 F.3d at 963. However described, the data and resulting loan represent money. Although tangible in some forms, money is simply a representation of a legal obligation or abstract concept. Therefore, the '829 patent fails the machine-or-transformation test.

C. The '829 Claims Provide Meaningful Limits and is Therefore Within the Scope of § 101

Despite failing the machine-or-transformation test, the Court must determine whether the invention falls under the *Bilski* or *Diehr* categories of patentability. *Ultramercial*, 2010 WL 3360098, at *6; *see also Bilski*, 130 S.Ct. at 3227, 3229-3231 (declaring the machine-or-transformation test to be merely an investigative tool in the patentability inquiry and applying an alternate abstract idea test); *Research Corp.*, 2010 WL 4971008, at *7.

Like the '862 patent, independent Claim 1 does not claim the abstract concept of collateralized loans and then attempt to limit its use to a particular field, as is the case in *Bilski*. *See Bilski*, 130 S.Ct. at 3223-24. Rather, the independent claim of the '829 patent recites an application of collateralized loans to the field of assignable income tax refunds in exchange for something of value. Moreover, it recites meaningful limits such that the '829 patent falls within the scope of § 101.

The '829 patent's limited field of applicability is not a mere field of use limitation. Specifically, the '829 patent limits the application of collateralized loans to spending vehicles with a prepaid value greater than the assigned income tax refund amount, redeemable only at a designated

retailer. *See* ‘829 patent at 5:37-6:28 (Claim 1). Similar to the spending vehicle limitation identified in the ‘862 patent, the spending vehicle referred to in the ‘829 patent leaves the door open for financial exchanges involving income tax refunds that do not use spending vehicles. Claim 1 explicitly recites the spending vehicle limitation: “A method of providing . . . an income tax refund amount to a taxpayer through a spending vehicle.” ‘829 patent at 5:37-38. Thus, for example, the ‘829 patent allows for the possibility that a taxpayer may assign his income tax refund in exchange for cash.

The ‘829 claims are further limited by the requirement that the spending vehicle is “redeemable only at a retailer designated by the arrangement.”⁹ ‘829 patent at 5:43-44. Not only is the invention claimed in the ‘829 patent limited to the use of spending vehicles, but said spending vehicles are limited to use at specific retailers identified in the assignment. Therefore, debit and credit cards that may be used at any establishment are not covered by the ‘829 patent. Thus, limiting the establishments where the spending vehicle may be used provides a meaningful limit that does not prevent the use of spending vehicles that are redeemable at any location.

Finally, the ‘829 claims are limited to spending vehicles loaded with an amount greater than the assigned portion of the expected income tax refund. *See* ‘829 patent at 6:24-26 (“spending vehicle having a prepaid value than said assigned at least a portion of said tax refund”).¹⁰ The specification provides multiple examples of this concept, stating “[t]he benefit to the retailer is that the taxpayer must spend his or her tax refund dollars at the retailer’s store(s), and the benefit to the

⁹ The Court found this term requires no construction. (Doc. No. 112) at 11-12.

¹⁰ The Court found that “said selected spending vehicle having a prepaid value greater than said assigned at least a portion of said tax refund” requires no construction. (Doc. No. 112) at 11-12.

taxpayer may be that the retailer offers buying power at the retailer's store(s) *in excess of the dollar amount of the taxpayer's refund.*" '829 patent at 1:56-61 (emphasis added); *see also* '829 patent at 3:55-67. This limitation narrows the scope of the invention and does not preempt the use of spending vehicles issued with a prepaid value less than, or equal to, the expected income tax refund.

Accordingly, the '829 patent has meaningful limits that prevent the preemption of the use of collateralized loans in the field of assignable income tax refunds in exchange for something of value. Therefore, the '829 patent is directed to patentable subject matter.

III. The '425 Patent

The '425 patent is entitled "System and Method for Providing a Loan to a Taxpayer Based on a Pre Year-End Tax Refund." The claimed invention "relates generally to a tax refund system, and more particularly, to a system in which a taxpayer receives a loan based on his or her estimated tax refund prior to the year end holidays of the calendar year preceding the year in which the taxpayer files his or her tax return forms." The challenged "computerized systems" claims consist of four independent claims and twelve dependent claims. Although the independent claims differ in their specifics, Claim 1 is representative:

A computerized system for providing a loan to a taxpayer prior to the end of the current tax year, comprising:

historical income tax refund data comprising income tax refund amount data for at least one year prior to the current year and in a computer;

year-to-date income data for the current year, for said taxpayer, wherein said date is prior to the end of the current tax year and said year-to-date income data is in said computer;

year-to-date expense data for the current year, for said taxpayer, wherein said date is prior to the end of the current tax year and said year-to-date expense data is in said computer;

a process in said computer to determine prior to the end of the current tax year an estimated income tax refund amount for said

taxpayer for said current tax year using said historical income tax refund data, said year-to-date expense data for a date prior to the end of the current tax year;

a loan provided to said taxpayer prior to the end of said current tax year in an amount based on said estimated income tax refund amount for said current tax year for said taxpayer as determined by said computer; and

an income tax refund for said current tax year, wherein said income tax refund is based on a tax return prepared using actual income and expense data and filed after said current tax year for said taxpayer and is applied to the balance of said loan based on said estimated income tax refund.

‘425 patent at 4:5-35 (Claim 1).

The challenged method claims consist of independent claim 17 and its dependent claims.

Claim 17 reads:

A computer-implemented method for providing a loan to a taxpayer prior to the end of the current tax year, said method comprising:

determining an income tax refund amount for at least one tax year prior to the current tax year;

estimating at a computer said taxpayer’s income tax refund amount due for said current year prior to the end of said current tax year based on said income tax refund amount;

providing a loan to said taxpayer prior to the end of the current tax year in amount based on said estimated income tax refund amount due for said current tax year for said taxpayer as determined by said computer;

assigning said taxpayer’s income tax refund to said lender;

preparing a tax return for said taxpayer using actual data after the end of the current tax year;

filing said tax return with a taxing authority;

receiving said taxpayer’s income tax refund from said taxing authority; and

applying said taxpayer’s income tax refund to said loan based on said estimated income tax refund.

‘425 patent at 6:25-46 (Claim 17).

A. The Parties’ Supplemental Contentions

Jackson Hewitt argues the ‘425 patent is invalid because it 1) fails the machine-or-transformation test and 2) the ‘425 patent’s claims seek to patent financial relationships. DFTS’ SUPP. BRIEF AT 20-22.

H&R Block, on the other hand, asserts that the ‘425 patent passes the machine-or-transformation test because it links the claimed systems and methods to a computer. PLTFF’S SUPP. RESPONSE AT 6. H&R Block further contends that the ‘425 patent provides meaningful limits on a particular application of providing loans, including limiting loans to “taxpayers,” limiting the timing of the loan to the “end of the current tax year,” and limiting the loan amount to the “estimated tax refund.” *Id.* In addition, H&R Block asserts the ‘425 claims limit the types of data inputs used to process the loan, *e.g.*, historical income tax refund and year-to-date income and expense data for each taxpayer. *Id.* at 5-6. Further limiting the claims, argues H&R Block, are the required additional steps performed after the loan is provided, such as a subsequent tax refund and application of the refund to the balance of the loan. *Id.* at 6-7. Finally, H&R Block contends that finding the ‘425 patent invalid would effectively rule against all business method patents because the majority of business methods involve some kind of financial relationship. *Id.* at 7 (citing *Bilski*, 130 S.Ct. at 3227-28 (rejecting a blanket prohibition against business method patents)).

B. The ‘425 Patent Fails the Machine-Or-Transformation Test

As an initial matter, the Court applies the machine-or-transformation test to Claim 17 of the ‘425 patent. Like the claims of the ‘829 patent, Claim 17 fails the transformation prong of the test. The steps claimed in the method manipulate data that represent money and the resulting loan. In other words, the data simply represent legal obligations and relationships, which do not represent physical objects. *See In re Bilski*, 545 F.3d at 963 (“Purported transformations or manipulations

simply of public or private legal obligations . . . cannot meet the test because they are not physical objects or substances, and they are not representative of physical objects or substances.”).

Moreover, the claim fails the machine prong of the test. Claim 17 recites a “computer-implemented method for providing a loan to a taxpayer prior to the end of the current tax year.” ‘425 patent at 6:25-26. Although a computer is a machine, *see In re Ferguson*, 558 F.3d 1359, 1364 (Fed. Cir. 2009), the only recitations of a computer within the claim are found in the step of “estimating at a computer said taxpayer’s income tax refund amount” and “providing a loan to said taxpayer . . . based on an estimated tax refund amount . . . as determined by said computer.” Even assuming Plaintiff’s contention that the computer is also used to store income and expense data, the claim’s recitations of a generic computer are inadequate. As previously noted, deriving tax refund data comprises data gathering steps, which are insufficient to make the claimed process patent eligible. *See In re Bilski*, 545 F.3d at 963; *In re Grams*, 888 F.2d at 840. Accordingly, the Court finds Claim 17 of the ‘425 patent, and its dependent claims (18-20), fail the machine-or-transformation test.

C. The ‘425 Claims are Directed to an Abstract Idea

Next, the Court must determine whether the ‘425 patent claims¹¹ an abstract idea. The general principle claimed in the patent is the use of collateralized loans. The ‘425 claims recite the use of loans collateralized by an income tax refund. However, the claimed invention merely discloses how collateralized loans would be utilized in the income tax refund field, a field of use limitation prohibited by *Flook*. *See Bilski*, 130 S.Ct. at 3231. Put differently, the ‘425 patent does not disclose any meaningful limits that prevent preemption of all uses of loans collateralized by

¹¹ This section applies to both the system and method claims in the ‘425 patent.

income tax refunds. To allow a patent on such a financial relationship without meaningful limits is unacceptable under 35 U.S.C. § 101.

H&R Block argues that the computer recited in the claims meaningfully limits the invention because the computer limitation leaves the door open for an entity to provide a loan without the use of a computer. PLTFF'S SUPP. RESPONSE AT 6. The Court disagrees. Claim 1 recites a system where certain data is stored in a computer, a process in a computer is used to estimate an income tax refund, a subsequent loan is provided to a taxpayer, and a tax refund is applied to the balance of the loan. Because the computer essentially stores and retrieves data, the claimed computer is merely an insignificant, post-solution component; the income tax refund amount is simply a variable that informs the value of the loan provided by the system. *Cf. In re Grams*, 888 F.2d 835, 840 (Fed. Cir. 1989) (finding step of deriving data for use in an algorithm insufficient to render the process patentable). Therefore, the computer is not a meaningful limit that narrows the scope of the '425 patent such that it does not preempt the use of loans collateralized by income tax refunds.

Moreover, the computer is no more than an "object on which the method operates." *See* INTERIM GUIDANCE, 75 Fed. Reg. at 43,925. Because H&R Block argues that the "[t]he system described for providing loans could be used without a computer," PLTFF'S SUPP. RESPONSE AT 6, the recited computer is not integral to the claimed system, nor is the machine needed to perform the claimed process. The claims are "so abstract and sweeping . . . [that they could] be performed through any existing or future-devised machinery, or even without an apparatus." INTERIM GUIDANCE, 75 Fed. Reg. at 43,925. Thus, the computer fails to provide a meaningful limit on the '425 claims, which weighs against patentability.

Nor do the other limits pointed out by H&R Block meaningfully limit the '425 patent. These

purported limits are simply accessories garnishing an unpatentable abstract financial relationship. Particularly, the historical income tax data and year-to-date income limits in the '425 patent are similar to the "historical averages" limitation in *Bilski*, which was not meaningful enough to make the abstract idea of hedging risk patentable. See *Bilski*, 130 S.Ct. at 3224-25. Furthermore, attempting to narrow the scope of the invention by 1) limiting eligible persons to taxpayers; 2) restricting the timing of the loan to the end of the current tax year; 3) limiting the loan amount to the estimated tax refund; 4) requiring a subsequent tax refund; and 5) applying the refund to the balance of the loan do not prevent preemption of all uses of loans collateralized by income tax refunds. Rather, these elements seem to be merely describing the process of advancing money based on an income tax refund. The Court can conceive of no other way to manifest this financial relationship in this particular field. Thus, these purported limits, like the recited computer, do not meaningfully limit the patent.

For the reasons above, the Court finds the '425 patent to be invalid.

CONCLUSION

In deciding whether H&R Block's patents fall within the scope of § 101, the Court not only applied the machine-or-transformation test, but also analogized the claims of the '862, '829, and '425 patents to those in *Bilski*. Furthermore, the Court examined whether the patents at issue recited meaningful limits on the core abstract ideas claimed in each patent such that they prevented the preemption of all uses of the principle in each claimed field of application. Accordingly, the Court **RECOMMENDS** that Defendant's Motion for Summary Judgment of Invalidity of All Asserted Patent Claims be **GRANTED-IN-PART** and **DENIED-IN-PART** and that U.S. Patent No. 7,127,425 be found invalid.

Within fourteen (14) days after receipt of the Magistrate Judge's Report, any party may serve and file written objections to the findings and recommendations contained in the Report. A party's failure to file written objections to the findings, conclusions and recommendations contained in this Report within fourteen (14) days after being served with a copy shall bar that party from *de novo* review by the district judge of those findings, conclusions and recommendations and, except on grounds of plain error, from appellate review of unobjected-to factual findings and legal conclusions accepted and adopted by the district court. *Douglass v. United States Auto. Ass'n*, 79 F.3d 1415, 1430 (5th Cir. 1996).

So ORDERED and SIGNED this 2nd day of February, 2011.



JOHN D. LOVE
UNITED STATES MAGISTRATE JUDGE