Patently Controversial

By Editor Test *Tue, Feb 21, 2012*

Lincoln National Life has received a new patent on its GLWB process, raising concerns that it might once again seek royalties from other VA issuers.

A new patent, or rather a continuation of an earlier patent, was issued to Lincoln National Life by the U.S. Patent Office last January 10, raising questions about whether Lincoln will use it to revive its intellectual property rights challenges against other issuers of variable annuities with lifetime income guarantees.

The patent document itself is lengthy, highly technical in nature and illustrated with flow charts. All but a few phrases have been published before, but according to several people familiar with it, those new phrases repair a flaw that caused a federal appellate court in July 2010 to nullify Lincoln's victory in February 2009 against Transamerica over patent rights.

"The language in the new patent addressed the points that Transamerica brought up," said an insurance executive familiar with the history of the legal dispute. "This brings up the question, why did Lincoln do this and what will they do with it?"

A Lincoln spokesperson would not comment on the matter when contacted last week by *RIJ*. Lincoln had also sued Jackson National Life Insurance Co., a unit of Britain's Prudential plc. That case is still active. At the end of the third quarter of 2011, Lincoln was the fifth biggest seller of variable annuity contracts in the U.S., with a 6% market share and $7.15 billion in premia collected in the first nine months of the year.

Billions of dollars in royalties may be at stake. If Lincoln were to resume legal action against other issuers of GLWB contracts, and if those actions succeeded, those companies might have to pay royalties on at least some of the assets under GLWB riders. (It's not clear which sales would be affected.) In February 2009, a jury decided that Transamerica should pay Lincoln royalties of 11 basis points, or $13 million. That judgment was nullified.

The pertinent language in the new patent, which protects a business process rather than a product, reads: "payments made thereafter may be made with or without a computer." The clause refers to the calculation of the income payments that GLWB contract owners receive if and when their account balances are exhausted while they are living.

Lincoln lost its dispute with Transamerica because, under the previous versions of the patent, the payments in question had to be made *with a computer*. Transamerica could hypothetically calculate the ongoing payments *without* a computer, however. (In point of fact, Transamerica's GLWB contracts were so new that none had yet reached the stage where such payments needed to be calculated.)

Michael C. Gilchrist, a Des Moines patent attorney who has written about the case on his blog, told *RIJ*, "Lincoln had a pretty bad result with their first Transamerica case. They won at the trial level, but their claim required that all of the steps in the process had to be done by a computer. On appeal, the judge said

nothing showed that Transamerica had used a computer. None of Transamerica's accounts had ever gotten to the guarantee phase."

On his blog, Gilchrist wrote, "It remains to be seen whether Lincoln will aggressively pursue enforcement of this new patent. Lincoln may be reluctant to sign on for additional litigation after going through the time and expense of the first litigation only to come away empty handed."

Actuary Tom Bakos of Ridgway, Colorado, who has written analyses of the Lincoln patent to help other insurers defend themselves against infringement actions, said the new patent could allow Lincoln to defend its patent anew.

"If Transamerica is still issuing and processing their GMWB the same way they were when Lincoln initially sued them for infringement, then this new '398′ patent gives Lincoln new ammunition to assert infringement again – but only for issues dating from June 2, 2011 – should Lincoln choose to pursue this either by lawsuit or settlement," Bakos told *RIJ* in an email.

To a lay person, it might seem counterintuitive that Lincoln could amend an earlier patent and, in essence, patch holes that became visible when competitors appeared to copy what Lincoln believed was its intellectual property. But under the patent laws such strategies are possible and legal.

"This exemplifies the value of having patent applications pending," Bakos told RIJ. "As long as Lincoln has pending applications they can file new applications (as they did in this case) to address issues they forgot or overlooked with respect to enforcing their applications. If Lincoln had no pending applications, they would not have been able to file a new application to correct the problem pointed out by the litigation in their [earlier] patent."

Gilchrist agrees with that view. "The new patent was the result of a 'continuation application.' A continuation application is a patent application that uses the same disclosure as an earlier application, but has different claims. Any continuation applications must be filed while the earlier application is still pending," he wrote on his blog.

"However, there is no limit to the number of continuations that can be daisy-chained together," he added. "Therefore, it can be a valuable strategy to file a continuation application with amended claims each time the issue fee is paid for an allowed application. Keeping a continuation application alive gives the patent owner the ability to address any weaknesses in the original patent that may be identified during litigation."

"Lincoln is hoping to get a monopoly in this area," Gilchrist said. "What happens to all the business that has been written? Courts would generally say that the patent owner is entitled to an injunction, but it also has to consider public interest. It's highly unlikely they would prevent the companies from servicing existing clients." He noted too that a competing insurance company might avoid infringement simply by farming out annuity calculations to a computer in Canada, for instance, because other countries don't recognize patents on business processes per se.

The executive who is familiar from the dispute worried that a renewed IP dispute could hurt the variable

annuity industry. “If other companies have to pay [Lincoln], who is it hurting?” he told *RIJ*. “It’s a cost to the manufacturer that will get passed on to the consumer.” At this point, the likelihood of that happening is difficult to gauge.