



## US Supreme Court reverses Federal Circuit's precedent on patent exhaustion

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*Impression Products Inc. v Lexmark International Inc.*, No. 15–1189, 581?US \_\_\_\_ (2017), Supreme Court of the United States, 30 May 2017

The US Supreme Court held that 'a patentee's decision to sell a product exhausts all of its patent rights in that item, regardless of any restrictions the patentee purports to impose or the location of the sale.' Justice Ginsburg issued her own opinion, in which she concurred 'in the Court's holding regarding domestic exhaustion' but dissented 'from the Court's holding on international exhaustion.' *Impression Products* reverses precedent of the United States Court of Appeals for the Federal Circuit on both domestic and international patent exhaustion.

### Legal context

A US patent grants the patentee an exclusive right to exclude others from 'making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States.' 35 USC § 154(a); see also 35 USC § 271(a).

In *Impression Products*, the US Supreme Court was asked to address two important questions regarding the scope of the doctrine of patent exhaustion:

1. Whether a patentee that sells an item under an express restriction on the purchaser's right to reuse or resell the product can enforce that restriction through a patent infringement lawsuit.
2. Whether a patentee exhausts its patent rights by selling its products outside the United States, where US patent laws do not apply.

The court found exhaustion in both instances, contrary to decades of Federal Circuit precedent.



## Facts

Lexmark International, Inc. ('Lexmark') designs, manufactures and sells toner cartridges that are used in laser printers. Lexmark holds patents that cover components of the toner cartridges and the manner in which the cartridges are used.

Lexmark sells toner cartridges in the United States and in other countries. Purchasers of Lexmark cartridges under its 'Return Program' receive a roughly 20 per cent discount on the price of the cartridges in exchange for their contractual promise to use them only once and to return the empty cartridges only to Lexmark. Each Return Program cartridge includes a microchip which renders the cartridge unusable once the toner runs out.

Several so-called 'remanufacturers' obtained empty Return Program toner cartridges from Lexmark customers in the United States and abroad. After developing a way to circumvent the microchips in the cartridges, the remanufacturers refilled the cartridges with toner and resold them.

Lexmark sued the remanufacturers, including Impression Products, Inc., for patent infringement based on both Return Program cartridges that Lexmark sold in the United States and Return Program cartridges that Lexmark sold abroad. Lexmark argued that it sold the cartridges domestically with an express prohibition on their reuse and resale, and that, as a result, Impression Products infringed Lexmark's patents when it refilled and resold the cartridges. With regard to its foreign sales of Return Program cartridges, Lexmark argued that it did not authorize anyone to import those cartridges into the United States, and thus Impression Products infringed Lexmark's patents when it imported the cartridges into the United States.

Impression Products countered that Lexmark's sales of the Return Program cartridges, both domestic and foreign, exhausted Lexmark's patent rights in those cartridges. The district court agreed with Impression Products as to Lexmark's domestic sales of Return Program cartridges, but not as to Lexmark's foreign sales.

In its *en banc* decision (816 F. 3d 721, 735 (2016)), the Federal Circuit ruled in favour of Lexmark as to both its domestic and foreign sales of Return Program cartridges. In accordance with its decision in *Mallinckrodt, Inc. v Medipart, Inc.*, the Federal Circuit held that Lexmark's domestic sales of Return Program cartridges did not result in patent exhaustion because Impression Products knew of the reuse and resale restrictions that accompanied those sales, and those restrictions were lawful. As to Lexmark's foreign sales of the Return Program cartridges, the Federal Circuit relied on its decision in *Jazz Photo Corp. v International Trade Commission* to hold that Lexmark's foreign sales also did not result in patent exhaustion.

A petition for certiorari was filed thereafter, raising both of these issues for resolution by the US Supreme Court.



## Analysis

The Supreme Court reversed the Federal Circuit, and held that ‘a patentee’s decision to sell a product exhausts all of its patent rights in that item, regardless of any restrictions the patentee purports to impose or the location of the sale.’ Slip op. at 2. The court reversed the *en banc* decision of the Federal Circuit below and remanded the case to the Federal Circuit for further proceedings consistent with its opinion.

### 1. Lexmark’s domestic sales of Return Program cartridges

The court concluded that Lexmark’s patent rights in the Return Program cartridges it sold in the United States were exhausted ‘the moment it sold them’. Slip op. at 5. ‘The single-use/no-resale restrictions in Lexmark’s contracts may have been clear and enforceable under contract law, but they do not entitle Lexmark to retain patent rights in an item it has elected to sell’ (Id). The Court’s conclusion was grounded in the ‘venerable principle’ against restraints on alienation, as well as in the court’s ‘well-settled line of precedent’ that, even in the face of an express restriction, a patentee does not retain patent rights in a product it has sold. Slip op. at 6–9. In particular, the court stated that its decision in *Quanta Computer, Inc. v LG Electronics, Inc.*, 553?US 617 (2008), settled that ‘patent exhaustion applies even when a sale is subject to an express, otherwise lawful restriction.’ Slip op. at 9.

The court also noted that, since a patent license does not pass title to a product, a patent license does not involve the same concerns about a restraint on alienation as a sale. Hence, a patentee can impose restrictions on a licensee. However, if the licensee complies with the license when selling a licensed product, the licensee’s sale of the product will exhaust the patentee’s patent rights in that item.

‘In sum, patent exhaustion is uniform and automatic. Once a patentee decides to sell—whether on its own or through a licensee—that sale exhausts its patent rights, regardless of any post-sale restrictions the patentee purports to impose, either directly or through a license.’ Slip op. at 13.

### 2. Lexmark’s foreign sales of Return Program cartridges

For the Return Program cartridges Lexmark sold outside the United States, the court held that ‘[a]n authorized sale outside the United States, just as one within the United States, exhausts all rights under the Patent Act.’ Slip op. at 13. Here, the court relied on its holding in *Kirtsaeng v John Wiley & Sons, Inc.*, 568?US 519 (2013), that the copyright ‘first sale’ doctrine applies to copies of copyrighted works sold outside the United States, and on the strong similarity between the copyright ‘first sale’ doctrine and the patent exhaustion doctrine and the bond between copyright and patent law. According to the court, the territorial limit on patent rights is irrelevant because patent exhaustion is triggered by a patentee’s decision to exchange a patented item and the invention it embodies for whatever



compensation it deems appropriate.

### 3. Justice Ginsburg's Opinion

Justice Ginsburg wrote separately to 'concur in the Court's holding regarding domestic exhaustion—a patentee who sells a product with an express restriction on reuse or resale may not enforce that restriction through an infringement lawsuit, because the U.S. sale exhausts the U.S. patent rights in the product sold.' Ginsburg, J., op. at 1. She dissented, however, from the court's holding that a foreign sale exhausts a US patentee's US patent rights (*Id.*). (Justice Ginsburg likewise dissented from the court's decision in *Kirtsaeng* that a foreign sale exhausts US copyright protections.)

Justice Ginsburg argued that, since patent rights are territorial, a foreign sale of a product does not implicate the US patent system and thus should not operate to exhaust a patentee's US patent rights. She also argued that the court's reliance on *Kirtsaeng* was inapposite since the US Patent Act does not have an analogue to the copyright first-sale provision in 17 USC §109(a), which was at issue in *Kirtsaeng*. Furthermore, Justice Ginsburg added that, unlike patent protections, copyright protections are harmonized across countries under the Berne Convention, and thus US and foreign copyright protections are likely to be similar.

### Practical significance

While *Impression Products* answered the two questions posed, it has raised new questions and while likely impact licensing strategy going into the future. For example, the rationale of *Impression Products* focuses heavily on the free alienability of goods in commerce, but it says nothing about services, and the impact of the exhaustion doctrine on such services. The court also found that under the exhaustion doctrine patent remedies would not be available for violations of post-sale restrictions of goods, but it expressly left open the possibility that contract law might be enforced. No doubt, many prior settlement agreements which tried to apportion liability among joint tortfeasors using the prior guidance in *Mallinckrodt, Inc. v Medipart, Inc.* will be subject to new scrutiny going forward. Patent infringement actions may be substituted with new breach of contract and tortious interference actions going forward. Only time will tell the ultimate impact of the significant deviation from the law as expressed by the Federal Circuit for decades.