

IP News, Litigation

## Federal Circuit “Getting Off on the Wrong Foot” Leads to a Reinforced Patent Exhaustion Doctrine

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Impression Products, Inc. v. Lexmark International, Inc. 581  
U.S. \_\_\_\_ (2017)

### *Abstract*

In the May 30, 2017, *Lexmark* decision, the United States Supreme Court reinforced a cut and dry approach to the patent exhaustion doctrine. The doctrine had been succinctly expressed previously in *Quanta Computer Inc. v. LG Electronics, Inc.*, 553 U.S. 617, 625 (2008) by requiring that a sale of a patented product “terminates all patent rights to that item.” In *Lexmark*, the Court concluded 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.” *Impression Products, Inc. v.*

*Lexmark International, Inc.*, No. 15-1189, 2017 U.S. Lexis 3397, \*12, slip op. at 2 (May 30, 2017). According to the Court, the Federal Circuit's earlier analysis reaching a different conclusion on the limits of the patent exhaustion doctrine simply "got off on the wrong foot." *Lexmark* at \*23, slip op. at 9.

### *Factual Background*

Lexmark International, Inc. ("Lexmark") manufactures and sells laser printer toner cartridges that are refillable for resale and later use. Lexmark owns patents that cover the structures of the cartridges and methods of using the cartridges, but third party resellers consistently retrieved used cartridges from Lexmark's customers, refilled the cartridges with toner, and placed the refilled cartridges on the market in competition with Lexmark's new cartridges. To address the resale market and later use of Lexmark's patented cartridges, Lexmark began to offer incentives for customers to return the cartridges to Lexmark for refilling. These incentives included discounts for customers who participated in Lexmark's cartridge "Return Program," which required customers to sign a contract with Lexmark agreeing to use each toner cartridge only once and to refrain from transferring spent cartridges to anyone other than Lexmark. Lexmark installed a microchip on its "Return Program" toner cartridges to ensure compliance. Third party remanufacturers, however, continued to retrieve used cartridges, refill them, and resell the filled cartridges regardless of the Lexmark patents and the contracts between Lexmark and its "Return Program" participants. Remanufacturers also retrieved cartridges that Lexmark had first sold abroad and refurbished the cartridges with toner for import and resale in the United States.

### *Legal Proceedings*

Lexmark filed patent infringement suits on two fronts by seeking patent remedies against identified groups of toner cartridge remanufacturers. A first group of defendants included domestic remanufacturers who did not abide by the resale restrictions that Lexmark alleged would transfer with

later possession of empty Lexmark toner cartridges. A second group of remanufacturers targeted by Lexmark included the above-noted remanufacturers who repurchased Lexmark toner cartridges abroad after the toner cartridges had been first sold by Lexmark in foreign jurisdictions.

The District Court of the Southern District of Ohio dismissed Lexmark's patent infringement counts for cartridges sold with resale restrictions pursuant to Lexmark's "Return Program" but denied the defendants' motion to dismiss in regard to Lexmark's cartridges that were imported back into the United States after being first sold abroad.

On appeal, the Federal Circuit ruled in favor of Lexmark in regard to both groups of products. The Federal Circuit held that a patentee selling patented products with sufficient ownership restrictions may legitimately enforce those restrictions in patent infringement actions, regardless of the patent exhaustion doctrine that would apply if a purchaser held full title to the products. The Federal Circuit further ruled that first sales to purchasers in foreign countries do not implicate the patent exhaustion doctrine over the patented product in the United States. *Lexmark Int'l, Inc. v. Impression Prods.*, 816 F.3d 721, 774 (Fed. Cir. 2016).

The Supreme Court granted certiorari to consider the Federal Circuit's analysis with respect to both U.S. and foreign patent exhaustion.

Prominent intellectual property trade groups weighed in on the proceedings before the Court. Regarding the post-sale restrictions on patented items, the American Intellectual Property Law Association ("the AIPLA") filed an amicus brief on the basis that "[i]f a patentee can temporally divide rights to make and sell its invention by express restrictions in a licensing agreement, it should also be able to sell limited use rights by express provisions in a sales contract." Brief for Amicus Curiae American Intellectual Property Law Association Supporting Neither Party, *Impression Products, Inc. v. Lexmark International, Inc.*, No. 15-1189, 2017 U.S. Lexis 3397 (May 30,

2017) at 9. The AIPLA argued that patent rights are the same as all property carrying a “bundle” of property interests, and if the consumer “neither needs nor wants to pay for the patentee’s entire patent monopoly, no rule should require it.” *Id.* at 12. Furthermore, the AIPLA went on to argue that there should be no foreign patent exhaustion rule, mostly on public policy grounds. As outlined in the AIPLA’s brief, the comparison of patent law and copyright law is tenuous when “[p]atent law contains no analogous provision to Section 109(a) [codifying the copyright first sale doctrine].” The AIPLA would only give Congress, not the Court, the authority to institute such a comparable first sale policy for international sales that implicate patent exhaustion. *Id.* at 24.

In another amicus brief, the Licensing Executives Society (“LES”) placed the decision in more practical terms. According to LES, the Court had to decide “whether the economic and efficiency benefits of [Lexmark’s] Status Quo freedom to contract are outweighed by the increased certainty and simplicity provided by an Increased Patent Exhaustion. Brief of Amicus Curiae Licensing Executives Society (U.S.A. and Canada), Inc. In Support of Neither Party, *Impression Products, Inc. v. Lexmark International, Inc.*, No. 15-1189, 2017 U.S. Lexis 3397 (May 30, 2017) at 19. LES viewed the case as one of potentially expanding the patent exhaustion doctrine past a “Status Quo” situation in which “patent rights conveyed in a transaction may continue to be controlled flexibly by the parties to that transaction.” *Id.* at 3. Any other result, according to LES would reflect an “Increased Patent Exhaustion” and potentially higher licensing rates or sales pricing for patented products. *Id.* at 3-4, 15.

### *Summary of the Opinion*

In deciding to reverse, the Supreme Court stated that the Federal Circuit’s analysis of limits on the patent exhaustion doctrine simply “got off on the wrong foot.” *Lexmark* at \*23, slip op. at 9. Where the Federal Circuit had considered the patent exhaustion doctrine as an interpretation of the U.S.

patent infringement statute and used in evaluating enforcement of patent rights, the Supreme Court stated that the patent exhaustion doctrine is actually “a limit on the scope of the patentee’s rights” from the start. *Lexmark* at \*24, slip op. at 10. The Court reversed the Federal Circuit on both points in favor of a black letter interpretation that sales of patented items exhaust the patent rights in the sold products, regardless of the geographic location of the purchaser and post-sale restrictions.

Under this interpretation, the Supreme Court held that “patent exhaustion is uniform and automatic” such that a patentee concluding a sale “exhausts its patent rights, regardless of any post sale restrictions the patentee purports to impose, either directly or through a license.” Accordingly, the patent infringement statute could not be used to enforce Lexmark’s post-sale restrictions and exclude the remanufacturers from the marketplace because “[e]xhaustion extinguishes that exclusionary power” granted to a patentee. *Id.*

In regard to the issue of whether Lexmark’s foreign sales implicated the patent exhaustion doctrine domestically in the United States, the Court turned to a comparison of the first sale doctrine in U.S. copyright law codified at 17 U.S.C. 109(a). “Under the first sale doctrine . . . when a copyright owner sells a lawfully made copy of its work, it loses the power to restrict the purchaser’s freedom ‘to sell or otherwise dispose of ... that copy.’” In *Kirstaeng v. John Wiley & Sons, Inc.* we held that this first sale [rule] applies to copies of a copyrighted work lawfully made [and sold] abroad.” (citation omitted) *Lexmark* at \*29, slip op. at 13. The Court’s rationale for the comparison was grounded in the fact that “[p]atent exhaustion, too, has its roots in the antipathy toward restraints on alienation [of property] . . . and nothing in the text or history of the Patent Act shows that Congress intended to confine that borderless common law principle to domestic sales.” *Id.* \*30, slip op. at 14. Accordingly, the Court decided that, like post-sale contractual restrictions on an item, a location of a sale is irrelevant, and after any sale, the patent exhaustion doctrine

terminates patent rights in that sold embodiment of a patented article.

### *Further Considerations*

If the Federal Circuit got off on the wrong foot with its analysis of the patent exhaustion doctrine, the U.S. Supreme made it personal. The Court concluded its opinion with a summary that “[e]xhaustion does not arise because of the parties’ expectations about how sales transfer patent rights . . . which can be addressed through contract law. Instead, exhaustion occurs because in a sale, the patentee *elects* to give up title to an item in exchange for payment. . . . As a result, restrictions and location are irrelevant; what matters is the patentee’s decision to make a sale.” *Id.* \*36 slip. op. at 18. (emphasis added).

In short, neither the intent of the parties to a first sale nor their geographic locations changes the fact that when a patentee makes a personal decision to sell a patented item, the patent exhaustion doctrine is a direct result of that decision. The doctrine is, therefore, an implicit limit on the patentee’s right to exclude others and is automatically applied upon the consummation of any sale.

The Court did not see the *Lexmark* decision as any kind of change or “increase” in the traditional patent exhaustion doctrine. *Lexmark* received a patent with an inherent limit defined by traditional patent exhaustion concepts. In the Court’s perspective, applying these traditional rules of patent exhaustion in no way cuts in on any patentee’s dance. It just ensures that all parties start out in well-defined positions for the next move.