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Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Patent Owners' Post-Sale Power On Line At High Court

By **Matthew Bultman**

Law360, New York (December 14, 2016, 11:07 PM EST) -- The U.S. Supreme Court could scale back the amount of control patent owners have over how their products are used after being sold, as the justices will review the Federal Circuit's holding that foreign sales never exhaust U.S. patent rights and that post-sale restrictions on patented items are permissible.

The high court agreed earlier this month to hear a case involving Impression Products Inc., a small West Virginia company that Lexmark International Inc. has accused of infringing its printer cartridge patents.

The case presents important questions about whether long-standing Federal Circuit rules on patent exhaustion are fair. Depending on how the court rules, companies across a wide range of industries could be forced to revisit contracts and might face new obstacles in enforcing their patents.

"A change in this will change [things] significantly for those that deal with IP and have, for example, post-sale restrictions on their IP rights," said Yar Chaikovsky of Paul Hastings LLP. He said the monetary impact in certain spaces — life sciences, in particular — could be sizeable.

Companies would have "to go relook at their agreements and rewrite their agreements within a world where, for example, there are no post-sale restrictions, which is not the world they have been living in," he said.

The case involves Impression's business of refurbishing and refilling Lexmark cartridges and reselling them. Impression does not dispute that the refilled printer cartridges infringe, but it argues that Lexmark's patent rights were exhausted by foreign sales or post-sale restrictions.

The full Federal Circuit sided with Lexmark on both aspects in a lengthy **10-2 decision** earlier this year. With respect to foreign sales, the court said its own 2001 decision that only sales in the U.S. trigger patent exhaustion rights is still good law, despite a recent Supreme Court copyright decision.

The copyright case, Kirtsaeng v. John Wiley & Sons, was decided in 2013 and held that sales outside the U.S. exhaust copyrights. The Federal Circuit said distinctions between copyright law and the Patent Act command different results.

Darren Donnelly of Fenwick & West LLP said this case provides the Supreme Court with an opportunity to bring some harmony to the IP legal framework. That's a good thing, he said, because "for businesspeople, the distinctions of the legal doctrine don't have a lot of practical sense."

“If something is sold abroad and the law is, 'I can import it back into the United States without fear of being sued by the intellectual property rights holder,' that shouldn’t be a different answer if there’s a technology and there’s a copyright on the label of the product, or a trademark on the label,” he said.

On the issue of post-sale restrictions, the Federal Circuit left intact its 1992 holding that when a patentee sells a patented article subject to sales restrictions that are lawful and clearly communicated to the purchaser, the sale does not give the buyer resale rights that were expressly denied.

Impression Products has tried to cast doubt on that decision by pointing to a 2008 Supreme Court case, Quanta Computer Inc. v. LG Electronics Inc., which held that authorized sales do exhaust patent rights. The Federal Circuit concluded that Quanta addressed a different scenario.

This leaves the Supreme Court with some thorny questions, and one that lends itself to different viewpoints. In terms of the potential impact of a decision, Matthew D’Amore of Morrison & Foerster LLP said there’s a conflict of free market principles.

“On the one hand, there’s this free market idea of ‘we want the unfettered exchange of goods, and we don’t want upstream holders of rights to constrain what downstream purchasers do with their products,’” D’Amore said.

“But on the other hand,” he said, “there’s a free market principle that says I should be able to freely contract with a buyer however I want. And buyers and sellers, you could argue, should be unrestricted in terms of their ability to reach a deal that meets their economic needs.”

It’s not uncommon for companies like drugmakers or software manufacturers to attach post-sale restrictions to the sale of their products. But that could all change if the Supreme Court decides to shut the door on these sorts of restrictions.

“Bonanza for transactional lawyers, let’s put it that way,” Chaikovsky said. “There will be a rewriting of agreements left and right.”

The justices agreed to hear the case at the urging of the Obama administration, which said the Federal Circuit was wrong on both aspects of the decision. And it comes at a time when the justices are considering another case that touches on questions of the extraterritorial reach of U.S. patent law.

That other case involves Life Technologies Corp. and Promega Corp., and deals with a question of whether shipping a single component of a patented invention to be combined with others overseas can constitute infringement.

“The issue of territorial lines is something the Supreme Court has stepped in on in the past, with the Microsoft v. AT&T case, so it is an area that is of interest for them,” D’Amore said.

Businesses will be paying close attention when the Supreme Court hears arguments in the Lexmark case early next year, hoping for some insight as to what the justices might be thinking. Not all will have the same rooting interests, though.

“Life science corporations have a lot stronger interest in not seeing the Federal Circuit’s opinion change in any way on both issues, first sale or post-sale restrictions,” Chaikovsky said. “Tech companies … would

rather see first-sale go away."

That's largely because drugmakers, who often sell drugs in foreign countries at lower prices than in the U.S., rely on the rule that overseas sales don't exhaust patent rights to prevent those drugs from being imported into the U.S. and sold in competition with their higher-priced American products.

In a Federal Circuit brief supporting Lexmark, the Biotechnology Industry Organization added that conditional sales allow companies to appropriately price their products. Some restrictions, on the sale of herbicides, for instance, can also help protect the health of people and the environment, it said.

Similarly, medical device manufacturers often sell products, like syringes, with the restriction that the device be used just once and on a single patient. The Medical Device Manufacturers Association has said removing the ability of patent owners to impose restrictions could be a public health issue.

"For decades, medical device manufacturers have relied on … the conditional-sale doctrine to aid them in ensuring compliance with safety-related restrictions on the use of their devices," it wrote in another Federal Circuit brief.

Meanwhile, companies and advocacy groups in the technology sector have lined up at the Supreme Court to back Impression Products. Intel Corp. and Vizio Inc. laid out their positions in an April filing, explaining that electronic devices and similar products "are often designed in one country, manufactured in another, assembled into finished products in a third and then shipped around the world."

"If [the Federal Circuit's] ruling is allowed to stand, a patentee could sell its patented article for use in a high tech component, and then turn around and sue for infringement when the finished product arrives in the United States," they wrote.

Impression Products is represented by Andrew J. Pincus, Paul W. Hughes and Matthew A. Waring of Mayer Brown LLP and by Edward F. O'Connor of Avyno Law PC.

Lexmark is represented by Constantine L. Trela, Robert N. Hochman, Benjamin J. Beaton and Joshua J. Fougere of Sidley Austin LLP, Timothy C. Meece, V. Bryan Medlock Jr., Jason S. Shull and Audra C. Eidem Heinze of Banner & Witcoff Ltd., Steven B. Loy of Stoll Keenon Ogden PLLC and in-house counsel D. Brent Lambert.

The case is Impression Products Inc. v. Lexmark International Inc., case number 15-1189, in the Supreme Court of the United States.

--Additional reporting by Ryan Davis. Editing by Philip Shea and Mark Lebetkin.
