

by Ryan Swank

Exhausting the **POSSIBILITIES**

After the *Impression Products v. Lexmark* ruling, manufacturers still may have legal avenues to enforce single-use restrictions on their products

THE U.S. Supreme Court's unanimous decision in *Impression Products, Inc. v. Lexmark International, Inc.* reflected an increased adherence to the doctrine of patent exhaustion.¹ Although the opinion, authored by Chief Justice John Roberts, roundly rejected Lexmark's attempts to limit use of its patented ink cartridges after their initial sale, analysis of the opinion suggests that there may still be options going forward. Lexmark attempted, but failed, to protect its patented product after sale. Yet, there may still be ways to use a patent to legally protect a patented product downstream in the marketplace.

In the present case, Lexmark made and sold patented ink cartridges in the United States and abroad for use in Lexmark printers. Some of Lexmark's cartridges were sold subject to a single-use restriction, also referred to as a no-resale restriction, which sought to require that the purchaser return the spent cartridges to Lexmark. Impression Products collected spent Lexmark cartridges previously sold in the United States and abroad, and resold the restricted cartridges in the United States in violation of the imposed restriction. The Supreme Court ruled that the doctrine of patent exhaustion precluded a finding that the actions of Impression Products were patent infringement.

Patent exhaustion is effectively a patent law parallel to the well-established property law abhorrence of anti-alienation restrictions on a seller's disposition of an entire interest in a chattel. Patent exhaustion declares that a patentee's rights in an individual patented article are "exhausted" once a patentee-authorized sale has occurred, thus enabling a purchaser to use the purchased individual article in any otherwise legal manner. Accordingly, the resale of a lawfully purchased patented good is free from restrictions under U.S. patent law under the patent exhaustion doctrine.

Because restrictions precluded by patent exhaustion would otherwise be burdensome to purchasers, the Supreme Court's decision in *Impression Products* appears to be ulti-

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mately beneficial to consumers at the cost of downstream control for patentees. Furthermore, the holding of *Impression Products* appears to align with the rationale for intellectual property law generally. For example, the U.S. Constitution authorizes Congress “[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.”² Accordingly, it seems that any legal precedent that eliminates a class of restrictions on devices embodying patented discoveries based upon extra-statutory limitations imposed by the patent owner itself, as accomplished by the holding of *Impression Products*, serves to ensure that the balance struck by Congress is maintained. The goal is to do enough to promote innovation without strangling commerce.

Because the holding of *Impression Products* provides a benefit to consumers while also providing a legal environment that still promotes technology-advancing inventions, it seems that the Supreme Court achieved the correct result. However, it is not entirely clear that the Supreme Court’s decision completely bars companies from contracting with their customers to retain patent rights in downstream patented items.

In reviewing the decision of *Impression Products*, a couple of issues are presented. First, what actions should patent owners consider as a result of the decision, regardless of whether such actions promote the progress of the useful arts? Second, what changes in the law would better serve the progress of the useful arts?

Companies like Lexmark can conceivably structure customer agreements, including a no-resale restriction, in the form of a license agreement. However, because establishing a license agreement with an ordinary customer seems to undermine the spirit of the Supreme Court’s decision in *Impression Products*, the Supreme Court may need to go further, perhaps to overrule previous Supreme Court decisions that provide a legal distinction between customers and licensees, should the right case come before it.

Prior Supreme Court Decisions

A number of Supreme Court decisions touch upon the doctrine of patent exhaustion, some dating back as far as the middle of the nineteenth century. Some of the decisions have provided more extensive rights to patentees, even when those rights conflicted with the underlying notions of patent exhaustion.

The 1912 Supreme Court decision of *Henry v. A.B. Dick Co.*, which has since

been overruled, served as a high point for the rights of patentees seeking to place restrictions relating to the post-sale use of their patented product (just as Lexmark sought to do with its patented ink cartridges).³ Furthermore, the facts presented to the Supreme Court in *A.B. Dick*, if adjusted for advancements in technology, seem to mirror the facts presented in *Impression Products*.

In *A.B. Dick*, the patent holder, A.B. Dick, sought to restrict the rights of a purchaser regarding the use of A.B. Dick’s patented product. The patented product sold was a mimeograph machine, which had a license restriction attached to it declaring that the machine was “sold by the A.B. Dick Company with the license restriction that it may be used only with the stencil, paper, ink, and other supplies made by A.B. Dick.”⁴ The Supreme Court held, 4-3, that A.B. Dick’s tie-in restriction was a legitimate and enforceable restriction on the basis of the inherency doctrine. The inherency doctrine states that because a patentee’s rights are exclusionary (e.g., “the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States,” as stated in 35 USC Section 154(a)(1)), the patentee has no obligation to allow the patented item to be sold at all. The majority held that, logically, this right must inherently provide a lesser right to sell the patented item subject to any otherwise lawful terms and conditions that the patentee may choose.

Chief Justice Edward Douglass White wrote for the dissent, explaining that what the majority’s holding meant “is that the patentee has the power, by contract, to extend his patent rights so as to bring within the claims of his patent things which are not embraced therein, thus virtually legislating by causing the patent laws to cover subjects to which, without the exercise of the right of contract, they could not reach.”⁵ That is, Chief Justice White believed that a contractual agreement should not be able to provide further protection under patent law.

The rationale of the dissent was ultimately determined to be sound legal reasoning, as *A.B. Dick* was eventually overturned by *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, which held that particular restrictions (i.e., tie-in restrictions requiring purchase of unpatented products) are improper and unenforceable under patent law.⁶ Specifically, *Motion Picture Patents* stated that “it is not competent for the owner of a patent...to in effect extend the scope of its patent monopoly by restricting the use of it to materials nec-

essary in its operation, but which are no part of the patented invention” noting that “the cost, inconvenience, and annoyance to the public which the opposite conclusion would occasion forbid it.”⁷

Had there never been a need to overturn *A.B. Dick* (that is, had the reasoning of the dissent in that case prevailed), a bright-line test likely would have resulted. Then, Lexmark’s current patent infringement claims would not have had any merit. Indeed, it is hard to envision the form of an argument legally distinguishing A.B. Dick’s tie-in restriction regarding the ink used with their patented mimeograph machine from Lexmark’s tie-in restriction regarding the ink used with their patented printer cartridges—in neither case was the ink covered by the subject patents claims.

Further muddying the waters in this area of patent law is another Supreme Court case, *General Talking Pictures Corp. v. Western Elec. Co.*⁸ The Supreme Court may need to revisit this case to provide further clarity regarding what restrictions can be legally made in accordance with patent law. In *General Talking Pictures*, the Supreme Court upheld field-of-use limitations as being in accordance with patent law. Field-of-use limitations allow a patentee to restrict an authorized licensee from using patented objects outside of a defined field of use as specified by the patentee. Specifically, the Supreme Court held that the patentee could legally require that the licensee sell patented amplifiers only in the field of home radios.⁹

More important, for determining how to advise a client in a position similar to that of Lexmark in light of *Impression Products*, the Supreme Court in *General Talking Pictures* held that the patentee could also sue a noncontracting purchaser that obtained a patented amplifier from the licensee and that made use of the amplifier outside the field of home radios if it could be demonstrated at trial that the purchaser was simply aware of the terms of the agreement between the patentee and licensee. The rationale of the court was that because the licensee knowingly made sales that were outside the scope of its license and because the purchaser knew of the patentee-imposed restrictions, the sales were therefore a breach of the terms of the subject license. Because the terms of the license were breached, the sale must therefore be treated as if no license had ever been granted by the patentee, the patentee could therefore sue both the licensee and the purchaser for infringement in accordance with the patent laws (as opposed to suing based on a theory gov-

erned by contract law).¹⁰

Accordingly, although the Supreme Court indicated in *Motion Picture Patents* that patent law may not generally be used to enforce post-sale restrictions on a purchaser of a patented item, the Supreme Court indicated that the opposite is true in *General Talking Pictures* when post-sale restrictions are enforced based on an agreement with a licensee. This disparate treatment of licensees and general purchasers seems to effectively weaken the patent exhaustion doctrine, and therefore may negatively affect the promotion of the useful arts.

Licensees vs. Contracting Purchasers

The unavoidable conclusion that licensees and contracting purchasers should be treated differently may have driven the thought process of the two-judge dissent for the Federal Circuit in *Lexmark International, Inc. v. Impression Products, Inc.* With respect to post-sale restrictions, the dissent expressed concern that practicing patentees may effectively have less control than nonpracticing patentees because a licensee operating outside of the terms of its license would be engaging in an infringing act. However, as the dissent expressed, the same cannot be said of a general purchaser ignoring a restriction tied to a sale. The dissent stated the belief that post-sale restrictions should be enforceable only as a matter of state contract law, even when the sale is conveyed through a nonexclusive patent licensee, as contract law would still provide adequate remedy for the patentee. Despite mostly siding with the dissent, the Supreme Court did not appear to share the more extreme position of further extending the doctrine of patent exhaustion and left *General Talking Pictures* intact.

In an attempt to distinguish the facts of *Impression Products* from those of *General Talking Pictures*, the Supreme Court stated that a licensee breaching the contract governing a license to make and sell a patented device was a “fundamentally different situation” from the case immediately before it.¹¹ However, the fundamentality of those differences may have been the least convincing aspect of the decision. The opinion emphasized that the facts in *General Talking Pictures* were different because the “licensee ‘knowingly ma[de]...sales...outside the scope of its license.’”¹² However, it seems that Impression Products knowingly obtained the restricted ink cartridges outside the scope of the agreement including the single-use restrictions. Accordingly, if a company producing a patented product were to place a single-use restriction in a license agree-

ment, and if that company were to treat an individual customer as a licensee, the act of allowing the patented product to be the subject of a “sale” to another would apparently be a violation occurring “outside the scope of” that license.

The opinion further noted that the court in *General Talking Pictures* “treated the sale ‘as if no license whatsoever had been granted’ by the patentee, which meant that the patentee could sue both the licensee and the purchaser—who knew about the breach—for infringement.”¹³ However, this is effectively what Lexmark was trying to accomplish: denial of any authorization to Impression Products to benefit from what would be an agreement-invalidating acquiring of the patented product. If Lexmark had been able to prove that the terms of its buyback program were part of a limited, nonexclusive license and had been able to prove that Impression Products was aware of those terms, then Lexmark would have recourse under patent law without having to sue its customers for their failure to follow their agreement with Lexmark.

The opinion declared that *General Talking Pictures* does not establish “that patentees can use licenses to impose post-sale restraints on purchasers”¹⁴ but failed to explain why that is necessarily true. Would the Supreme Court have reached a different conclusion with respect to Lexmark had they couched the terms of their agreement with their customers as a license? The opinion emphasized that *General Talking Pictures* involved a licensee that “infringed the patentee’s rights because it did *not* comply with the terms of its license.”¹⁵ However, with respect to Lexmark, whether the consumers failed to comply with the terms of their agreement with Lexmark was not apparently contested, if brought up at all. That is, Lexmark would have argued that both their customers and Impression Products failed to comply with the terms of the purchase agreement, thereby infringing Lexmark’s patent rights.

The opinion also stated that the patentee in *General Talking Pictures* “could bring a patent suit against the purchaser only because the purchaser participated in the licensee’s infringement.”¹⁶ Does this mean that the court did not accept as fact that Impression Products was aware of the terms of Lexmark’s buyback program?

The Supreme Court declared that “*General Talking Pictures*, then, stands for the modest principle that, if a patentee has not given authority for a licensee to make a sale, that sale cannot exhaust the patentee’s rights.”¹⁷ However, Lexmark had

never given authority for their customers to dispose of the cartridges in a manner causing them to be in the possession of a competitor.

Nothing in the holding of *Impression Products* indicates that there is a legal distinction between a licensee-user and a licensee-manufacturer. It seems the only significant distinction causing the Supreme Court to uphold the patentee’s rights in *General Talking Pictures*, and to find that no such rights existed for Lexmark, is that the terms of the single-use restriction were not part of license agreements, and Lexmark’s customers were therefore not licensees. Despite recognizing that Lexmark’s contractual rights should not be enforced under the patent laws, it seems that the Supreme Court is comfortable with the notion of a patent-related cause of action (i.e., infringement) arising from a contract-related cause of action (i.e., breach of the terms of the license). This position does, in fact, indicate that a practicing patentee has fewer rights than a nonpracticing patentee, just as the Federal Circuit’s dissent had indicated.

Perspective on the Future

Lexmark’s desire to control a larger share of the printer ink market is, from a business standpoint, and without regard to the progress of the useful arts, understandable. In light of the Supreme Court’s holding, it seems that companies now have only a few routes for maintaining a legal way to enforce single-use restrictions on a patented product—either contract with their customers to restrict resale of a patented product, and thereafter sue the customers under a contract theory, or structure the terms of restrictions in accordance with a “license to use” agreement to provide a patent infringement cause of action against a company obtaining the patented product despite being aware of such restrictions. The theoretical license agreement could either be a limited, nonexclusive license with the consuming customers or a manufacturing license with some third party, who would ultimately sell the manufactured product to the customers.

It should be apparent that a business strategy based on numerous lawsuits with individual customers is untenable. But why wouldn’t a company like Lexmark attempt to identify future buyback agreements with their customers as license agreements that form a licensor-licensee relationship? The cost of the proposed license would be the market price for the patented cartridges with some discount or benefit provided to the licensee-customer as compared with a customer that buys the patented product

free of restrictions. It doesn't seem that such companies would experience any significant added cost, and these companies would maintain a valid patent infringement suit against a competitor reselling the patented product (assuming that it could be proven that the competitor was aware of the terms of the license agreement associated with the initial sale).

Had Lexmark decided to enforce its single-use restrictions by granting a license to a third party allowing them to manufacture only cartridges that were to be filled by Lexmark or its subsidiaries, given that Impression Products was aware of such a restriction, the facts would mirror those of *General Talking Pictures*. The patentee (Lexmark) contracted with a licensee (third-party manufacture) dictating that the patented product (cartridge) be used in a specific field-of-use (single-use). Had the third party licensee made a sale outside the scope of the license to a purchaser (Impression Products), and the purchaser was aware of the restrictions, Lexmark's post-sale restriction should have been upheld under the Supreme Court's analysis.

Just as software companies have implemented end-user agreements as an end run around copyright's codified first sale doctrine, we may see patent holders taking

affirmative measures to maintain patent rights with respect to sold items. Such patent holders may contract with a licensee-manufacturer whose sales are subject to use-related restrictions or may attempt to structure each individual sale of the subject patented articles as an extremely narrow, nonexclusive license binding each end user to the same use-related restrictions. What legal theory may be used by the patent holders to successfully enforce these restrictions remains less than perfectly clear.

Accordingly, it seems that businesses that identify a licensor-licensee relationship with their customers will maintain an avenue of recourse in a patent infringement action, even though such recourse would potentially include action against their customer-licensees. This would, therefore, provide a level of downstream control of the patented products, something that seems to be at odds with the base notion of patent exhaustion. Should another company ever come into possession of such restricted patented products, they may be shielded from liability if it cannot be shown that they were aware of the terms of such restrictions contained in the subject license agreement.

But should the patent laws be allowed to be used in such a way? As indicated by the Supreme Court, selling a patented

product ends the patentee's rights to how that product is legally used. If the results of the patent exhaustion doctrine provide a public good, and if that public good is valued over that of the interests of companies like Lexmark, it may be necessary for the Supreme Court to eventually overrule *General Talking Pictures*, just as it overruled *A.B. Dick*. Alternatively, Congress may need to take action to clarify the patent exhaustion doctrine. ■

¹ Impression Prods., Inc. v. Lexmark Int'l, Inc., 137 S. Ct. 1523 (U.S. 2017).

² U.S. CONST. art. I, §8, cl. 8.

³ Henry v. A.B. Dick Co., 224 U.S. 1 (U.S. 1912).

⁴ *Id.* at 12.

⁵ *Id.* at 53.

⁶ Motion Picture Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502 (U.S. 1917).

⁷ *Id.* at 516.

⁸ General Talking Pictures Corp. v. Western Elec. Co., 304 U.S. 175 (U.S. 1938).

⁹ *Id.* at 182.

¹⁰ *Id.*

¹¹ Impression Prods., Inc. v. Lexmark Int'l, Inc., 137 S. Ct. 1523, 1535 (U.S. 2017).

¹² *Id.* at 1535, citing *General Talking Pictures*, 304 U.S. 175 at 181-82 (emphasis in original).

¹³ Impression Prods., 137 S. Ct. at 1535.

¹⁴ *Id.* at 1534-35.

¹⁵ *Id.* at 1535 (emphasis in original).

¹⁶ *Id.*

¹⁷ *Id.*

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