IMPRESSION PRODUCTS, INC. V. LEXMARK INTERNATIONAL, INC.

POST-SALE RESTRICTIONS AND FOREIGN SALES DO NOT AVOID PATENT EXHAUSTION

June 1, 2017

In a nearly unanimous decision delivered May 30, 2017 by Chief Justice Roberts in *Impression Prods., Inc. v. Lexmark Int'l, Inc.*,[1] the U.S. 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." The Court's decisive opinion overturned more than 25 years of lower court precedent, including that of the Court of Appeals for the Federal Circuit, and rejected the notion that a patent owner can enforce its patent against downstream purchasers – even when it sells its product with express restrictions on post-sale use or resale, or sells its product abroad.

This case arose from a dispute between Lexmark International, Inc., a manufacturer and seller of patented toner cartridges for laser printers, and Impression Products, Inc., a remanufacturer that acquired and refilled used Lexmark cartridges for resale at a lower price. Customers buying cartridges from Lexmark were given two purchase options: buy toner cartridges at full price with no restrictions, or buy toner cartridges at a discount under a "Return Program" that required the customer to sign an agreement promising not to transfer empty cartridges to anyone other than Lexmark. To help protect its Return Program, Lexmark installed microchips on its cartridges to prevent refilling and reuse. Impression Products, among other remanufacturers, knew of Lexmark's purchase agreements but nevertheless acquired empty Lexmark cartridges and developed a way to circumvent the microchips, allowing the cartridges to be refilled and resold at a discount. In 2010, Lexmark sued several remanufacturers, including Impression Products, for patent infringement. While most of those cases settled or otherwise resolved, the dispute with Impression Products continued on to the Supreme Court.

A U.S. patent bestows an exclusionary right on the patent owner – namely, "the 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 U.S.C. §154(a). Anyone who engages in such acts without authority from the patent owner is liable for patent infringement under 35 U.S.C. §271(a).

For over 160 years, however, the doctrine of patent exhaustion has limited this right to exclude, generally extinguishing the patent owner's rights after the patented product is purchased by a consumer, with possible exceptions according to some pre-*Lexmark* courts. For instance, in *Mallinckrodt, Inc. v. Medipart, Inc.*, 976 F. 2d 700 (Fed. Cir. 1992), the Federal Circuit held that a manufacturer of patented medical devices sold to hospitals with an explicit "single use only" restriction could assert a claim of patent infringement against a downstream servicing company that rendered the devices suitable for reuse without authorization by the patentee. The Federal Circuit relied on its *Mallinckrodt* decision, among other Federal Circuit and Supreme Court decisions, when considering *Impression Prods.*, and similarly concluded that when a resale violates an express and valid restriction imposed by the patentee on the initial purchaser, the resale is made "without authority" of the patentee and thus may be remedied under patent law, provided that no other law prevents enforcement of the patent.

In Lexmark's suit against Impression Products, the claim of patent infringement was based on two groups of products sold by the remanufacturer: Return Program cartridges resold in the United States, which Lexmark argued were unauthorized sales because it had expressly prohibited cartridge reuse and resale; and cartridges imported from abroad and resold in the United States, which Lexmark argued were unauthorized sales because it had not given anyone permission to import its foreign-sold cartridges back into the country. Accordingly, the case centered on two issues – the viability of post-sale restrictions, and the existence of foreign exhaustion. More specifically, the Court addressed: (i) whether a patentee that sells an item with an express restriction on the purchaser's right to reuse or resell the product may enforce that restriction through a patent infringement lawsuit, and (ii) whether a patentee exhausts its patent rights when it sells its product outside the United States.

Post-Sale Restrictions. In assessing whether a patent owner can retain and enforce patent rights by subjecting customers to express restrictions on downstream sales, the Court relied heavily on the common law principle against restraints on alienation – i.e., limits on a purchaser's ability to resell or otherwise dispose of a product. Quoting the 17th century writings of Lord Coke, the Court made clear that post-sale restrictions do not create an exception to the patent exhaustion doctrine, which is grounded in this "venerable principle" against "hateful" restraints on alienation. In other words, patent rights strictly end at the moment of sale. Consequently, Lexmark was instantly cut off from any remedy under patent law at the time it sold its Return Program cartridges, regardless of any restrictions it placed on those sales.

The Court reasoned that "the purpose of the patent law is fulfilled … when the patentee has received his reward for the use of his invention." That is, the patentee is free to set the price for its product and collect its reward, but has no right under the patent laws to further restrict the use and enjoyment of the thing that is sold. The Court illustrated this reasoning by reference to its early twentieth century decision in *Boston Store of Chicago v. American Graphophone Co*., 246 U.S. 8, 17-18 (1918), in which a graphophone manufacturer contracted with retailers to resell at a specific price, and brought a patent infringement suit against a retailer who sold for less. In *Boston Store*, the Court unequivocally concluded that the details of the contract did not extend the reach of the manufacturer's patent rights. Rather, "[b]y selling the item, the manufacturer placed it 'beyond the confines of the patent law, [and] could not, by qualifying restrictions as to use, keep [it] under the patent monopoly."

Notably, the Court also made clear that contract law remains an option, and possibly the only option, for restricting downstream customer use and resale, assuming such restrictions do not run afoul of antitrust or other laws. Hence, even if a patent owner cannot sue for patent infringement, it could potentially sue for breach of contract. While in many cases, including that of Lexmark, this option may be undesirable as it would involve suing customers, other situations such as that of the *Boston Store* manufacturer, might be effectively resolved under contract law if the contract terms do not unreasonably restrain trade.

Foreign Exhaustion. In considering whether foreign sales exhaust patent rights, the court analogized the patent exhaustion doctrine to the first sale doctrine under copyright law, which is 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 cannot then restrict the purchaser's freedom to sell or otherwise dispose of that copy. Although there is nothing in the copyright statute that limits this doctrine geographically, the Court concluded that no geographical distinctions were intended since the first sale doctrine originated from the common law principle against restraints on alienation of chattels, which has no geographical limit. Hence, the Court reasoned that since both doctrines are rooted in "the antipathy toward restraints on alienation," both should be consistently interpreted as borderless. The Court further supported its conclusion by observing that the patent exhaustion and copyright first sale doctrines share a "strong similarity … and identity of purpose" and a "historic kinship," and that many consumer products are protected by both patents and copyrights, making it impractical and nonsensical to recognize a geographic distinction for one and not the other.

The United States submitted an *amicus* brief advocating for a middle ground position wherein a foreign sale would only exhaust a patentee's rights if it was made without an express reservation of such rights. However, the Court rejected this position along with "a smattering of lower court decisions [that] mentioned this express-reservation rule for foreign sales," including a 2001 Federal Circuit decision in *Jazz Photo Corp.* v. *International Trade Commission*, 264 F. 3d 1094, 1105 (Fed. Cir. 2001), which set forth a “blanket rule that foreign sales do not trigger exhaustion, even if the patentee fails to expressly reserve its rights.”

In summary, the Court held fast to global principles against restraint on alienation, leaving parties to address post-sale disputes through contract law, not patent law.

In Justice Ginsberg’s opinion, she concurred with the holding on domestic exhaustion, but dissented from the holding on foreign exhaustion. In her view, since U.S. patents offer no protection abroad, foreign sales should not diminish the protections of U.S. law in the United States. She also criticized the Court’s analogy to copyright law since copyright protections are generally harmonized across countries whereas patent protection varies greatly since each country may uphold “different policy judgments about the relative rights of inventors, competitors, and the public in patented inventions.”

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[1] *Impression Prods., Inc. v. Lexmark Int’l, Inc.*, No. 15-1189, slip op. (U.S. May 30, 2017). All of the justices joined Chief Justice Roberts’ opinion except for Justice Ginsburg who filed an opinion concurring in part and dissenting in part, and Justice Gorsuch who took no part in the decision.