WILL *LEXMARK* INTRODUCE INTERNATIONAL PATENT EXHAUSTION TO AMERICA?[*]

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I. OVERVIEW

In *Lexmark International, Inc. v. Impression Products, Inc*., No. 2014-1617, either the Federal Circuit or the Supreme Court on review is expected to determine whether the United States should adopt international patent exhaustion. Such a view would, if adopted, overrule *Jazz Photo v. International Trade Commission*, 264 F.3d 1094 (Fed. Cir. 2001), that is basis for denial of this doctrine. Under international patent exhaustion, if adopted, the holder of parallel patents in the United States and a foreign country would lose all right to enforce his United States patent against the offshore purchaser of his patented product.

Lexmark could reach the Supreme Court as early as the Fall of 2016. First, however, *Lexmark* must go through an *en banc* argument and decision at the Federal Circuit. Depending upon what happens at the Federal Circuit, there may well be grant of *certiorari* in this very important case.

If *Lexmark* does reach the Supreme Court, this would be a case of first impression at that level. *See* § II, *A Case of First Impression for the Supreme Court.* To be sure, *domestic* patent exhaustion has been well settled through a number of cases dating back to the nineteenth century. *See* § II-A, *From Adams v. Burke to the Present Century.*

The controversy is squarely before the Federal Circuit in the *Lexmark* case. *Should* the *en banc* Court sustain the holding in *Jazz Photo* denying international exhaustion, and if so, can the Federal Circuit successfully distinguish the patent situation from the establishment of international copyright exhaustion in *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S.Ct. 1351 (2012)? *See* § II-B, *Lexmark Case En Banc at the Federal Circuit*

To understand whether the holding in *Jazz Photo* should be sustained and, if so, how this can be successfully accomplished, it is useful to see *Jazz Photo* in the context of historical precedent. *See* § III, *Jazz Photo in the Context of Precedent.*

II. A CASE OF FIRST IMPRESSION FOR THE SUPREME COURT

A. From *Adams v. Burke* to the Present Century

The Supreme Court as early as Fall 2016 may entertain arguments in a case of first impression at that tribunal: Where a patentee has parallel patents in both a foreign country and the United States and sells his product in the foreign country, does such first sale "exhaust" his patent rights as to that product in the United States?

Today, the answer is in the negative, there is no international patent exhaustion in the United States.

There are critical reasons *why* the denial of international patent exhaustion is very important for the United States which are chronicled even by critics of the American position. *See* Clugston, *International Exhaustion, Parallel Imports, and the Conflict between the Patent and Copyright Laws of the United States,* 4 Beijing L. Rev. No. 3, 95-99 (2013).

At the end of the last century the economic interests of the United States and developed country allies in the Uruguay Round leading up to the TRIPS were successful in creating an intellectual property trade treaty: Almost all points pushed by the United States were successfully included in the ultimate TRIPS treaty. The most significant TRIPS defeat for the United States was the inclusion of TRIPS Article 6 that *excluded* any consideration of the denial of international exhaustion from the treaty. *Id.*

Until now, the Federal Circuit has denied the existence of international patent exhaustion under its notorious opinion in *Jazz Photo*: The entire reasoning of the leading case is that the Federal Circuit is bound by *Boesch v. Graff*, 133 U.S. 697 (1890), a case having a holding having absolutely nothing to do with exhaustion of patent rights: The patent owner did not "exhaust" his rights through the first sale of products imported in the United States because the patent owner had nothing to do with the sale of such products; the "first sale" was by the patentee's *competitor*.

B. Lexmark Case *En Banc* at the Federal Circuit

The international patent exhaustion road to the Supreme Court is routed through the Federal Circuit. The appellate court decided on April 14, 2015, to entertain an *en banc* argument in *Lexmark.* The first of two issues[*] presented in *Lexmark* is whether an overseas "first sale" exhausts parallel patent rights in the United States:

> "In light of *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S.Ct. 1351 (2012) should this court overrule *Jazz Photo v. International Trade Commission*, 264 F.3d 1094 (Fed. Cir. 2001), to the extent [*Jazz Photo*] ruled that a sale of a patented item outside the United States never gives rise to United States patent exhaustion."

It is likely that an *en banc* decision will be reached very late in 2015 or early in 2016, so that under such a situation the earliest likely hearing at the Supreme Court would be in the October 2016 Term that runs through June 2017, *if* the Supreme Court were to grant *certiorari*.

To the extent that the *en banc* Court continues to deny the existence of international patent exhaustion *solely* based upon *Jazz Photo* without meaningful distinction of the policy reasons implicated in *Kirtsaeng*, there could be a significant chance for grant of *certiorari.*

[*]The *second* issue asks: "In light of *Quanta Computer, Inc. v. LG Electronics, Inc.*, 553 U.S. 617 (2008), should this court overrule *Mallinckrodt, Inc. v. Medipart, Inc.*, 976 F.2d 700 (Fed. Cir. 1992), to the extent [that *Mallinckrodt*] ruled that a sale of a patented article, when the sale is made under a restriction that is otherwise lawful and within the scope of the patent grant, does not give rise to patent exhaustion?"

III. *JAZZ PHOTO* IN THE CONTEXT OF PRECEDENT

If *Jazz Photo* is simply rubberstamped as binding *because* of *Boesch v. Graff* it is difficult to see how anyone can disagree with critics of the American position on international patent exhaustion. As pointed out in an overseas law journal by a critic of the American viewpoint:

> "[T]he Federal Circuit's continued opposition to international exhaustion in patent law is untenable. The *Jazz Photo* line of cases improperly relies on *Boesch* [*v. Graff*] as precedent and is, thus, legally unsound. … [T]he *Boesch* [*v. Graff*] case does not involve a first sale by or under the authority of the patent owner. Such a sale can have no effect whatsoever on the importation rights of the patentee."

Clugston, 4 Beijing L. Rev. at 98.

A. Historic International Patent Exhaustion

"Patent exhaustion" is the doctrine whereby a patent owner on his "first sale" loses all right to control the use or resale of patented goods. After the patent owner has received his reward through the first sale, the customer is then free to resell or otherwise dispose of the patented product free from the now "exhausted" patent right.

As explained by the Supreme Court in *Quanta Computer*:

"The longstanding doctrine of patent exhaustion provides that the initial authorized sale of a patented item terminates all patent rights to that item. This Court first applied the doctrine in 19th-century cases addressing patent extensions on the Woodworth planing machine. Purchasers of licenses to sell and use the machine for the duration of the original patent term sought to continue using the licenses through the extended term. The Court held that the extension of the patent term did not affect the rights already secured by purchasers who bought the item for use 'in the ordinary pursuits of life.' *Bloomer* v. *McQuewan***,** 55 U.S. (14 How.) 539, 549 (1853); see also *ibid.* ('[W]hen the machine passes to the hands of the purchaser, it is no longer within the limits of the monopoly'); *Bloomer* v. *Millinger*, 68 U.S. (1 Wall.) 340, 351 (1864). In *Adams* v. *Burke*, 84 U.S. (17 Wall.) 453 (1873), the Court affirmed the dismissal of a patent holder's suit alleging that a licensee had violated postsale restrictions on where patented coffin-lids could be used. '[W]here a person ha[s] purchased a patented machine of the patentee or his assignee,' the Court held, 'this purchase carrie[s] with it the right to the use of that machine so long as it [is] capable of use.' *Id.*, 84 U.S. (17 Wall.) at 455."

Quanta Computer, 533 U.S.at 625.

International patent exhaustion refers to the situation where the patentee holds parallel patents in two countries, a first sale occurs in the first country, and the purchaser then resells the patented product in the second country without further permission from the patentee.

Countries that permit such resale are said to follow a doctrine of international patent exhaustion.

Other countries say that the territorial limits of the patent right mean that a *separate* royalty or tribute is necessary for each country. This is a *denial* of the doctrine of international patent exhaustion.

B. Global Public Policy Considerations

International exhaustion is one of the most contentious points of international patent trade discussions. While many developing countries have adopted international patent exhaustion, there has also been adoption of international patent exhaustion within the developed countries of the world. Within the European Union, there is now a doctrine of international patent exhaustion for a first sale in a member state so that, for example, the purchaser of pharmaceuticals on the open market in the United Kingdom is able to export the thus-purchased products to Germany and Holland free from patent infringement. Japan has adopted international patent exhaustion with the exception that there is no exhaustion where the purchaser is on notice of the patent right.

In the negotiations leading up to the 1994 Marakesh Agreement establishing the TRIPS, the United States was able to lead a coalition of developed countries to striking victories to establish minimum standards of patent protection that favored strong patent rights.

The one area where victory could not be achieved in Marakesh was the establishment of a standard *denying* international patent exhaustion. To avoid any possibility that future panels of the World Trade Organization deciding disputes under the TRIPS could reach this issue, the developing countries insisted upon an express provision in the TRIPS that makes it clear that international exhaustion was *not* a topic of agreement.

Hence, the express statement is found in the Treaty itself that "[f]or the purposes of dispute settlement under this Agreement, subject to the provisions of [TRIPS] Articles 3 [providing for national treatment] and 4 [providing most-favored-nation treatment,] nothing in this [TRIPS] Agreement shall be used to address the issue of the exhaustion of intellectual property rights." TRIPS, Article 6.

C. *Jazz Photo,* the Law of the Federal Circuit

In the United States, the Supreme Court has never had a holding on all fours to either embrace or deny the doctrine of international patent exhaustion, despite a rich history of *domestic* patent exhaustion jurisprudence.

Filling this vacuum, the Federal Circuit *denied* the application of international patent exhaustion in its 2001 *Jazz Photo* decision.

Jazz Photo is a problematic opinion from the standpoint that as a case of first impression at the Federal Circuit it considered none of the policy arguments for or against international patent exhaustion and provided no reasoning at all, other than to rely upon what it inferred was binding Supreme Court precedent, while the holding had nothing to do with an issue of exhaustion.

1. A Holding Keyed to Precedent Unrelated to Exhaustion

The entire basis for the holding denying international exhaustion in *Jazz Photo* is set forth in less than seventy-five words:

> United States patent rights are not exhausted by products of foreign provenance. To invoke the protection of the first sale doctrine, the authorized first sale must have occurred under the United States patent. See *Boesch v. Graff*, 133 U.S. 697, 701-703 (1890) (a lawful foreign purchase does not obviate the need for license from the United States patentee before importation into and sale in the United States).

Jazz Photo, 264 F.3d at 1105.

The holding in *Boesch v. Graff* had absolutely nothing to do with "exhaustion" of the patentee's right through a first sale of goods by the patentee, because the goods in question were *not* purchased from the patentee: How can *the patentee* "exhaust" *his* right if the goods in question are purchased from a competitor who did not operate under license or otherwise take title from the patentee? Thus, the patentees held parallel patents in both Germany and the United States for their patented burners, while competitor Hecht sold the burners in Germany *but without license from the patentee.* There clearly could never have been a question of exhaustion – domestic or international – because as to the German burners resold in the United States the patentee *never had title to the burners.* Since the provenance of the burners cannot be traced back to the patentee – nor to anyone taking title from the patentee – the patentee could not have "exhausted" his rights under the German patent because the goods that were sold were not his goods.

In fact, the burners were obtained from a third party, one Hecht, who operated outside the patent under the German prior user right statute because Hecht had made such burners before the critical date of the German patent:

"By section 5 of the imperial patent law of Germany, of May 25, 1877, it was provided that 'the patent does not affect persons who, at the time of the patentee's application, have already commenced to make use of the invention in the country, or made the preparations requisite for such use.' 12 O. G. 183. Hecht had made preparations to manufacture the burners prior to the application for the German patent. The official report of a prosecution against Hecht in the first criminal division of the royal district court, No. 1, at Berlin, in its session of March 1, 1882, for an infringement of the patent law, was put in evidence; wherefrom it appeared that he was found not guilty, and judgment for costs given in his favor, upon the ground 'that the defendant has already prior to November 14, 1879,—that is to say, at the time of the application by the patentees for and within the state,—made use of the invention in question, especially, however, had made the necessary preparations for its use. Section 5 [ ]. Thus [the] patent is of no effect against him, and he had to be acquitted accordingly.'"

Boesch v. Graff, 133 U.S. at 701-02.

The issue of exhaustion as being based on *the patentee* exhausting his patent right is underscored:

"The inventor might lawfully sell [his patented product to a purchaser], whether he had a patent or not…. And when the machine passes to the hands of the purchaser it is no longer within the limits of the monopoly. It passes outside of it, and is no longer under the protection of the act of congress.' In Adams v. Burke, 84 U.S. (17 Wall.) 453 (1873), it was held that 'where a patentee has assigned his right to manufacture, sell, and use within a limited district an instrument, machine, or other manufactured product, a purchaser of such instrument or machine, when rightfully bought within the prescribed limits, acquires by such purchase the right to use it anywhere, without reference to other assignments of territorial rights by the same patentee;' and that 'the right to the use of such machines or instruments stands on a

different ground from the right to make and sell them, and inheres in the nature of a contract of purchase, which carries no implied limitation to the right of use within a given locality.' Mr. Justice BRADLEY, with whom concurred Mr. Justice SWAYNE and Mr. Justice STRONG, dissented, holding that the assignee's interest 'was limited in locality, both as to manufacture and use.'"

Boesch v. Graff, 133 U.S. at 702-03.

To be sure, there is also *dicta* that, isolated and standing alone, supports the view of *Jazz Photo: "*A prior foreign patent operates under our law to limit the duration of the subsequent patent here, but that is all. The sale of articles in the United States under a United States patent cannot be controlled by foreign laws." *Boesch v. Graff*, 133 U.S. at 703.

2. Déjà vu: Later Cases Echoing *Jazz Photo*

Since *Jazz Photo* the subsequent panels of the Federal Circuit have totally ducked or largely avoided the issue and merely cited *Jazz Photo* as precedent to be followed. *See FujiFilm Corp. v. Benum,* 605 F.3d 1366 (Fed. Cir. 2010)(per curiam)(Michel, C.J., Mayer, Linn, JJ.); *see Fuji Photo Film Co., Ltd. v. International Trade Com'n,* 474 F.3d 1281, 1285 (Fed. Cir. 2007)(Dyk, J.)(discussing *Jazz Photo Corp. v. United States,* 439 F.3d 1344 (Fed.Cir.2006); *Fuji Photo Film Co. v. Jazz Photo Corp.,* 394 F.3d 1368 (Fed.Cir.2005); *Fuji Photo Film Co. v. Int'l Trade Comm'n,* 386 F.3d 1095 (Fed.Cir.2004).

D. *Kirtsaeng* Adoption of International Copyright Exhaustion

The *Kirtsaeng* establishment of a doctrine of international intellectual property rights exhaustion was in the context of copyright law.

The issue in *Kirtsaeng* as phrased by the majority was "whether the 'first sale' doctrine applies to protect a buyer or other lawful owner of a copy (of a copyrighted work) lawfully manufactured abroad. Can that buyer bring that copy into the United States (and sell it or give it away) without obtaining permission to do so from the copyright owner? Can, for example, someone who purchases, say at a used bookstore, a book printed abroad subsequently resell it without the copyright owner's permission?" *Kirtsaeng,* 133 S.Ct. at 1355.

The Court held that international exhaustion *does* apply: " In our view, the answers to these questions are, yes. We hold that the 'first sale' doctrine applies to copies of a copyrighted work lawfully made abroad. "*Kirtsaeng*, 133 S.Ct. at 1355-56.

While the *Kirtsaeng* case dealt with specific statutory language relevant to copyright law, nevertheless the majority opinion delved deeply into policy considerations including the history of the law in England:

The "first sale" doctrine is a common-law doctrine with an impeccable historic pedigree. In the early 17th century Lord Coke explained the common law's refusal to permit restraints on the alienation of chattels. Referring to Littleton, who wrote in the 15th century, Gray, Two Contributions to Coke Studies, 72 U. Chi. L.Rev. 1127, 1135 (2005), Lord Coke wrote:

"[If] a man be possessed of ... a horse, or of any other chattell ... and give or sell his whole interest ... therein upon condition that the Donee or Vendee shall not alien[ate] the same, the [condition] is voi[d], because his whole interest ... is out of him, so as he hath no possibilit[y] of a Reverter, and it is against Trade and Traffi[c], and bargaining and contracting betwee[n] man and man: and it is within the reason of our Author that it should ouster him of all power given to him." 1 E. Coke, Institutes of the Laws of England § 360, p. 223 (1628).

A law that permits a copyright holder to control the resale or other disposition of a chattel once sold is similarly "against Trade and Traffi[c], and bargaining and contracting." *Ibid.*

With these last few words, Coke emphasizes the importance of leaving buyers of goods free to compete with each other when reselling or otherwise disposing of those goods. American law too has generally thought that competition, including freedom to resell, can work to the advantage of the consumer. See, e.g., *Leegin Creative Leather Products, Inc. v. PSKS, Inc*., 551 U.S. 877, 886 (2007)(restraints with "manifestly anticompetitive effects" are per se illegal; others are subject to the rule of reason (internal quotation marks omitted)); 1 P. Areeda & H. Hovenkamp, Antitrust Law ¶ 100, p. 4 (3d ed. 2006) ("[T]he principal objective of antitrust policy is to maximize consumer welfare by encouraging firms to behave competitively").

The "first sale" doctrine also frees courts from the administrative burden of trying to enforce restrictions upon difficult-to-trace, readily movable goods. And it avoids the selective enforcement inherent in any such effort. Thus, it is not surprising that for at least a century the "first sale" doctrine has played an important role in American copyright law. See *Bobbs–Merrill Co. v. Straus*, 210 U.S. 339 (1908); Copyright Act of 1909, § 41, 35 Stat. 1084.

See also Copyright Law Revision, Further Discussions and Comments on Preliminary Draft for Revised U.S. Copyright Law, 88th Cong., 2d Sess., pt. 4, p. 212 (Comm. Print 1964) (Irwin Karp of Authors' League of America expressing concern for "the very basic concept of copyright law that, once you've sold a copy legally, you can't restrict its resale").

Kirtsaeng, 133 S.Ct. at 1363.

E. Last Chance to Deny International Patent Exhaustion

Jazz Photo has had a remarkable history as precedent, given the shallow treatment of the issue at hand. *Jazz Photo* It survived review in the wake of *Quanta Computer, Inc. v. LG Electronics, Inc.*, 533 U.S. 617 (2008). *See* Harold C. Wegner, *Post-Quanta, Post-Sale Patentee Controls*, 7 J. Marshall Rev. Intell. Prop. L. 682, 698 (2008). It is now nearly fifteen years since the simple, remarkable decision in *Jazz Photo* where the Court has had ample time to provide policy reasons for or against the doctrine of international patent exhaustion.

The Federal Circuit took the right approach in granting *en banc* review of *Jazz Photo*. Whether the holding in that case was right or wrong, the reasoning of *Jazz Photo* is manifestly deficient. The Federal Circuit now has an opportunity to revisit *Jazz Photo* anew and either conform its decision in conflict with *Kirtsaeng* or provide a better supported argument favoring retention of its holding.

IV. CONCLUSION

The clock is running out. A decision in *Lexmark* simply reaffirming the *result* in *Jazz Photo* should be ripe for Supreme Court review. The writer expresses no view, here, whether the *holding* in *Jazz Photo* is right or wrong.[*]

It now remains to be seen whether the Federal Circuit will be able to sustain the *holding* in *Jazz Photo* while repudiating the reasoning of that case, providing instead arguments distinguishing the patent situation from *Kirtsaeng* and demonstrating the public policy reasons to support the holding.

Reaffirming the holding in *Jazz Photo* without making a meaningful distinction of *Kirtsaeng* would be a gold plated invitation to the Supreme Court to grant *certiorari* to permit Supreme Court merits review of international patent exhaustion.

[*] The point of this paper is *not* to argue the merits or demerits of international patent exhaustion. The author's views on the merits are well known through his writings and speeches. *See, e.g., Negram: The Common Market-Wide Exhaustion of Patent Rights Through Territorial Licenses*, 57 JOUR. PAT. & TRADEMARK OFF. SOCY 46 (1975) (coauthor with F. Müller); *Parallel Imports of Patented Goods: Killing the Technology Transfer Goose*, paper presented to the Licensing Executives Society (France), Paris, May 1998 ; and presentation at the Fordham University School of Law, Sixth Annual Conference on International Intellectual Property Law & Policy, Apr. 16-17, 1998; *Parallel Imports*, lecture to Peking University Law Faculty, May 1994; *Parallel Import Practice Restored in Japan: Negating the Implied License to Resell a Patented Product*, privately circulated analysis of the 1997 Japanese Supreme Court opinion keyed to the writer's appearance by affidavit as expert in pleadings before the court; *Japan AIPPI Gotemba Intellectual Property Law Conference*, Gotemba, Japan, September 29-30, 1995; *Patent Parallel Imports in Japan, Consumer Promise or Patent Peril: The Aluminum Wheels Parallel Import Case* (www.foleylardner.com) (1995); *Japan Violation of Patent Trade Principles - Impact, Consequences and Dealing with the Decision Permitting Patent Parallel Imports into Japan*, Dinwoodey Center White Paper, April 28, 1995;