US Supreme Court rules in landmark case on patent exhaustion

Recently, the Supreme Court of the United States issued one of the most important patent decisions in the US. In *Impression Products, Inc. v. Lexmark International, Inc.*, the Supreme Court ruled that restrictions by contract and location are irrelevant for patent exhaustion; what matters is the patentee’s decision to make a sale. After this authorised first sale, whether within US territory or abroad, the patentee can no longer rely on patent protection in the US for the product concerned. This means that the Supreme Court has embraced a worldwide exhaustion principle. Proprietors of US patents, especially those currently benefitting from revenue from post-sale restrictions or licensing restrictions (which are generally difficult or impractical to enforce on the basis of contract law) are advised to reassess their business models.

When a patentee, or other party authorised by the patentee, sells one of his patented products, the patent rights on this product are exhausted, meaning the patentee can no longer control the further sale of that product on the basis of patent law. This is called the patent exhaustion doctrine. In *Impression Products, Inc. v. Lexmark International, Inc.*, a case regarding the reselling of toner cartridges for laser printers, the Supreme Court ruled that the authorised sale of a patented product, including sales outside the US, bars the patentee from relying on patent protection in the US.

Factual background of the dispute
Lexmark designs, manufactures and sells toner cartridges to consumers in the US and abroad and is the owner of several patents relating to those cartridges. Lexmark gives its purchasers two options: buy them at full price, no strings attached, or buy them at a discount in the Lexmark Return Program and sign a contract agreeing to use the cartridge only once and refrain from transferring it to third parties. In the toner cartridges market, Lexmark has had to compete with "remanufacturers": parties that acquire empty Lexmark cartridges from purchasers in the US, including the Return Program purchasers, and from purchasers abroad, refill them with toner and resell them in the US. Unhappy with this course of events, Lexmark decided to sue these remanufacturers – amongst them, Impression Products – claiming that they infringe on its patents. The case against Impression Products reached the Supreme Court.

Supreme Court’s decision
The Supreme Court identified two legal issues: (i) one concerning the exhaustion of the patent rights in the Return Program cartridges sold and resold in the US, and (ii) the other concerning the exhaustion of patent rights in the cartridges sold abroad and resold in the US.
Regarding issue (i), the Supreme Court ruled that Lexmark’s patent rights in the US are exhausted on the basis of the principle that when a patentee decides to sell he consequently gives up his patent rights on that product. This principle is not altered when the patentee decides to conclude contracts with purchasers. These contracts, even when clear and enforceable under contract law, do not entitle Lexmark to retain patent rights in the product concerned. Lexmark, however, may be able to act towards the purchaser on the basis of contract law. As an aside, the Supreme Court clarified that patentees cannot use licensees to impose post-sale restrictions.

Regarding the issue under (ii), the Supreme Court also ruled that the rights were exhausted; even an authorised sale outside the US exhausts all rights under the US Patent Act. The Supreme Court reached this conclusion by drawing the analogy with international exhaustion that exists in the context of US copyright law (see Kirtsaeng v. John Wiley & Sons, Inc. on the import and sale in the US of foreign edition textbooks produced outside the US) and considering that applying patent exhaustion to foreign sales is just as straightforward. The rationale behind patent exhaustion is that the patentee decides to sell, and his reward for the invention lies in the remuneration he receives in exchange. Although the patentee may not be able to charge the same price for his products abroad – which was Lexmark’s argument – the US Patent Act does not guarantee a particular price, and the patentee was rewarded for his invention.

**Consequences**

At first glance, the decision has a major impact, especially the ruling on international patent exhaustion. It also raises questions, in particular: how does this decision relate to the current US policy on several global trade agreements?

With this decision, the Supreme Court has lowered the bar for cross-border trade in patented products. It will especially affect proprietors of US patents that sell pharmaceuticals outside the US. These companies, which sell their products at various prices – often at low prices in less developed countries – will now face third parties trying to import these products in the US and make a profit in the resale. The patentees facing such resale are advised to rethink their strategy, in particular in the low-price markets. At the same time, this could of course hamper access to medicines in less developed countries and it might be that regulatory bodies, such as the US Food & Drug Administration, limit the impact of the Supreme Court’s decision.

The decision in any event impacts patentees that currently rely on revenue from post-sale restrictions or licensing restrictions that are hard or impractical to enforce on the basis of contract law. These patentees in particular are advised to reassess their business models, especially any license agreements, as this ruling provides good reason to license at product level rather than at component level.

In addition, patentees facing limits on relying on patent law remedies are advised to look into their protection strategy and consider whether diversified branding would help, or whether protection by trade secret law might be a more viable option. For more detailed information on the new US federal trade secret law and what this means for your company, please see our earlier article.

Several online sources have already speculated on mechanisms for patentees to circumvent the Supreme Court’s ruling, such as setting up a business structure so that foreign sales will not be seen as sales authorised by the proprietor of a US patent. Other interpretation issues also arise, such as: will sales by the licensee that conflict with the licensing terms be seen as sales authorised by the patentee? More specifically; what
happens if the licensed product sold by the licensee does not fully comply with the product conditions in the licensing terms, or if the licensee sells more products than permitted by the patentee in the licensing terms?

It is likely that in US litigation, the focus will shift to the question of whether the first sale of the concerned products was indeed authorised and how to interpret “authorised”.

**Patent exhaustion in Europe**

Legislation at EU level on harmonised IP topics – patents excluded – departs from EU-wide exhaustion. With regard to national patents, the Court of Justice of the EU has ruled that once the patented product is sold by the patentee, or with his consent, in an EU member state, the patent rights on this product are exhausted in the EU. It is interesting to note that there is, in principle, no exhaustion of rights in the event of parallel imports and sales by a licensee beyond the scope of its license terms.

As the national and regional doctrines on exhaustion of IP rights in the US and Japan have undoubtedly played a role in the formation of the exhaustion doctrine in the EU, it will be interesting to see whether the Supreme Court’s decision will have a political impact in Europe as well.

In the new patent system (the Unified Patent Court and system of unified patents), exhaustion will also be on EU-wide basis. The [UPC Agreement](#) explicitly provides that the patent rights are exhausted if the patented product has been placed on the market in the EU by, or with the consent of, the patentee “unless there are legitimate grounds for the patent proprietor to oppose further commercialisation of the product”. As this new system has not yet been launched, it remains to be seen how this provision will be interpreted. For more information on this new patent system, see our earlier [article](#).