U.S. Supreme Court Expands Applicability of Patent Exhaustion Doctrine

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On May 30, 2017, the United States Supreme Court, in *Impression Products, Inc. v. Lexmark International, Inc.*, expanded the doctrine of patent exhaustion, further limiting a patent owner’s ability to control patented products post-sale.

Justice Roberts, writing for the majority, explains 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.” Reasoning that “[a]llowing patent rights to stick remora-like to that item as it flows through the market would violate the principle against restraints on alienation,” the Supreme Court overruled the Federal Circuit’s decades-old interpretation of the patent exhaustion doctrine. First, the Supreme Court unanimously decided (8-0) that exhaustion applies regardless of any restrictions the patentee purports to impose through, e.g., contractual terms. Second, the Supreme Court held (7-1, with Justice Ginsburg dissenting) that exhaustion applies to foreign sales and that a patentee’s decision to sell a product exhausts all of its rights, regardless of the location of the sale. The *Lexmark* decision marks another opinion from the Supreme Court that seemingly detracts from the rights of patent owners.

Patent litigants should expect to see the *Lexmark* decision potentially impacting their cases, where parties should further scrutinize all agreements (e.g., patent licenses or sales contracts) from the patent owner and agreements up and down the supply chain relating to any components that are allegedly implicated in a patent infringement suit. Where parties to an agreement have previously been able to avoid patent exhaustion by careful drafting or by making sales internationally, the *Lexmark* decision stands to force everyone to take a closer look at their agreements and the supply chain to fully understand its impact on business and potential exposure to patent infringement in the U.S. The decision potentially unleashes new patent exhaustion defenses that were not viable under prior Federal Circuit precedent, which may lead to an uptick in motion practice where the defense is viable. Litigants may also see a decrease of patent cases filed in the upcoming months as patent owners reassess their existing patent license agreements and list of potential infringers to determine whether the *Lexmark* decision has exhausted their patent rights.

The decision leaves potential disputes arising from post-sale activity (such as that between Lexmark and Impression) as a matter of contract law, but the viability of seeking remedies via breach of contract is also unclear. For example, suing for breach of contract may be cost prohibitive compared to a patent infringement suit where patentees have the potential to obtain injunctive relief. Breach of
contract actions, depending on the circumstances, may also raise antitrust issues (such as patent misuse) or present standing issues with respect to downstream buyers.

The Supreme Court’s ruling may reverberate the most in technology transactions where the effectiveness of thousands of existing patent license agreements may be placed in doubt, in particular where post-sale restrictions were integral terms to parties negotiating the agreement. Technology companies should anticipate revisiting their existing technology agreements and certainly accounting for the impact of the *Lexmark* decision on current and future negotiations.

If you have any questions concerning these developing issues, please do not hesitate to contact either of the following Paul Hastings Palo Alto lawyers:

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