Quanta: **Separating the Wheat from the Chaff**

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Owners of U.S. patents have the right to exclude unauthorized parties from, for example, using, making or selling protected technology throughout the country. Since Wilson v. Simpson, 50 U.S. 109 (1850), however, lawful first sales of items covered by patents presumptively give purchasers unrestricted rights to repair them. Likewise, Bloomer v. McQuewan, 55 U.S. 539, 549 (1852), holds that when a patented article "passes to the hands of a purchaser, it is no longer within the limits of the monopoly" — in that case, despite a patent term extension. In other words, patent rights are said to be exhausted by the first legitimate sale of a patented article.

Additional Supreme Court precedent on the exhaustion doctrine is scarce. Although the Court intended to address it in General Talking Pictures Corp. v. Western Electric Co., Inc., 305 U.S. 124 (1938), that was unnecessary once it was appreciated that the purchaser claiming rights was not among those to whom an otherwise authorized manufacturer was permitted to sell.

Such precedent, however, leaves many questions unanswered — including ones posed by Quanta Computer v. LG Electronics, argued before the Supreme Court on January 16. At the most basic level, the question might be framed as: When, if ever, may patent owners retain, by contract, rights otherwise implicitly exhausted by sale? Yet that seems to have been answered in United States v. Univis Lens Co., 316 U.S. 241 (1942). Because restrictions at issue there were interwoven with illegal price fixing, all were regarded as unacceptable. The Court nevertheless noted that some restrictions, "independently established, might have been used for lawful purposes." *Univis Lens,* 316 U.S. at 254.

The *Univis Lens* observation is merely dicta. If credited, however, resolution of *Quanta* should be confined to whether restrictions now under consideration serve lawful purposes. It seems to us that they do. They resolve, perhaps inelegantly, an earlier dispute between LG Electronics and Intel. By agreement, Intel acquired rights to make, use and sell patented LG chips, but sales were to convey limited title. In line with that, commercial purchasers, including Quanta, were informed and fully aware that use of chips in issue required a separate license from LG.

The district court found all of LG's patent rights to have been exhausted by Intel's clearly authorized sales, but the Federal Circuit reversed. Consistent with earlier circuit decisions as well as *Univis Lens,* it held that the exhaustion doctrine "does not apply to an expressly conditional sale or license." LG Electronics, Inc. v. Bizcom Electronics, Inc., 453 F.3d 1364, 1370 (Fed. Cir. 2006).

We regard Mallinckrodt, Inc. v. MediPart, Inc., 976 F.2d. 700 (Fed. Cir. 1992) as the circuit's most noteworthy precedent. There, an explicit single-use restriction on dangerous medical devices was not found per se inconsistent with purchasers' rights to have their patented devices repaired by MediPart. To have thwarted Mallinckrodt's

ability to prevent repair and reuse seems unwarranted. To void that restriction by rigid application of the exhaustion doctrine would have prevented Mallinckrodt from avoiding potentially serious harm to patients on whom the devices were used as well as concomitant tort liability.

Some seem to regard *Mallinckrodt* as evidence that the Circuit is hostile to the exhaustion doctrine. The converse, however, seems clear from Jazz Photo Corp. v. International Trade Commission, 264 F.3d 1094 (Fed. Cir. 2001). In some respects, the facts are similar, but the case presents no explicit restriction on purchasers' implied right to repair Fuji's disposable cameras, much less credible public risk. Thus, proxies such as Jazz were permitted to replace film and other components despite patents alleged to be infringed. Not only did the court find such replacement to fall within the ambit of precedent akin to the 1850 *Wilson* case, it refused to imply limits from Fuji's labeling. Indeed, one must wonder whether patentees might be obligated to justify explicit single-use restrictions in such cases. When reconditioned products can pose risks to original manufacturers' reputations, Champion Spark Plug v. Sanders, 331 U.S. 125 (1947), illustrates how they can be controlled by proper labeling.

As for *Quanta,* the challenge to LG's ability to rebut by contract what might otherwise be implied arises only because chips were bought from Intel. If justification is needed, LG's holding a patent on a system incorporating its chips as well as a patent on the chips themselves tends to supply it.

Had Intel made chips for sale by LG, there could be no quarrel with LG's ability to extract royalties under both patents. Likewise, had Intel sold only to parties already licensed under the second, it is difficult to see a basis for complaint. Quanta and other sophisticated parties knew exactly what they were (and were not) getting. Absent anti-trust based concerns, we see nothing warranting need for justification, much less for allowing Quanta to escaping the burden of limitations known in advance of purchase.

Should the Court disagree, however, it would be most unfortunate if the peculiar facts of *Quanta* were to wholly eliminate patentees' capacity to rebut by contract implied understandings reasonably imposed by the exhaustion doctrine.

No party in *Quanta* has had occasion to defend *Mallinckrodt,* but the facts in that case demonstrate a compelling need for some such capacity — particularly when it advances public safety. We therefore urge that the proverbial wheat not be discarded with anything regarded as chaff.

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