

Antitrust And Misuse Considerations Following Lexmark

By James Kobak

Law360, New York (June 19, 2017, 2:30 PM EDT) --

The U.S. Supreme Court in *Lexmark* held 8-0 (with Justice Neil Gorsuch not participating) that a patent owner's restrictions on resale of patented products in domestic transactions could not be enforced through infringement suits because all patent rights were exhausted by the first sale. This decision, authored by Chief Justice John Roberts, rejected the theory, first articulated by the Federal Circuit in *Mallinckrodt v. Medi Part Inc.*, 976 F. 2d 706 (Fed. Cir. 1992), that a patent owner could circumvent exhaustion by conditioning grant of its patent rights in a sales agreement as a legitimate means of obtaining compensation for the value of its invention.[1]



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What Happens Next?

The Supreme Court noted in *Lexmark* that contractual restrictions on the resale of patented products might still be enforceable as contracts in accordance with applicable commercial law. These contractual actions would not involve the same panoply of remedies as infringement suits and very likely would create no remedies at all against those not in privity with the patent owner. It is also easy to foresee the impracticality and loss of market goodwill that would be involved if a company instituted scores of law suits directed at its ultimate customer base. (See “3 Takeaways from the High Court’s Patent Exhaustion Ruling,” *Law 360* May 30, 2017).

The policy animating exhaustion, or as it is sometimes called the first sale doctrine, is to avoid a regime that will, in Justice Roberts’ words, “clog the channels of commerce” (slip opinion at 8) with restrictions that would prevent purchasers even several levels removed from the original seller from freely reselling, reusing, or repairing items they have purchased.

Patent owners and their licensees and purchasers will need to review existing restrictions and distribution arrangements in light of *Lexmark*. Patent owners will undoubtedly seek to find ways to tighten restrictions to achieve indirectly what *Lexmark* now prohibits directly. This will not be easy because *Lexmark* was based on very strong policy concerns. The court held that patent exhaustion functions automatically once a good is sold (slip opinion at 6), that exhaustion operates as an “unwritten limit on the scope of the patentee’s monopoly” (id. at 14), and that the Patent Act, like the common law, incorporates “enmity” toward restraints on alienation (id. at 7). But *Lexmark*’s adoption of this language and rejection of the *Mallinckrodt* rule may create more than just enforcement difficulties. They may also bring to bear renewed attention to antitrust and misuse theories.

Antitrust and Misuse Doctrines Come Into Play

With contractual limitations now definitively held to be outside the scope of a patentee's rights under the patent law, restrictions on sales of patented objects will be subject to unfair competition, antitrust and patent misuse law. Before *Lexmark*, under *Mallinckrodt*, cases seeking to enforce such restrictions were treated as infringement cases within the scope of the patent; the Federal Circuit, which has exclusive jurisdiction over patent cases, held that its law, not regional circuit law, would apply to such questions. In *Mallinckrodt* the Federal Circuit developed a two part misuse test that it has followed in a long series of cases. "The appropriate criterion is whether [a] restriction is reasonably within the patent grant, or whether the patentee has ventured beyond the patent grant and into behavior having an anticompetitive effect not justifiable under the rule of reason." (*Mallinckrodt*, 976 F. 2d 708). This test it created conflated misuse and antitrust principles but made reward related to the scope of a patent a key part of the analysis.

The Supreme Court has now determined that restrictions on downstream users are no part of a patent owner's legitimate reward and in fact are inimical to an important, if unwritten, principle of the patent laws. And with no special patent overlay, questions involving the interpretation, effect and legality of provisions imposing those restrictions should presumably now be determined in accordance with applicable regional federal circuit (and state) law.

Not only should the misuse and antitrust rules to be applied to restrictions on sales of patented goods no longer be those developed by the Federal Circuit, but also, in misuse cases, that part of the test that stressed conduct or contract provisions "reasonably within the patent grant" should no longer suffice to justify or even be relevant to a resale restriction. The Supreme Court confirmed in *Lexmark* that such a restriction is beyond the scope of the patent grant because of the long-standing "enmity" of patent and other law toward restraints on alienation.

Lexmark and Antitrust

Restrictions on sales imposed by a patent owner or its licensee should receive no benefit or special antitrust treatment after *Lexmark*. That means that patented products will simply stand on the same footing as other products. Vertical sales restrictions are now subject to rule of reason treatment under antitrust law, whether goods are patented or not, and regional circuit antitrust precedent (where differences among circuits can exist on the analysis of some claims) should now control all elements of the claim. (Previously the Federal Circuit applied its law exclusively to questions relating to scope or proper enforcement of patent and regional federal circuit law only to questions such as market power and antitrust inquiry.)

Lexmark and the Possible Revival of a Robust Misuse Defense

The effect of *Lexmark* on the misuse doctrine could be much more pronounced. This could pose significant potential dangers for patent owners — and potential unexpected benefits for infringers.

Misuse is not an antitrust doctrine but developed originally out of concern for use of the inherent power a patent might confer on a patentee to impose restrictions beyond the claims of a patent itself; this patent-extending conduct, whether accomplished through contract or otherwise, could not only be anti-competitive but, more importantly for purposes of misuse, was deemed inconsistent with the Patent Act's limitations on patent rights and the claiming system it mandates based on carefully defined claims

evaluated and granted by the patent office. Historically, the effect of finding of misuse could be extreme. Under the Supreme Court's Morton Salt decision (*Morton Salt Co. v. C.S. Suppiger Co.*, 314 U.S. 488 (1942)), a misused patent was held to be unenforceable until the practice constituting misuse was deemed to have been purged — an uncertain standard with few precedents for guidance.

In the possibly lengthy interval before purgation could be achieved, the patent was unenforceable against all potential purchasers. In *Morton Salt* the defendant was not a contracting party or even a third party like those in *Lexmark* and *Mallinckrodt* that failed to abide by contractual restrictions. Rather, the defendant who succeeded in using misuse as a complete defense to an infringement suit was a direct infringer who copied and used *Morton Salt*'s patented invention — and in fact itself engaged in the same practice — tying — held to be misuse as practiced by *Morton Salt*.

Morton Salt and classic misuse cases, though concerned in part with effects on competition, did not rely on antitrust principles or require detailed market power findings to establish misuse. *Morton Salt* affirmed a grant of summary judgment dismissing the infringement case on the basis of a contractual restriction in a single contract with a non-party to the suit. The Supreme Court specifically rejected any necessity of proof of further market impact or competitive effects.

This is not to say that misuse is likely to be restored post-*Lexmark* in all its pre-*Mallinckrodt* vigor. Over time, even before the Federal Circuit largely occupied the field, some courts added a measure of market-based antitrust analysis to the *Morton Salt* approach for any practice not held to have been *per se* illegal by the Supreme Court. (Judge Richard Posner was a leading proponent of this approach. See *USM Corp. v. SPS Technologies Inc.*, 69F. 2d 505 (7th Cir. 1982).) Congress also stepped in twice, in 1952 (35 U.S.C. §271 (d)(1)-(3)) and again in 1988 (35 U.S.C. §271(d)(4)-(5)), to narrow the scope of misuse for tying, the conduct at issue in *Morton Salt*. The statute now requires a showing of market power in the tying product or technology (which may not be presumed from the existence of the patent) as well as conditioning and other factors before misuse may be found.

It is therefore unlikely that many restrictions will be condemned on a strict *per se* basis. It is also possible that courts may, with more experience, temper the doctrine of unenforceability until purge. But this does not mean the potential for revival of a newly robust misuse doctrine can be safely ignored. Misuse may still be found on the basis of a showing of patent extension requiring far less proof than an antitrust case, and its effect on enforcement of patents could be severe. Misuse also poses a potent potential defense that may be exploited by innovative defense counsel to complicate otherwise straightforward infringement cases. And the process of exploiting it could lead to extensive discovery about a patent owner's marketing and licensing practices.

Conclusion

Lexmark poses constraints on patent owners' ability to use patent law to control distribution or reuse of products embodying their inventions. Misuse (and to some extent antitrust and unfair competition) may pose additional constraints and risks on efforts to revamp distribution and licensing schemes in the wake of *Lexmark*. Some restrictions such as tie-ins governed by statute will not be affected by a renewed misuse doctrine while others such as import or reuse restrictions would be likely candidates for its application. Much will depend on context and the manner in which enforcement is attempted. The possibilities for a successful misuse defense cannot be fully analyzed in a vacuum or catalogued in the compass of a short article, but they are possibilities that anyone needing to deal with *Lexmark* will need to address.

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[1] The Supreme Court, over Justice Ginsburg's dissent, also applied the exhaustion doctrine to sales made by the patent owner outside the United States even though the patent owner could have no patent rights to condition at the point of sale. I believe that Justice Ginsburg actually had the better of this argument, at least as a matter of theory if not practicality, since grants of rights under separate national patent laws represent separate and non-extraterritorial sovereign acts. But that debate has now been conclusively resolved and is not the principal concern of this article.

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