

June 20, 2008

Authored by Jason D. Haislmaier, Scott R. Bialecki, and Olympia Z. Fay

UNITED STATES SUPREME COURT ISSUES DECISION ON PATENT EXHAUSTION: NO DOUBLE DIPPING FOR UNCONDITIONAL LICENSES

On June 9, 2008, the U.S. Supreme Court issued a unanimous decision in the closely followed case of *Quanta Computer, Inc. v. LG Electronics, Inc.* (No. 06-937). The *Quanta* case has garnered much commentary within the patent law community and the decision of the Court is not likely to quell interest in the case. While the decision clarifies that the patent exhaustion doctrine applies to method claims in patents (in addition to other types of claims), it leaves open the possibility that a carefully crafted patent license could bar the doctrine's application in certain circumstances. In the wake of this possibility, both patent licensors and licensees alike should take steps to understand both the scope and limitations of this highly fact-driven decision.

For over a century, the patent exhaustion doctrine has been applied to limit the rights of a patent holder following the initial authorized sale of a patented product. The Court in *Quanta* addressed whether and to what extent the doctrine applies to the sale of components of a patented system when the components themselves do not infringe the claims of the method patent-at-issue until they are combined with additional items.

In *Quanta*, LG Electronics, Inc. ("LGE") had granted Intel Corporation ("Intel") the unqualified right in a license agreement to "make, use, sell (directly or indirectly), offer to sell, import or otherwise dispose of" Intel's own products (*i.e.*, microprocessors/chipsets) that practiced certain LGE method patents aimed at improving computer efficiency. Intel's products, on their own, did not infringe the patents-at-issue, but instead, needed to be combined with additional components (*e.g.*, buses, memory, etc.) to infringe LGE's patents. Although an additional master agreement between LGE and Intel clearly explained that no license had been given to any downstream purchaser that combined Intel's licensed products with non-Intel components to practice the inventions of LGE's method patents, the license to Intel at issue in the case did not contain such a restriction. *Quanta* ultimately purchased Intel's microprocessors, combined them with its own components in computer systems, and was sued for infringement of LGE's method patents.

Reversing an earlier decision by the Court of Appeals for the Federal Circuit, the Court clarified that method claims could be barred by the patent exhaustion doctrine. In doing so, the Court looked to whether Intel's products "substantially embodied" the LGE's licensed patents. As the Intel products did not have any non-infringing uses, the Court found that the doctrine applied and more broadly held that "[t]he authorized sale of an article that substantially embodies a patent exhausts the patent holder's rights and prevents the patent holder from invoking the patent law to control post-sale use of the article."

In a last ditch effort to escape the grasp of the patent exhaustion doctrine, which solely applies to "authorized sales," LGE argued that *Quanta's* downstream purchases had not been "authorized." The Court disagreed, noting that there was nothing in the license agreement that limited Intel's ability to practice any of the LGE patents. Further, the Court distinguished this case from its earlier precedent, notably the 1938 decision of the Court in

HRO CONTACTS

BOULDER

Jason D. Haislmaier
jason.haislmaier@hro.com

DENVER

Olympia Z. Fay
olympia.fay@hro.com
Scott R. Bialecki
scott.bialecki@hro.com
Mark L. Yaskanin
mark.yaskanin@hro.com
Paul Sung Cha
paul.cha@hro.com
Kathryn J. Coggon
kathryn.coggon@hro.com
Donald L. Samuels
donald.samuels@hro.com
Samantha Sturgis
samantha.sturgis@hro.com

COLORADO SPRINGS

Eric Bentley
eric.bentley@hro.com
Susan D. Campbell
susan.campbell@hro.com
Jill J. Chalmers
jill.chalmers@hro.com

PHOENIX

Glenn S. Bacal
glenn.bacal@hro.com
Christine Meis McAuliffe
christine.mcauliffe@hro.com

SALT LAKE CITY

William J. Athay
william.athay@hro.com
Thomas J. Rossa
thom.rossa@hro.com
David O. Seeley
david.seeley@hro.com
Craig A. Buschmann
craig.buschmann@hro.com
Lin C. Hsu
lin.hsu@hro.com

SAN FRANCISCO

Katherine Keating
katherine.keating@hro.com
Rachel Matteo-Boehm
rachel.matteo-boehm@hro.com

MUNICH

Ulrich Fuelbier
ulrich.fuelbier@hro.com
Jens Roehrborn
jens.roehrborn@hro.com



Holme Roberts & Owen LLP
Attorneys at Law

General Talking Pictures Corp. v. Western Electric Co., in which it held that patent exhaustion did not apply to a license that specifically narrowed the use and subsequent resale of the products in question. The Court did, however, note that even though the exhaustion doctrine applied in this particular matter, it did not have any opinion as to whether contract damages could be available to LGE.

Practical Implications

The decision in *Quanta* holds potential implications for all parties to patent license agreements in that the Court leaves open the possibility that the doctrine of patent exhaustion will not apply to patent licenses in all circumstances. With this possibility left open, patent licensors and licensees alike should consider the following issues when entering into patent license agreements in the future:

- As the patent exhaustion doctrine applies to both method and apparatus claims, patent holders should seek to be reasonably compensated for their method patents in their initial licenses versus attempting to seek additional funds from downstream, unlicensed purchasers.
- Parties to a patent license involving a method patent should clearly delineate in the license grant any restrictions on the use or resale of any article that is to be used as part of the licensed, patented method.
- Patent licensors should consider including terms in their license agreements requiring that failure to meet any explicit restrictions on any downstream use or sale voids the license grant.
- In order to avoid later confusion, the parties should state in any license agreement involving licensed components whether such products “substantially embody” the patented methods and/or have any non-infringing uses.

For more information about the issues discussed in this alert, contact any of the intellectual property attorneys at Holme Roberts & Owen LLP.

This article is a periodic publication of Holme Roberts & Owen LLP and should not be construed as legal advice or legal opinion on any specific facts or circumstances, nor is it intended to address specific disclosure or compliance issues that may arise in particular circumstances or provide an exhaustive discussion of the topics discussed herein. The contents are intended for general informational purposes only, and you are urged to consult counsel concerning your own situation and any specific legal questions you may have. For further information regarding the topics described herein, please contact any of the attorneys listed on the right side of page one.