

Patent Exhaustion and New Business Models: Sales, Servitudes, and Services

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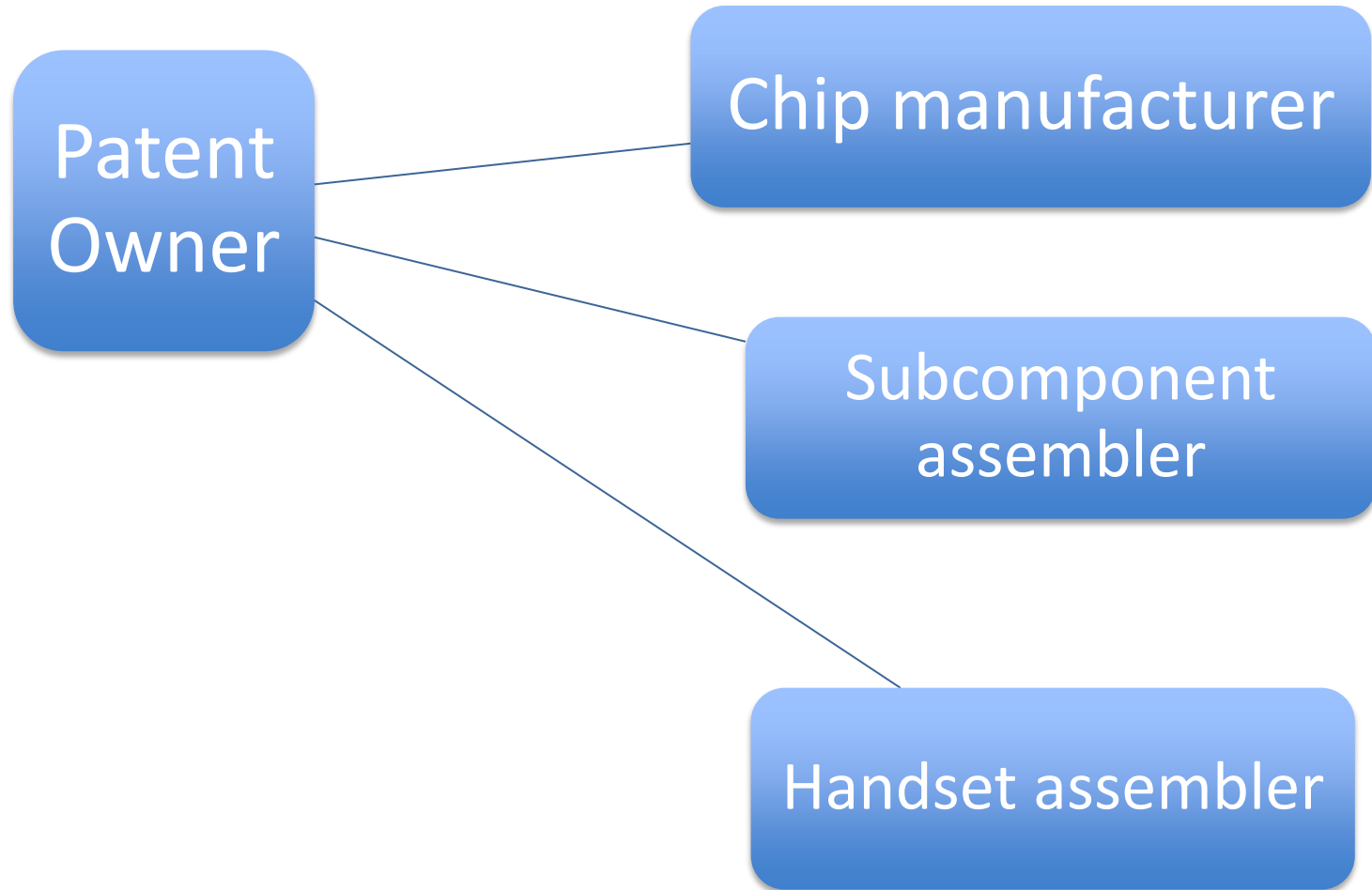
Three IP-based Product Distribution Models

- Sales
 - Unconditioned ([exhaustion](#))
 - Conditioned (*Mallinckrodt v. Medipart*, 976 F.2d 700 (Fed Cir 1992); [limited or no exhaustion?](#))
- “Lease-license”
 - Lease of physical object, no title transfer; “servitudes”; contractual terms of use including IP license (material transfer agreements; software EULAs w/CD-ROMs; [no exhaustion](#))
- Service
 - No possessory interest in user; physical objects simply part of service; service contract ([no exhaustion](#))
 - IP license as needed

Developments in Exhaustion

- *Quanta v. LG*, 553 U.S. 617 (2008)
 - Challenged forms of value chain licensing; largely ignored clear intent of parties
 - Method claims *can* be exhausted
 - Did *Mallinckrodt* survive?
 - LG should have granted limited make *and sell* license to Intel (but reasonable collateral issues prevented this)

Value Chain Licensing



Developments in Exhaustion

- *Bowman v. Monsanto*, S Ct 2013 slip op.
 - Patented GMO seeds are exhausted *qua* beans (but not as “replication machines” (seeds))
 - Good result *but* seems to conflict with *U.S. v. Univis*, 316 U.S. 241 (1942)(buyer has to be able to use lens blanks for expected purpose; implied license); Ct says Bowman can still eat or sell as beans—is this the primary expected use though?
 - But beans = seeds; no one would buy at Monsanto premium seed price to eat or transfer

Developments in Exhaustion

- *Bowman v. Monsanto*, S Ct 2013 slip op.
 - Confusion on 3+ generations of seeds/beans
 - 1st gen: bought from Monsanto; exhaustion *qua* beans
 - 2nd gen: grown by farmers from 1st gen; no exhaustion, can only sell/convey for human or animal consumption
 - 3rd+ gen: grown from 2nd gen (Bowman argued no exhaustion)

Developments in Exhaustion

- *Helferich Patent Licensing v. New York Times*, (ND Ill. 2013)
 - Adopts “double dipping” value chain royalties view; ignores reality of *proportional* royalties
 - Interprets *Quanta* and *Univis* to say that “whole patent” must be licensed; cannot license individual claims
 - Ct relied heavily on exhaustion re *combination* patents where patentability turns on combination, not components; but this doesn’t address separate claims issue
 - Real question is what handset firms were authorized to do under “make and sell” license terms

Developments in Exhaustion

- *Keurig v. Sturm Foods* (Fed Cir 2013)
 - Sale of patented cartridge-based coffee machines exhausted method claims for use of third party cartridges
 - Split panel adopts “whole patent” licensing interpretation to reject Keurig’s claim-by-claim approach; O’Malley, concurring, rejects whole patent interpretation
 - Court also rejects Keurig’s argument that coffee maker was capable of significant noninfringing uses; accepted Sturm’s argument that *Quanta/Univis* decisions were about unpatented objects

Developments in Exhaustion

- *Keurig v. Sturm Foods* (Fed Cir 2013)
 - Real issue is that Keurig engaged in unconditional sales of coffee makers and did not sue on its cartridge patents, but rather sued Sturm for inducing infringement by selling cartridges that machine owners would use to infringe method claims
 - Court used very similar language as ND Ill court in *Helperich* to assume that:
 - Keurig would collect “multiple royalties” if court did not find exhaustion
 - Absent strict exhaustion, no one would be able to know whether a patent was exhausted
 - These are highly debatable points

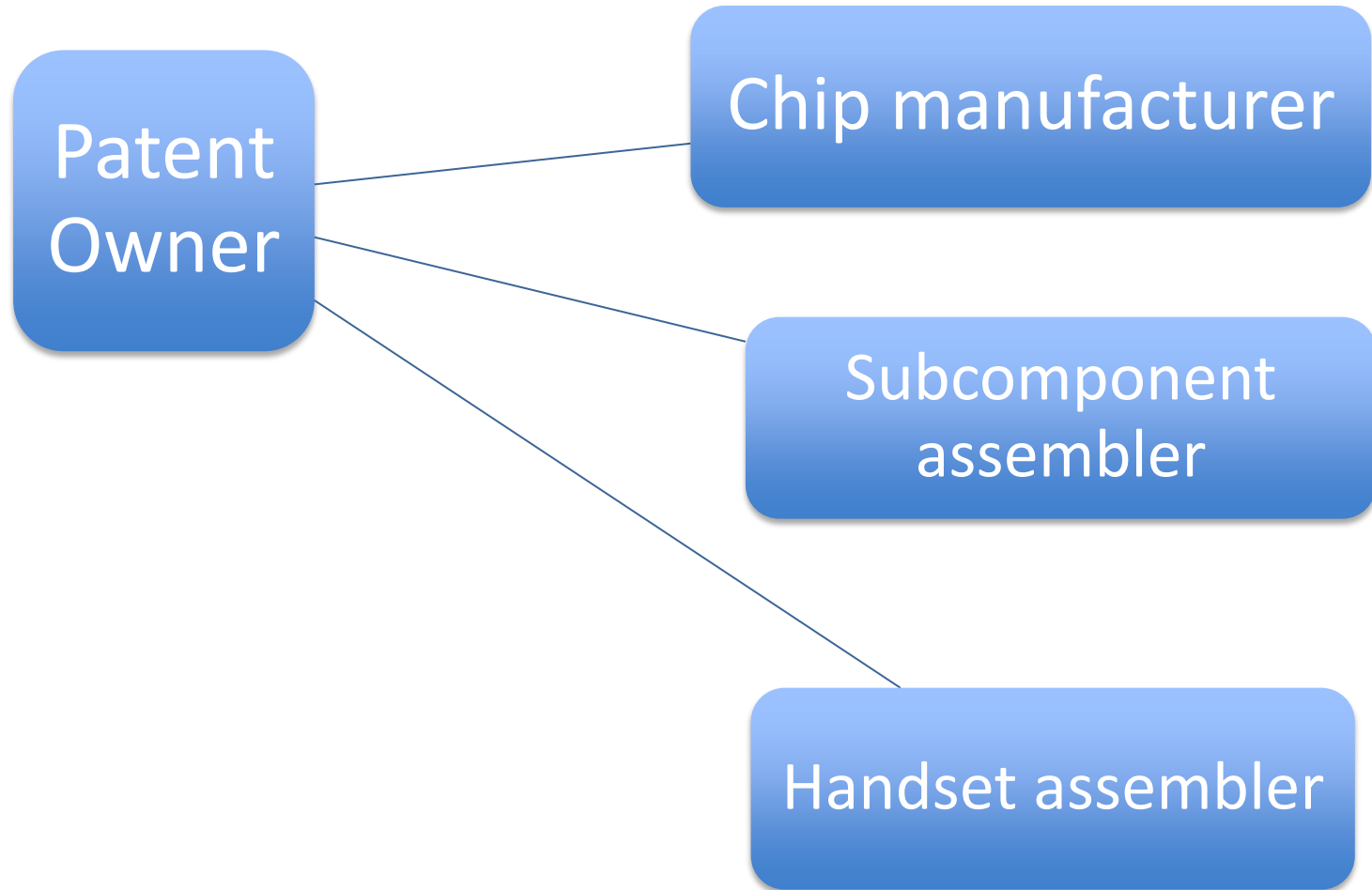
General Talking Pictures Provides Path to Value Chain Licensing

- *General Talking Pictures v. Western Electric Corp.*, 305 U.S. 124 (1939), concerned licenses that segmented the professional and amateur markets for amplifiers
- American Transformer Co. was licensed only to make *and sell* to amateur market
- Supreme Court held that Transformer's manufacture and sale to professional market rendered those amps effectively counterfeit as they were unauthorized

General Talking Pictures Provides Path to Value Chain Licensing

- Qualcomm has used the *General Talking Pictures* holding to enable its value chain licensing (amicus curie brief submitted in *Quanta*)
- Licenses granted to upstream firms to make and sell only to Qualcomm-licensed downstream parties
- Thus, sales by upstream licensee to anyone not bound by a Qualcomm license is effectively an unauthorized sale of counterfeit goods

Value Chain Licensing



General Talking Pictures Provides Path to Value Chain Licensing

- Patent owners can structure value chain licenses by careful limits on “sell” right
- Should have an account for why each license in chain generates only a portion of the “total” licensing value of the patent
- Otherwise courts may find that patentee is collecting “multiple royalties” on the same patent

Navigating a World of Exhaustion Uncertainty

- If “whole patent” licensing view prevails, then field of use licensing based on claim segmentation is jeopardized
- Uncertain as to when no other practical and reasonable use of sold item will be found, sufficient to mandate exhaustion
- Method claims particularly vulnerable to changing exhaustion rules

Navigating a World of Exhaustion Uncertainty

- Uncertainty of *Mallinkrodt* as good law means that exhaustion may apply even to “conditioned” sales
- Thus, patentees seeking to protect full value of patents—especially those with method claims—should consider distributing products under lease-license or service business models
- Lease-license generally upheld by courts (in the form of MTAs and EULAs); but lingering concerns that if it “looks like a sale” then it will be treated as one

Navigating a World of Exhaustion Uncertainty

- A move to products delivered as services?
- Eliminates exhaustion problems
- Anything can be delivered as service (cars, bikes, coffee makers, software, biological materials)
- Benefits consumers by making products available at lower costs and with sharply reduced risks to user; competitive service providers will keep products updated and serviced

Conclusion

- Evolving contours of exhaustion doctrine threaten existing conditional sale and licensing regimes
- Patentees can reduce their risk of limited monetization of their patents by moving to lease-license or service distribution model
- Service model may be wave of future as it presents benefits consumers like anyway and best minimizes risk to patentee from exhaustion