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Lost in Translation: How Practical Considerations in Kirtsaeng Demand International Exhaustion in Patent Law

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COMMENTS

LOST IN TRANSLATION: HOW PRACTICAL CONSIDERATIONS IN *KIRTSAENG* DEMAND INTERNATIONAL EXHAUSTION IN PATENT LAW

INTRODUCTION

The right of exclusivity powers the engines of innovation within the United States. Patent law is designed to reward the inventor with a monopoly over his or her creation. The scope of the monopoly a patent holder enjoys, however, has historically been limited in time and space to control its anticompetitive effect. The exhaustion doctrine is a key tool used by courts to police this effect and protect consumers.

Within patent law, the exhaustion doctrine permits the patent holder exclusive control over the first sale of a patented good.¹ However, after the patented good is released into the stream of commerce by authorized sale, the purchasers and their successors are free to use and resell the product without paying further royalties or requiring additional authorization from the patent holder.² This makes good sense, as the patent holder receives the full value of patented goods. The patent exhaustion doctrine rewards patent holders with the benefit of sale to preserve their incentive to innovate, while at the same time it prevents unnecessary double-dipping through continued control of the patented good in subsequent transactions.

1. Sarah R. Wasserman Rajec, *Free Trade in Patented Goods: International Exhaustion for Patents*, 29 BERKELEY TECH. L.J. 318, 327 (2014).

2. Joyce B. Klemmer, *Client Alerts: International Patent Exhaustion*, SMITH, GAMBRELL & RUSSELL, LLP (Oct. 5, 2010), http://www.sgrlaw.com/resources/client_alerts/1562/.

Application of the exhaustion doctrine is well-settled for patented goods first sold within the United States. Complexity arises in the matter of parallel imports—those goods that are authorized for sale abroad by the U.S. patent holder, but are then subsequently imported into the United States without the patent holder's authorization. Formalistic application of the exhaustion doctrine would permit patent holders to sell their goods outside of the United States, only to have purchasers import them into the United States and resell them in competition with the patent holder. The specter of these competing "gray goods" raises fairness concerns and potentially damages the incentives patent law strives to create.

In 2001, the Federal Circuit³ confronted the parallel imports problem in *Jazz Photo Corp. v. ITC* and imposed a geographical limitation on the patent exhaustion doctrine: U.S. patent holders exhaust their patent rights upon the first authorized sale of the patented good if the sale occurred in the United States.⁴ Otherwise, the patent holder retains exclusivity rights and can sue for infringement against those foreign resellers who attempt to import the patented good back into the United States.

Copyright law possesses a comparable exhaustion doctrine to patent law regarding the parallel import problem. The Supreme Court resolved this issue within the copyright context in *Kirtsaeng v. John Wiley & Sons, Inc.*, and did so differently than the Federal Circuit in *Jazz Photo Corp.*⁵ The Court adopted an "international exhaustion" theory: the doctrine of exhaustion will apply whenever the U.S. copyright owner sells or authorizes the first sale of a good, regardless of whether the good was manufactured or originally sold in the United States or abroad.⁶ Although

3. The Federal Circuit refers to the United States Court of Appeals for the Federal Circuit. Congress created the court in its passage of the Federal Courts Improvement Act of 1982, effectively merging the United States Court of Customs and Patent Appeals with the appellate division of the United States Court of Claims. Pub. L. No. 97-164, 96 Stat. 25 (1982). Federal courts have exclusive and original jurisdiction over patent cases, 28 U.S.C. § 1338 (2012), and the Federal Circuit is the only appellate-level court empowered to hear patent case appeals. 28 U.S.C. § 1295 (2012).

4. See 264 F.3d 1094, 1098–99 (Fed. Cir. 2001).

5. See *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S. Ct. 1351, 1355–56 (2013) (holding that "the 'first sale' doctrine applies to copies of a copyrighted work lawfully made abroad"); *Jazz Photo Corp.*, 264 F.3d at 1098, 1111 (affirming the Commission's orders determining that twenty-six respondents "had infringed all or most of the claims in suit of fourteen Fuji United States patents").

6. *Kirtsaeng*, 133 S. Ct. at 1355–56.

applied to different intellectual property rights and *Jazz Photo Corp.* decision. This comment was being written at the time of the issue in *Lexmark International, Inc. v. Static Control Systems, Inc.* is a prime candidate for Supreme Court review. Its disruptive potential within

This comment's purpose is to analyze the exhaustion doctrine announced in *Kirtsaeng v. John Wiley & Sons, Inc.* Part I begins by examining the exhaustion doctrine in light of international exhaustion jurisprudence. It also analyzes the effect of the recent Supreme Court decision on the exhaustion doctrine. Part II discusses the exhaustion doctrine policies and how they differ from the right as it does in patent law. Part III discusses an extension of the *Kirtsaeng* doctrine.

I. COMMON LAW ORIGIN OF THE EXHAUSTION DOCTRINE

Intellectual property rights are constitutionally mandated.⁷ The exhaustion doctrine is not, nor does it derive au-

7. No. 14-1617, 14-1619, 2016 U.S. LEXIS 1000 (U.S. Supreme Court, 2016). The Federal Circuit upheld the geographical exhaustion doctrine announced in 2001. The court's justification for its decision was based on an erroneous interpretation of *Boesch v. Silver*, 133 F.3d 1108 (9th Cir. 1998). *Photo Corp.*; (2) a strained reading of section 109(a) of the Copyright Act, which compares the exhaustion doctrine to the mutual common law origin of the doctrine. See *id.* at *59–98.

8. See U.S. CONST. art. 1, § 8, cl. 8 (Congress has the power "to secure for limited Times to Authors the exclusive Right to their respective Writings and Discoveries.")

9. See *id.*; 35 U.S.C. §§ 261–62, 264–65, 269–70 (1994) (adding an importation right following the Uruguay Round Agreements Act, Pub. L. No. 103-465, 110 Stat. 1761 (1996)). See also 33 I.L.M. 1125, 1200, 1208. Nor does Congress intend to alter the common law exhaustion doctrine. FROM THE PRESIDENT OF THE UNITED STATES: EXECUTIVE ORDER ON TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY AGREEMENTS, TEXTS OF AGREEMENTS, AND ADMINISTRATIVE ACTION AND REQUIREMENTS.

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applied to different intellectual property regimes, the *Kirtsaeng* and *Jazz Photo Corp.* decisions appear to conflict. While this comment was being written, the Federal Circuit considered this issue in *Lexmark International v. Impression Products*.⁷ The case is a prime candidate for Supreme Court consideration due to its disruptive potential within global markets.

This comment's purpose is to explore whether the principles announced in *Kirtsaeng* should apply to the patent exhaustion doctrine. Part I begins by examining the history of patent exhaustion jurisprudence. It also introduces the competing theories of international exhaustion and territorial exhaustion. Part II analyzes the effect of the recent Supreme Court decision in *Kirtsaeng* on the exhaustion doctrine in copyright. Part III contends that exhaustion doctrine polices the same practical problems in copyright as it does in patent law. Finally, the conclusion argues for an extension of the *Kirtsaeng* holding to the patent exhaustion doctrine.

I. COMMON LAW ORIGINS OF THE UNITED STATES PATENT EXHAUSTION DOCTRINE

Intellectual property rights in copyright and patent are constitutionally mandated.⁸ The patent exhaustion doctrine, however, is not, nor does it derive authority from statute.⁹ Rather, the doc-

7. No. 14-1617, 14-1619, 2016 U.S. App. LEXIS 2452 (Fed. Cir. Feb. 12, 2016). The Federal Circuit upheld the geographical limitation on patent exhaustion that it first recognized in 2001. The court's justification for such a ruling originates from: (1) the same erroneous interpretation of *Boesch v. Graff* that the Federal Circuit committed in *Jazz Photo Corp.*; (2) a strained reading of Supreme Court precedent; and (3) an inappropriate comparison of section 109(a) of the Copyright Act with the several Patent Acts that minimizes the mutual common law origins of patent exhaustion and copyright's first-sale doctrine. *See id.* at *59-98.

8. *See* U.S. CONST. art. 1, § 8, cl. 8 ("To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.").

9. *See id.*; 35 U.S.C. §§ 261-62, 271-73 (2012). Congress amended the Patent Act in 1994 to add an importation right following U.S. ratification of the TRIPS Agreement requiring member nations to include a right to import. 35 U.S.C. § 154 (2012). This Agreement expressly disclaims any effect on the exhaustion doctrine. *See* Uruguay Round Agreements Act, Pub. L. No. 103-465, §§ 532-533, 108 Stat. 4809, 4983-90 (1994); Agreement on Trade-Related Aspects of Intellectual Property Rights arts. 6, 28, Apr. 15, 1994, 33 I.L.M. 1125, 1200, 1208. Nor does the legislative history of this amendment show that Congress intended to alter the common law patent exhaustion doctrine. *See* MESSAGE FROM THE PRESIDENT OF THE UNITED STATES TRANSMITTING THE URUGUAY ROUND TRADE AGREEMENTS, TEXTS OF AGREEMENTS IMPLEMENTING BILL, STATEMENT OF ADMINISTRATIVE ACTION AND REQUIRED SUPPORTING STATEMENTS, H.R. DOC. NO. 103-316,

trine originates from English common law.¹⁰ The Supreme Court first articulated the doctrine with regard to patent law in *Adams v. Burke*.¹¹ The *Adams* Court clarified the limit of patent rights to patented goods.¹² Patent holders have a limited right to exclude others from the use, sale, and manufacture of their patented good. Protection is a negative right; it does not empower patent holders to assert their rights at will.¹³ As the value of patented goods is in their use, an authorized sale of the patented good terminates the patent holder's exclusive right to control how the purchaser uses the patented good thereafter.¹⁴

At its heart, the exhaustion doctrine serves two goals. First, it marks the boundary of the patent holder's monopoly. The doctrine emphasizes the "single-reward" principle used to incentivize inventors to create.¹⁵ Inventors are entitled to a single reward as compensation, and no more.¹⁶ An authorized sale serves as a single reward,¹⁷ after which patent rights exhaust.¹⁸ The single reward principle is not about helping the inventor maximize his or her reward; it only guarantees enough to incentivize the inventor to continue innovating.¹⁹ The compensatory scheme must be un-

at 1-2 (1994), reprinted in 1994 U.S.C.C.A.N. 4040.

10. See 1 SIR EDWARD COKE, INSTITUTES OF THE LAWS OF ENGLAND § 360 (19th ed. 1832); see also *Kirtsaeng*, 133 S. Ct. at 1363.

11. 84 U.S. (17 Wall.) 453, 456 (1873). Earlier decisions laid the groundwork for the exhaustion doctrine in patent. See *Mitchell v. Hawley*, 83 U.S. (16 Wall.) 544 (1872); *Bloomer v. Millinger*, 68 U.S. (1 Wall.) 340 (1863); *Bloomer v. McQuewan*, 55 U.S. (14 How.) 539 (1852).

12. *Adams*, 84 U.S. at 456 ("When the patentee or the person having his rights, sells a machine or instrument whose sole value is in its use, he receives the consideration for its use and he parts with the right to restrict that use. The article . . . passes without the limit of the monopoly. That is to say, the patentee or his assignee having in the act of sale received all the royalty or consideration which he claims for the use of his invention in that particular machine or instrument, it is open to the use of the purchaser without further restriction on account of the monopoly of the patentee.").

13. See 35 U.S.C. § 271(a) (2012) (granting patent holders exclusive rights to the make, use, sale, and importation of the invention); see also Jay A. Erstling & Frederik W. Struve, *A Framework for Patent Exhaustion from Foreign Sales*, 25 FORDHAM INTELL. PROP., MEDIA & ENT. L.J. 499, 506-07 (2015).

14. See *Quanta Comput., Inc. v. LG Elecs., Inc.*, 553 U.S. 617, 625 (2008) (quoting *Adams*, 84 U.S. at 455) ("[W]here a person ha[s] purchased a patented machine of the patentee or his assignee, . . . this purchase carri[es] with it the right to the use of that machine so long as it [is] capable of use.").

15. See Erstling & Struve, *supra* note 13, at 519-23.

16. See *id.* at 519; see also *United States v. Univis Lens Co.*, 316 U.S. 241, 250 (1942).

17. See *Quanta Comput., Inc.*, 553 U.S. at 625 ("[T]he initial authorized sale of a patented item terminates all patent rights to that item.").

18. Erstling & Struve, *supra* note 13, at 520-21.

19. See Margreth Barrett, *The United States' Doctrine of Exhaustion: Parallel Imports*

derstood within the overall context of the Arts and Sciences for the

Second, the exhaustion doctrine imposes constraints on the alienation of the patent. It reaches back to Lord Coke's view that post-sale restrictions are not enforceable because they undermine bargaining and contracting. The doctrine, in their use, and patent law is justified for the public benefit, then allows for the spirit of the law.

A. *International Exhaustion*

The common law exhaustion doctrine asks whether authorized sales are enforceable whether authorized sales are applied universally or only in the United States. It hardly promotes a geographic approach to exhaustion. Early cases dealt with parallel importation;²³ the Supreme Court has since imports for patented goods. The Supreme Court and federal courts supports a

The Supreme Court first articulated the constraints in patents in *Adams v. Burke*. The manufacturer of improved coffins assigned all patent rights to a firm in Boston. The firm subsequently assigned the rights to another firm. The manufacturer's suit for patent infringement was dismissed. The court held that the use of the patented goods by the assignee was not an infringement because the assignee was using the patented goods with the

of *Patented Goods*, 27 N. KY. L. REV. 100 (1939).

20. See *id.* at 922.

21. See *Lifescan Scot., Ltd. v. Amgen*, 563 U.S. 203 (2013) (quoting *Straus v. Victor T. Smith*, 100 U.S. 103 (1879) (patent holder's attempt] to place restrictions on the use of the patented [was] such as have been hateful to the public interest.").

22. See COKE, *supra* note 10, at 346.

23. See, e.g., *Quanta Comput., Inc. v. LG Elecs., Inc.*, 553 U.S. 617 (2008) (doctrine of patent exhaustion to U.S. market).

24. 84 U.S. (17 Wall.) 453 (1873).

25. *Id.* at 453-54.

26. *Id.*

27. *Id.*

¹⁰ The Supreme Court to patent law in *Adams* permit of patent rights to limited right to exclude nature of their patented is not empower patent the value of patented the patented good term to control how the

¹⁴ has two goals. First, it is monopoly. The doctrine used to incentivize to a single reward as sale serves as a single reward.¹⁸ The single reward inventor maximize his or incentivize the inventor scheme must be un-

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laid the groundwork for the U.S. (16 Wall.) 544 (1872); *McQuewan*, 55 U.S. (14

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Exhaustion: Parallel Imports

derstood within the overarching goal of patent law: promoting the Arts and Sciences for the public benefit.²⁰

Second, the exhaustion doctrine reflects an abhorrence for restraints on the alienation of personal property.²¹ This sentiment reaches back to Lord Coke's writings in the 17th century, arguing that post-sale restrictions are "against Trade and Traffi[c], and bargaining and contracting."²² If the value of patented goods is in their use, and patent law seeks to disseminate inventions for the public benefit, then allowing post-sale restrictions undermines the spirit of the law.

A. *International Exhaustion and a Century of Precedent*

The common law exhaustion doctrine left as an open question whether authorized sales by the intellectual property owner applied universally or only domestically. Supreme Court precedent hardly promotes a geographical limitation within patent exhaustion. Early cases dealt primarily with domestic instances of exhaustion;²³ the Supreme Court has yet to directly address parallel imports for patented goods. The scant case law on this issue from federal courts supports a theory of international exhaustion.

The Supreme Court first indicated its aversion to territorial restraints in patents in *Adams v. Burke*.²⁴ In *Adams*, a Boston manufacturer of improvements for coffin lids, Merrill & Horner, assigned all patent rights in its invention within a ten-mile radius of Boston to a firm, Lockhart & Seelye.²⁵ Lockhart & Seelye subsequently assigned those rights to Adams.²⁶ Adams brought a suit for patent infringement against Burke, an undertaker allegedly using coffins with the patented lids in his business.²⁷ Burke

of Patented Goods, 27 N. KY. L. REV. 911, 912, 922 (2000).

20. *See id.* at 922.

21. *See Lifescan Scot., Ltd. v. Shasta Techs., LLC*, 734 F.3d 1361, 1376 (Fed. Cir. 2013) (quoting *Straus v. Victor Talking Mach. Co.*, 243 U.S. 490, 500-01 (1917)) ("[A patent holder's attempt] to place restraints upon [a patented product's] further alienation [was] such as have been hateful to the law from Lord Coke's day to ours.").

22. *See COKE*, *supra* note 10, at 223.

23. *See, e.g., Quanta Comput., Inc. v. LG Elec., Inc.*, 553 U.S. 617 (2008) (applying the doctrine of patent exhaustion to United States computer technology patents).

24. 84 U.S. (17 Wall.) 453 (1873).

25. *Id.* at 453-54.

26. *Id.*

27. *Id.*

lived seventeen miles from Boston and purchased the lids from the original patent holder within the ten-mile limit before those rights transferred to Adams.²⁸ Theoretically, authorized sale of the coffin lid improvements to Burke constituted a transfer of rights to the purchaser that attached within the ten-mile restriction; exhaustion of the patent holder's rights would not occur beyond that radius. Yet, the *Adams* Court ignored the territorial restriction and declared Adams's rights to the patented good exhausted simply by virtue of an authorized sale.²⁹ The *Adams* decision left indicia about the Supreme Court's broader inclinations towards geographical restraints on alienation.

Two decades later, the Supreme Court clarified its holding in *Adams*. In *Keeler v. Standard Folding Bed Co.*, the Court explained that "a person who buys patented articles from a person who has a right to sell, though within a restricted territory, has a right to use and sell such articles in all and any part of the United States."³⁰ The Court elaborated that someone who purchases patented goods from the patent holder in an authorized sale "becomes possessed of an absolute property in such articles, *unrestricted in time or place*."³¹ Again, patent right exhaustion turned on the presence of an authorized sale rather than where the sale occurred. The *Keeler* Court concluded that "payment of a royalty once, or, what is the same thing, the purchase of the article from one authorized by the [patent holder] to sell it, emancipates such article from any further subjection to the patent throughout the entire life of the patent."³² The Supreme Court maintained this view over the next century and recently reiterated its interpretation of the doctrine in 2008.³³

For the next century, federal courts consistently applied international exhaustion principles to patent cases coming before them.³⁴ Pointedly, the Second Circuit in *Curtiss Aeroplane & Mo-*

28. *Id.*

29. *Id.* at 456-57.

30. *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659, 664 (1895).

31. *Id.* at 666 (emphasis added).

32. *Id.*

33. *See Quanta Comput. Inc. v. LG Elecs., Inc.*, 553 U.S. 617, 625 (2007).

34. *See, e.g., Dickerson v. Tinsling*, 84 F. 192, 195 (8th Cir. 1897) (assuming, without deciding, "that one who buys a patented article without restriction in a foreign country from the owner of the United States patent has the right to use and vend it in this country"); *Dickerson v. Matheson*, 57 F. 524, 527 (2d Cir. 1893) ("A purchaser in a foreign country, of an article patented in that country and also in the United States, from the owner of

tor Corp. v. United A application of intern ports.³⁵ In *Curtiss*, a an patents for airplan Curtiss Aeroplane lic the planes were built ponents.³⁷ After the v to the defendant, wh resale.³⁸ Curtiss Aero patent infringement.³⁹

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35. 266 F. 71 (2d Cir. 192

36. *Id.* at 72.

37. *Id.* at 73.

38. *Id.* at 74.

39. *Id.* at 72.

40. *Id.* at 79-80.

41. *Id.* at 78.

42. *Id.* at 77-78 ("If the v tents, the sale frees the artic tents, and where there is no complete title and full right t Holiday v. Mattheson, 24 F. 1

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United States, from the owner of

tor Corp. v. United Aircraft Engineering Corp. elaborated on the
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ports.³⁵ In *Curtiss*, a U.S. company owned both U.S. and Canadi-
an patents for airplane-related inventions.³⁶ During World War I,
Curtiss Aeroplane licensed airplanes to the British government;
the planes were built in Canada and incorporated patented com-
ponents.³⁷ After the war, the British government sold the planes
to the defendant, who imported them into the United States for
resale.³⁸ Curtiss Aeroplane responded by suing the defendant for
patent infringement.³⁹

The Second Circuit held for the defendant because it claimed
Curtiss Aeroplane exhausted its patent rights when it originally
sold the airplanes abroad to the British government.⁴⁰ In its ra-
tionale, the Second Circuit explained that "[i]f a patentee or his
assignee sells a patented article, that article is freed from the
monopoly of any patents which the vendor may possess . . . and if
the vendor has divided his monopoly into different territorial mo-
nopolies, his sale frees the article from them all."⁴¹ The *Curtiss*
court emphasized that location of sale is immaterial to the ex-
haustion doctrine, even where the possibility exists that subse-
quent foreign purchasers may attempt to import the patented
good into the United States and resell.⁴²

More recently, the Southern District of New York applied in-
ternational exhaustion principles in the 1988 decision *Kabushiki*

each patent, or from a licensee under each patent, who purchases without any restrictions
upon the extent of his use or power of sale, acquires an unrestricted ownership in the arti-
cle, and can use or sell it in this country."); *Holiday v. Mattheson*, 24 F. 185, 185-86
(C.C.S.D.N.Y. 1885) (finding patent rights exhausted for a United States patent owner
who sold a patented good in England without restrictions or conditions on sale); *Sanofi,
S.A. v. Med-Tech Veterinarian Prods., Inc.*, 565 F. Supp. 931, 938 (D.N.J. 1983) ("The
court will . . . not grant to Sanofi an injunction against distribution in this country of the
product that it sold in France without restriction.").

35. 266 F. 71 (2d Cir. 1920).

36. *Id.* at 72.

37. *Id.* at 73.

38. *Id.* at 74.

39. *Id.* at 72.

40. *Id.* at 79-80.

41. *Id.* at 78.

42. *Id.* at 77-78 ("If the vendor's patent monopoly consists of foreign and domestic pa-
tents, the sale frees the article from the monopoly of both his foreign and his domestic pa-
tents, and where there is no restriction in the contract of sale the purchaser acquired the
complete title and full right to use and sell the article in any and every country."); see also
Holiday v. Mattheson, 24 F. 185 (C.C.S.D.N.Y. 1885).

*Kaisha Hattori Seiko v. Refac Technology Development Corp.*⁴³ Hattori entered into a contractual agreement with Refac Technology for the rights to the sale and distribution of digital timepieces.⁴⁴ Refac Technology possessed the patent rights to these timepieces, but in a grant provision of its agreement with Hattori, it stated in relevant part that Hattori, having "fully paid up," had a non-exclusive license for the entire term of the patent to the making, using, and selling of Refac Technology's patented timepiece products.⁴⁵ Hattori made sales abroad to customers who, directly or indirectly, resold the timepieces into the United States as "gray goods" or incorporated them into products that were sold in the United States.⁴⁶ Refac Technology sued Hattori for patent infringement.⁴⁷ The district court considered whether the license to Hattori permitted a right to sell the timepieces outside of the United States.⁴⁸ It ultimately affirmed that patent rights exhaust where an unconditional authorized sale occurs, whether domestic or abroad.⁴⁹

Throughout the 20th century, federal courts consistently applied international exhaustion doctrine in parallel import cases. In the eyes of these courts, authorized sales sufficiently compensated the patent holder for the purposes of patent law. Allowing additional royalties placed an undue restraint on the alienation of personal property and bred uncertainty in the market.

B. Territorial Exhaustion and Jazz Photo Corp.

The jurisprudence for international exhaustion was built on inferences drawn from *Adams* and its progeny. Advocates of territorial exhaustion argue against international exhaustion as an extraterritorial application of U.S. patent law.⁵⁰ Patent holders, especially those segmenting their markets geographically, also

43. 690 F. Supp. 1339, 1342 (S.D.N.Y. 1988).

44. *Id.* at 1341.

45. *Id.* at 1340-41.

46. *Id.* at 1341.

47. *Id.* at 1342.

48. *Id.* at 1342-43.

49. *See id.* at 1342-44. The court dismissed an implicit territorial restriction to the exhaustion doctrine. *Id.* This stands in contrast to the patent holder's ability to control his exclusive rights through contract. *Id.*

50. Rajec, *supra* note 1, at 326-27. Extraterritoriality incites vigorous debate in exhaustion doctrine. While an important consideration for evaluating the reach of patent rights, the topic exceeds the scope of this comment.

fear the real threat porters of territorial supporting application in *Jazz Photo* tion.⁵²

In *Jazz Photo Corp* use" cameras called domestic and foreign patents on various co Photo Corporation (imported the discarded Fuji Film sued for pa

Among other arg claimed Fuji Film e when it authorized sa circuit, relying on *Boes*. The court explicitly s first sale doctrine, th under the United Sta protections of patent sold outside of the U its position when the patentee's authorizat the United States] d

51. John A. Rothchild, *E* (2011).

52. The second case, *Bo* sales never exhaust United F.3d 1094, 1105 (Fed. Cir. 20 not support that proposition. not foreign law, determines v preme Court reinforced this 157 U.S. 659, 664-65 (1894).
See Barrett, *supra* note 19, a Supp. 1283, 1285 (E.D. Penn.

53. *Jazz Photo Corp.*, 264

54. *Id.* at 1107.

55. *Id.* at 1101.

56. *Id.* at 1098.

57. *Id.*

58. *Id.* at 1105.

59. *Id.*

60. *See id.*

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incites vigorous debate in ex-
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fear the real threat of gray goods in parallel importation.⁵¹ Sup-
porters of territorial exhaustion theory generally cite three cases
supporting application of the doctrine; the Federal Circuit’s deci-
sion in *Jazz Photo Corp. v. ITC* shows its most recent applica-
tion.⁵²

In *Jazz Photo Corp.*, the respondent, Fuji Film, sold its “single-
use” cameras called “lens-fitted film packages” (“LFFP”) to both
domestic and foreign customers.⁵³ Fuji Film held multiple active
patents on various components within the LFFP.⁵⁴ Appellant Jazz
Photo Corporation (“Jazz Photo”) purchased, refurbished, and
imported the discarded LFFPs into the United States for resale.⁵⁵
Fuji Film sued for patent infringement.⁵⁶

Among other arguments made in its defense, Jazz Photo
claimed Fuji Film exhausted its patent rights over the LFFP
when it authorized sales of its cameras abroad.⁵⁷ The Federal Cir-
cuit, relying on *Boesch v. Graff*, rejected Jazz Photo’s position.⁵⁸
The court explicitly stated that “[t]o invoke the protection of the
first sale doctrine, the authorized first sale must have occurred
under the United States patent.”⁵⁹ The court refused to extend the
protections of patent exhaustion to imported LFFPs originally
sold outside of the United States.⁶⁰ The Federal Circuit reiterated
its position when the case returned to the court on appeal: “[A]
patentee’s authorization of an international first sale [outside of
the United States] does not affect exhaustion of that patentee’s

51. John A. Rothchild, *Exhausting Territoriality*, 51 SANTA CLARA L. REV. 1187, 1188 (2011).

52. The second case, *Boesch v. Graff*, is often cited for the proposition that foreign sales never exhaust United States patent rights. See, e.g., *Jazz Photo Corp. v. ITC*, 264 F.3d 1094, 1105 (Fed. Cir. 2001) (citing *Boesch v. Graff*, 133 U.S. 697, 703 (1890)). It does not support that proposition. Rather, the *Boesch* Court held that United States patent law, not foreign law, determines whether a sale is authorized. *Boesch*, 133 U.S. at 703. The Supreme Court reinforced this interpretation in *Keeler*. *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659, 664–65 (1894). The third case, *Griffin v. Keystone Mushroom Farm*, also argues for territorial exhaustion, but has been highly discredited for ignoring case precedent. See Barrett, *supra* note 19, at 943–47 (citing *Griffin v. Keystone Mushroom Farm*, 453 F. Supp. 1283, 1285 (E.D. Penn. 1978)).

53. *Jazz Photo Corp.*, 264 F.3d at 1105.

54. *Id.* at 1107.

55. *Id.* at 1101.

56. *Id.* at 1098.

57. *Id.*

58. *Id.* at 1105.

59. *Id.*

60. See *id.*

rights in the United States. . . . [F]oreign sales can never occur under a United States patent because the United States patent system does not provide for extraterritorial effect."⁶¹ Several subsequent district court decisions have followed the *Jazz Photo Corp.* rule without critical comment on the doctrine.⁶²

Commentators, however, lambasted the Federal Circuit's decisions as injurious to free trade and anomalous within patent exhaustion jurisprudence.⁶³ *Jazz Photo Corp.* muddied the waters for the exhaustion doctrine, offering a competing interpretation of Supreme Court precedent.⁶⁴

Resolving the tension between the two theories on the patent exhaustion doctrine requires reference to exhaustion in copyright, which shares the same common law roots. The Supreme Court has previously recognized "the historic kinship between patent law and copyright law" and how concepts of one may analogize to the other under the appropriate circumstances.⁶⁵ The Federal Circuit also endorses this view.⁶⁶

61. *Fuji Photo Film Co., Ltd. v. Jazz Photo Corp.*, 394 F.3d 1368, 1376 (Fed. Cir. 2005).

62. *See, e.g.,* *Laserdynamics, Inc. v. Quanta Storage Am., Inc.*, No. 2:06-CV-348-TJW-CE, 2009 U.S. District LEXIS 115848 at *1 (E.D. Tex. June 29, 2009), *rev'd on other grounds*, 694 F.3d 51 (Fed. Cir. 2012); *Minebea Co., Ltd. v. Papst*, 444 F. Supp. 2d 68, 140-41 (D.D.C. 2006).

63. *See, e.g.,* *Rothchild*, *supra* note 51, at 1205-06, 1211. The United States patent holder in *Boesch* derived no benefit from the unauthorized sale in Germany. *Id.* at 1200-01. Nor did the licensee of the patent holder make the sale. *Id.* at 1206 (quoting *Sanofi, S.A. v. Med-Tech Veterinarian Prods., Inc.*, 565 F. Supp. 931, 937 (D.N.J. 1983)). The vendor had the right to sell under German patent laws, which provided that patents do not affect persons who, at the time of the patent application, were already making use of the invention. Ultimately, the patent holder did not receive compensation for use of his invention, nor did he consent to its importation into this country. *Id.* at 1206 (quoting *Sanofi* 565 F. Supp. at 938). Exhausting his patent rights without an authorized sale would undermine the balancing of interests United States patent law seeks to achieve by disseminating the inventor's work to the public without incentivizing its creation.

64. *Compare Jazz Photo Corp.*, 264 F.3d at 1105, *with Keeler v. Standard Folding Bed Co.*, 157 U.S. 659, 661, 666 (1894).

65. *See Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 439 (1984) (borrowing vicarious liability in patent law to inform vicarious liability in copyright law).

66. *See Helderich Patent Licensing, LLC v. N.Y. Times Co.*, 778 F.3d 1293, 1305-06 (Fed. Cir. 2015); *Lifescan Scot., Ltd. v. Shasta Techs., LLC*, 734 F.3d 1361, 1375 n.9 (Fed. Cir. 2013).

II. A GUIDING LIC

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67. *See Bobbs-Merrill Co.*

68. Copyright Act of 1909 version at 17 U.S.C. § 109 (20

69. Section 109(a) read phonorecord lawfully made u entitled, without the authori possession of that copy or ph tains no geographical limita *Bobbs-Merrill*.

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71. *Compare, e.g.,* *Sebas* 1093, 1099 (3rd Cir. 1988) (U.S.A., Inc. v. Toys "R" Us, I fied geographical interpretati

72. 133 S. Ct. 1351 (2013)

73. Brief for Petitioner a (2013) (No. 11-697).

74. *Id.* at 7-8.

75. *Id.*

76. *Id.* at 8.

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II. A GUIDING LIGHT FROM COPYRIGHT: *KIRRTSAENG V. JOHN WILEY & SONS, INC.*

The comparable exhaustion doctrine in copyright, known as the first-sale doctrine, emerged in U.S. common law more than thirty years after its appearance in patent.⁶⁷ Congress subsequently codified the doctrine within the Copyright Act of 1909.⁶⁸ The first-sale doctrine survives as 17 U.S.C. § 109.⁶⁹ The statutory text animating the doctrine remains relatively consistent with the version first announced by the Court in 1908.⁷⁰ Through the next century, however, federal circuit courts split over whether it should apply to copyrighted articles sold abroad and imported into the United States.⁷¹ The Supreme Court definitively answered the question of whether the first-sale doctrine should contain any geographical limitation two years ago in *Kirtsaeng v. John Wiley & Sons, Inc.*⁷²

Kirtsaeng was a Thai national who immigrated to the United States for study and attended a Ph.D. program at the University of Southern California.⁷³ To subsidize the cost of his education, Kirtsaeng asked friends and family in Thailand to purchase textbooks in Thailand and ship the books to the United States.⁷⁴ After using them for class, Kirtsaeng sold the textbooks on eBay for a profit.⁷⁵ Among the stock Kirtsaeng sold were eight textbooks printed in Asia by John Wiley & Sons, Inc. (“Wiley”).⁷⁶ Wiley sued

F.3d 1368, 1376 (Fed. Cir.

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 34 F.3d 1361, 1375 n.9 (Fed.

67. See *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350-51 (1908).

68. Copyright Act of 1909, § 41, 35 Stat. 1084 (repealed and superseded 1978) (current version at 17 U.S.C. § 109 (2012)).

69. Section 109(a) reads, in relevant part: “the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.” 17 U.S.C. § 109(a) (2012). This codification contains no geographical limitation and is relatively unchanged since first announced in *Bobbs-Merrill*.

70. Compare *Bobbs-Merrill*, 210 U.S. at 350-51, with 17 U.S.C. § 109(a) (2012).

71. Compare, e.g., *Sebastian Int’l, Inc. v. Consumer Contracts (PTY) Ltd.*, 847 F.2d 1093, 1099 (3rd Cir. 1988) (favoring a nongeographical interpretation), with *Denbicare U.S.A., Inc. v. Toys “R” Us, Inc.*, 84 F.3d 1143, 1149-50 (9th Cir. 1996) (favoring a modified geographical interpretation).

72. 133 S. Ct. 1351 (2013).

73. Brief for Petitioner at 7, *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S. Ct. 1351 (2013) (No. 11-697).

74. *Id.* at 7-8.

75. *Id.*

76. *Id.* at 8.

Kirtsaeng for copyright infringement, but Kirtsaeng asserted that Wiley exhausted its copyright under section 109(a) of the Copyright Act.⁷⁷ The Court of Appeals for the Second Circuit ruled against Kirtsaeng, stating that the first-sale doctrine applies only to domestic sales.⁷⁸ The Supreme Court reversed on appeal, holding that the first-sale doctrine was geographically unbound.⁷⁹

The *Kirtsaeng* Court traced the origins of exhaustion doctrine to Lord Coke's writings.⁸⁰ These roots are shared by copyright and patent law.⁸¹ The Court interpreted Lord Coke's statement to prohibit the holder of an intellectual property right from controlling what happens to the good after the initial and complete sale.⁸² To prohibit the holder after receiving full consideration for the sale of the good undermines free trade and fundamental contract principles.⁸³ In the same breath, the Court frontally addressed the parallel imports problem, acknowledging "the importance of leaving buyers of goods free to compete with each other when reselling or otherwise disposing of those goods."⁸⁴

The Court also surveyed case precedent and section 109(a) of the Copyright Act for evidence of a geographical limitation to the first-sale doctrine.⁸⁵ It found none.⁸⁶ Rather, the Court observed that "no language, context, purpose, or history . . . would rebut a 'straightforward application' of that doctrine here."⁸⁷ The same can be said of the exhaustion doctrine in patent law, as no Su-

77. *Kirtsaeng*, 133 S. Ct. at 1357.

78. *Id.*

79. *Id.* at 1371.

80. *Id.* at 1363. Specifically, the Court noted that he wrote:

[If] a man be possessed of . . . a horse, or of any other chattell . . . and give or sell his whole interest . . . therein upon condition that the Donee or Vendee shall not alien[ate] the same, the [condition] is voi[d], because his whole interest . . . is out of him, so as he hath no possibilit[y] of a Reverter, and it is against Trade and Traffi[c], and bargaining and contracting betwee[n] man and man: and it is within the reason of our Author that it should ouster him of all power given to him.

Id. (citing COKE, *supra* note 10, at 223).

81. See *Lifescan Scot. Ltd. v. Shasta Techs., LLC*, 734 F.3d 1361, 1376 (Fed. Cir. 2013) (stating that the first sale doctrine is "comparable" to the patent exhaustion doctrine and shares roots in common law).

82. *Kirtsaeng*, 133 S. Ct. at 1363.

83. See *id.* at 1376-77.

84. *Id.*

85. *Id.* at 1363.

86. *Id.*

87. *Id.* at 1364.

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III. TERRITORIAL EXH

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preme Court precedent has deviated from this straightforward application either.⁸⁸

Kirtsaeng's reliance on common law to justify a nongeographic interpretation of the first-sale doctrine encourages similar adoption within patent law. Important to that adoption, however, is understanding whether the problems the *Kirtsaeng* Court addressed in copyright are comparable in the world of patented goods. Extension makes sense only where these parallels may be drawn.

III. TERRITORIAL EXHAUSTION UNNECESSARILY RESTRAINS FREE TRADE

Pivotal to the *Kirtsaeng* Court's nongeographic interpretation of the first-sale doctrine were the practical problems that territorial exhaustion creates in copyright.⁸⁹ The Court cited the "ever-growing importance of foreign trade to America" as fundamental to its consideration and ultimate rejection of a geographic limitation.⁹⁰ The "practical problems" in copyright apply with even greater force in patent law and suggest that the *Kirtsaeng* holding ought to extend to the patent exhaustion doctrine.

A. Patent Holders Do Not Need a Geographical Limitation

One of the more common arguments made in support of territorial exhaustion is that patent law should enable patent holders to segment the market by price without fear of parallel importation. The theory suggests that part of the monopoly incentive inherent in a patent is the ability to maximize the return.⁹¹ Foreign countries may implement price controls or not offer patent protection for a type of invention.⁹² Territorial exhaustion compensates for that reality by allowing the patent holder to retain his or her U.S.

88. *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659, 664 (1895); *Boesch v. Graff*, 133 U.S. 697, 703 (1890); *Adams v. Burke*, 84 U.S. (17 Wall.) 453, 456-57 (1873).

89. *Kirtsaeng*, 133 S. Ct. at 1367 ("[W]e believe that the practical problems that petitioner and his amici have described are too serious, too extensive, and too likely to come about for us to dismiss them as insignificant.").

90. *Id.*

91. *International First Sales and Imports Under U.S. and European IP Laws*, BLOOMBERG BNA (Mar. 3, 2016, 10:37 AM), <http://www.bna.com/international-first-sales-and-imports-under-u-s-and-european-ip-laws/>.

92. *Athersys, Inc.*, Annual Report (Form 10-K) (Mar. 3, 2008).

patent rights for sales abroad.⁹³ Also, by allowing the patent holder to retain the right to sue for parallel imports, the patent holder can regulate the price of patented goods in domestic sales and mute the disruptive impact of the gray market.⁹⁴ This rationale suffers from two major flaws: (1) it enables unnecessary incentivization and (2) it ignores the initial control patent holders have over their monopoly.⁹⁵ The impact of gray market goods can be mitigated without reliance on patent law.⁹⁶

1. Geographical Limitations Overincentivize Patent Holders

When the patent holder authorizes an unrestricted sale of a patented good, the transaction follows the principles of contract law.⁹⁷ He offers the good to the purchaser for a set price, who assents. The patent holder has bargained for the value of the good at a price the two can mutually agree upon. After the sale of the good, he receives just compensation. Framed in terms of personal property, this vests title in the patented good with the purchaser.⁹⁸ The purchaser, as *Adams* suggests, has the right to use the good however he chooses.⁹⁹ The patent holder's efforts have been rewarded only once. Whatever happens to the patented good afterward would entail a post-sale restriction, and courts are reluctant to inhibit alienation of personal property after the patent holder has received his due.¹⁰⁰

If the patent holder were to retain his patent rights for sales abroad, that would enable him to extract additional value from subsequent purchasers who import into the United States. This certainly benefits the patent holder, but the law does not require that "just compensation" be the maximum utility the patent hold-

93. See Barrett, *supra* note 19, at 965.

94. See *id.* at 970.

95. See *infra* Part III.A.1.

96. See *infra* pp. 1420–21.

97. See *Keurig, Inc. v. Sturm Foods, Inc.*, 732 F.3d 1370, 1373 (Fed. Cir. 2013) ("[A]n unconditional sale of a patented device exhausts the patentee's right to control the purchaser's use of that item thereafter because the patentee has bargained for and received full value for the goods.")

98. See *Filmtec Corp. v. Allied Sign, Inc.*, 939 F.2d 1568, 1572 (Fed. Cir. 1991) (discussing how patent rights may be analogized to personal property rights).

99. See *Adams v. Burke*, 84 U.S. (17 Wall.) 453, 456–57 (1873).

100. See *Lifescan Scot., Ltd. v. Shasta Techs., LLC*, 734 F.3d 1361, 1376 (2013) (quoting *Straus v. Victor Talking Mach. Co.*, 243 U.S. 490, 500–01 (1917)).

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101. See Barrett, *supra* note 19, at 965.

102. See *id.* at 922.

103. See Rajec, *supra* note 101, at 100.

104. See *id.*

105. See *id.*

106. See, e.g., *Erstling & Co. v. American Optical Co.*, 12 N.C. J.L. & T. 100 (1917) (enabling patent holders to maintain their rights through private resolution, 12 N.C. J.L. & T. 100 (1917)).

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er can extract from the good.¹⁰¹ It must only be sufficient to re-
 ward the patent holder for his initial investment.¹⁰²

If anything, enforcement of patent rights through territorial
 exhaustion, rather than through international exhaustion backed
 by private contracts, shifts enforcement costs from the parties to
 the government.¹⁰³ The government must invest more in patrol-
 ling imported goods (e.g., hiring customs officials) to police a pa-
 tent holder’s importation right under such a model.¹⁰⁴ Territorial
 exhaustion burdens the government further by charging the U.S.
 court system with enforcement of private disputes.¹⁰⁵

The government may cover these anticipated costs by raising
 the duty on imported goods, with the necessary implication that
 such increases will pass to the consumer. A territorial exhaustion
 scheme may benefit the patent holder, but only by distributing
 the costs to the government and consumers. These significant
 costs suggest that geography-based price discrimination is incon-
 gruous with the goal of balancing patent monopoly rights with so-
 cial benefit.

In contrast, an international exhaustion regime would not shift
 costs but rather would rely on private enforcement of contract
 disputes. Here, the burden would be on the contracting parties to
 negotiate the boundaries of their rights to the patented goods and
 to assert those rights when infringed. The patent holder has more
 control if he or she licenses the patented good because the patent
 holder retains patent rights to the goods (in limited circumstanc-
 es) and may elect, through mutual agreement with other parties,
 to resolve infringement cases through neutral arbitration rather
 than the court system.¹⁰⁶ Arbitration may also result in speedier
 resolution than use of the court system, which benefits the par-
 ties involved.

101. See Barrett, *supra* note 19, at 912, 922.

102. See *id.* at 922.

103. See Rajec, *supra* note 1, at 365.

104. See *id.*

105. See *id.*

106. See, e.g., Erstling & Struve, *supra* note 13, at 529–30 (suggesting that licensing
 enables patent holders to maintain their importation right). See generally Anne Louise St.
 Martin & J. Derek Mason, *Arbitration: A Quick and Effective Means for Patent Dispute
 Resolution*, 12 N.C. J.L. & TECH. 301 (2011) (discussing the merits of using arbitration as
 an alternate dispute resolution regime in patent law).

Proponents of territorial exhaustion also raise the specter that the inability to price discriminate will result in a "one price for the world" model because gray market resale will force uniform pricing in order for the patent holder to compete.¹⁰⁷ Part of the justification for price discrimination is the ability for patent holders to maintain high prices in developed markets while increasing consumer access to patented goods in developing markets by offering the same product at a lower price.¹⁰⁸ Price discrimination enables greater social welfare in this manner. Multiple commentators, however, have identified that the social welfare justification is not borne out in reality because wealth disparities in countries cause companies to target high-income markets rather than selling their goods at lower prices.¹⁰⁹ Patent holders have alternate means to price discriminate beyond use of geography.¹¹⁰

2. Patent Holders Control How to Collect Their Reward

Patent holders' insistence on using patent law to price discriminate is subject to attack on three fronts. First, Congress remains silent on whether patent holders have a right to constrain the alienation of personal property. Second, patent holders already control how they collect their reward and can form private contracts to manage their rights.¹¹¹ And third, patent holders can address concerns with uniform pricing and parallel imports under an international exhaustion regime by offering more versions of patented goods.

The *Kirtsaeng* Court emphasized that the right to price discriminate must be grounded in either the Constitution or congressional intent.¹¹² The Court recognized that "the Constitution's language nowhere suggests that [an intellectual property holder's] limited exclusive right should include a right to divide markets or a concomitant right to charge different purchasers differ-

107. See, e.g., Darren E. Donnelly, Comment, *Parallel Trade and International Harmonization of the Exhaustion of Rights Doctrine*, 13 SANTA CLARA COMPUTER & HIGH TECH. L.J. 445, 501-04 (1997).

108. See Rajec, *supra* note 1, at 361-62.

109. See *id.* at 366.

110. *Id.* at 367.

111. See *United States v. Gen. Elec. Co.*, 272 U.S. 476, 485 (1926) (explaining that "under the patent law the patentee is given by statute a monopoly of making, using and selling the patented article").

112. See *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S. Ct. 1351, 1370-71 (2013).

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113. *Id.* at 1371.

114. *Id.*

115. *Id.*

116. See *supra* note 9 a

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118. See *supra* note 9 a
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119. Cf. *Kirtsaeng*, 133
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raise the specter that in a "one price for all" world, the law will force uniformity of competition.¹⁰⁷ Part of the difficulty for patent holders is that while increasing competition by opening markets by offering price discrimination is commendable, multiple commercial welfare justifications for disparities in countries rather than patent holders have altered the focus of geography.¹¹⁰

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law to price discrimination, Congress remains constrained to constrain the actions of patent holders already constrained by private contracts. Patent holders can address imports under an importation version of pa-

right to price discrimination or constitutionalism or contract. "the Constitution's" equal property holder's right to divide markets among purchasers differ-

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ent prices . . . to increase or to maximize gain. Neither, to our knowledge, did any Founder make any such suggestion."¹¹³ Nor did the Court find any "precedent suggesting a legal preference for interpretations of copyright statutes that would provide for market divisions."¹¹⁴ Instead, the Court cited in support of its contention a statement from the Copyright Office claiming that division of territorial markets was "primarily a matter of private contract."¹¹⁵

Copyright law contains section 109, which discusses the first-sale doctrine, but patent law has no corollary.¹¹⁶ *Kirtsaeng* infers that geographical limitations are impermissible in the absence of congressional intent to provide the rights holder with "more than ordinary commercial power to divide international markets."¹¹⁷ Nothing in the several Patent Acts demonstrates congressional intent to allow price discrimination using the exhaustion doctrine.¹¹⁸

At the same time, the *Kirtsaeng* Court left open an avenue for relief in contract.¹¹⁹ Businesses may strategize how to bring the patented goods to market. They control supply. They set the price, cognizant of what the costs are to produce the good and the price points that the market will tolerate. With this amount of unilateral authority, the patent holder controls to which markets it brings patented goods and the terms on which they might be purchased.¹²⁰ Essentially, businesses know what occurs when selling patented goods and can reduce parallel importation problems by limiting their sales to markets where stable price points may be maintained. This may reduce the social welfare of the patented good in the first instance, but to do otherwise exposes the patent holder to greater risk of gray market competition.

113. *Id.* at 1371.

114. *Id.*

115. *Id.*

116. *See supra* note 9 and accompanying text.

117. *See Kirtsaeng*, 133 S. Ct. at 1371.

118. *See supra* note 9 and accompanying text; *cf.* *United States v. Univis Lens Co.*, 316 U.S. 241, 252 (1942) (asserting that price-fixing licensing schemes for resold patented goods do not enjoy patent law protection under the fair meaning of the several Patent Acts).

119. *Cf. Kirtsaeng*, 133 S. Ct. at 1371 (demonstrating that the Court did not specify whether parties could segment markets by geography through something less than a full assignment of copyright).

120. *See generally* Rajec, *supra* note 1 (providing a broader discussion on the ways businesses price discriminate without reliance on patent law).

This rationale applies as much to the sole proprietor as it does to the corporation. When a business or inventor chooses to make an authorized sale, part of control deals with expectations. Sophisticated patent holders are aware of the doctrine of patent exhaustion; the introduction of a geographical limitation uses intellectual property rights as a means of allowing them to game the system and extract a competitive advantage by mere sale abroad. For the simple patent holder, the problem of parallel imports should come as no surprise. It would be unreasonable for the patent holder to think that he could exert downstream control of a patented good if he made a sale within the United States and subsequent purchasers resold the item in direct competition.

An international exhaustion model may promote better price discrimination than geography. Without territorial exhaustion, patent holders may introduce more versions of their patented goods, customized to meet differing income levels and needs.¹²¹ This approach permits patent holders to maximize their profits by segmenting based on more granular demand curves rather than a macroscopic model. This will enable patent holders to capture a greater share of the market, thereby improving their return. Such an approach may also result in greater consumer access because price points on certain versions of the patented goods may be tailored to meet lower-income markets.

Versioning of the patented good also combats parallel import problems. By pushing patent holders to customize their goods with greater attention to customer needs, they insulate themselves from the gray market threat. The version of a patented good sold for less in a developing market will differ in the features it offers compared to the version sold in a high-income market. Competitive pressure from resellers within the high-income market lessens when the imported good lacks the custom features provided by the domestic version of the good. Incidentally, versioning encourages innovation by pushing the patent holder to adapt the patented goods to a wider set of consumer demands. In sum, if the patent holder wants to prevent uniform pricing and maximize returns on the patented good, the patent holder should adapt the patented good to meet the market he wishes to dominate. Versioning also improves social welfare by granting broader consumer access to a patented good.

121. Rajec, *supra* note 1, at 321, 367.

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If businesses want to impose restrictions on sale, they should do so up front by contract rather than at the end. Licenses are fairly commonplace in the world of patented goods.¹²² An international exhaustion scheme may push more United States patent holders towards this model, where they may exert greater control over the patented goods. Fear of parallel imports may be overblown, and price discrimination can be achieved by more than geographic segmentation of markets. Versioning may provide patent holders an alternative means to price discriminate, thereby maximizing their returns, increasing consumer access to the patented good, and suppressing the negative influence of gray market resale. Patent law, however, is an inappropriate legal tool to enforce price discrimination, especially when Congress has not spoken on the issue.

B. *Geographical Limitations Introduce Too Much Uncertainty*

A geographical limitation to the exhaustion doctrine also breeds uncertainty for multiple market players. The Court poignantly used the *amici* in *Kirtsaeng* to detail a parade of horrors within the copyright context that recommend international exhaustion.¹²³ These same concerns—market inefficiency, consumer liability, and determining the location of sale—also bedevil the world of patent goods. Each may be circumvented by relying on private contract law rather than a national exhaustion scheme.

1. Market Inefficiency for Manufacturers

The *Kirtsaeng* Court observed the growing global character of the consumer goods within the United States.¹²⁴ Many of these goods—computers, smartphones, and automobiles—also incorporate hundreds or thousands of patented components within their design.¹²⁵ Component manufacturers may hold patents within

122. See WORLD INTELL. PROP. ORG. EXCHANGING VALUE: NEGOTIATING TECHNOLOGY LICENSING AGREEMENTS 14–16 (2005), http://www.wipo.int/export/sites/www/sme/en/documents/pdf/technology_licensing.pdf (providing multiple reasons why companies and inventors select licenses over sales).

123. See *Kirtsaeng*, 133 S. Ct. at 1364–67.

124. *Id.* at 1365 (stating that the Retail Litigation Center reported over \$2.3 trillion worth of foreign good imports in 2011).

125. Bronwyn H. Hall & Rosemarie Ham Ziedonis, *The Patent Paradox Revisited: An Empirical Study of Patenting in the U.S. Semiconductor Industry, 1979–1995*, 32 RAND J. ECON. 101, 110 (2001) (“[A] given semiconductor product . . . will often embody hundreds if not thousands of ‘potentially patentable’ technologies.”).

numerous countries, including the United States.¹²⁶ The number of implicated patents will only increase as patented goods become more complex.

Obvious problems arise for manufacturers of finished goods if the United States imposes a geographical limitation on the patent exhaustion doctrine. Take the manufacture of a laptop as an example.¹²⁷ To import a laptop into the United States, the laptop manufacturer will have to track the patent rights of each component. Major parts of the laptop may include the motherboard, coolant systems, liquid crystal display, graphic card, physical case, and so on.¹²⁸ Several of these major parts, such as the motherboard, consist of hundreds of individual components (e.g., semiconductors), and there may be several links in the supply chain between the laptop manufacturer and the components manufacturer.¹²⁹ If each component of the laptop was not involved in a United States domestic sale along the supply chain, the laptop manufacturer must negotiate with the component manufacturer for license to use the component in the laptop when imported into the United States.

This royalty is *in addition to* the initial reward the components manufacturer received when it first sold the component. Due to the complexity of the laptop design, a geographical limitation creates a hold-out situation during license negotiations. The threat of litigation is a powerful bargaining chip for components manufacturers to extract more value for their inventions than their

126. *Protecting Intellectual Property Rights (IPR) Overseas*, U.S. PATENT AND TRADEMARK OFFICE, <http://www.uspto.gov/patents-getting-started/international-protection/protecting-intellectual-property-rights-ipr> (last visited Apr. 15, 2016).

127. The proceeding analysis applies with equal force to similarly situated goods, for example, smartphones, tablets, automobiles, aircraft, etc. Notably, this argument does not consider the special circumstances incident on the pharmaceutical industry. See generally Jeffrey Atik & Hans Hendrik Lidgard, *Embracing Price Discrimination: TRIPS and the Suppression of Parallel Trade in Pharmaceuticals*, 27 U. PA. J. INT'L ECON. L. 1043 (2006) (providing further analysis of the impact of geographical limitations within that industry).

128. See *Your Laptop's Important Parts Unveiled*, TECHADVISORY.ORG (Feb. 20, 2014), <http://www.techadvisory.org/2014/02/your-laptops-important-parts-unveiled/>; Repair Man, *All Main Laptop and Notebook Parts Explained*, LAPTOP PARTS 101 (May 2, 2009), <http://www.laptopparts101.com/category/laptop-parts/>; *Hardware*, EXPLAININGCOMPUTERS.COM, <http://explainingcomputers.com/hardware.html> (last visited Apr. 15, 2016).

129. See Brief for LG Electronics, Inc., Dell Inc., Google Inc. et al. as Amici Curiae Supporting of Appellant at 6, *Lexmark Int'l, Inc. v. Impression Prods., Inc.*, No. 14-1617, 1619 (Fed. Cir. 2015) [hereinafter Google Inc. et al. as Amici Curiae].

actual market will control the exhaustion doctrine.

The efforts to limit exhaustion under a territoriality approach invest substantial resources in patent holders of components with the threat of infringement litigation. The decision presents a dilemma.

In the first scenario, the court creates market power for the manufacturer and takes to determine the appropriate royalty to secure the appropriate return on investment. The manufacturer brings the product to market at a point to cover the costs of the components manufacturer. In sum, the manufacturer's profit margins are reduced and the consumer gets a second chance to purchase the product.

The result is a market where the manufacturer must bear the costs of litigation and the threat of reputational damage, shakedown payments, and other costs alike. Similarly, the manufacturer's sales are reduced in the United States market and the consumer gets a second chance to purchase the patented good.

The Kirtsaeng companies faced a similar dilemma with software and packages.¹³²

130. Cf. *Kirtsaeng v. John Wiley & Sons, Inc.*, 135 S. Ct. 1116 (2013) (authors may have bargained for a limited right to sell a copyright).

131. In more elastic markets, the manufacturer's profits are reduced through to the consumer. While consumer prices are reduced, the manufacturer's profits are reduced directly. This also frees up resources for other improvements. The act of exhaustion creates economic incentives of the manufacturer.

132. *Kirtsaeng*, 135 S. Ct. 1116 (2013).

tes.¹²⁶ The number of patented goods become

of finished goods if attention on the patent of a laptop as an example. In the United States, the laptop manufacturer of each component of the motherboard, the chip card, physical components such as the motherboard, and the supply chain components manufacturer not involved in a supply chain, the laptop manufacturer when imported into

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Similarly situated goods, for this argument does not hold industry. See generally *International-protection: TRIPS and the WTO* (2006) (2016).

WORLD TRADE ORGANIZATION (Feb. 20, 2014), *International-protection: TRIPS and the WTO* (May 2, 2009), <http://www.wto.org> (2016).

et al. as Amici Curiae, *International-protection*, No. 14-1617, 2016 WL 1353 (2016).

actual market worth.¹³⁰ In a sense, this is the type of downstream control the exhaustion doctrine is meant to prevent.

The efforts a business must go through to comply with the law under a territorial exhaustion model leave two major options: (1) invest substantial resources locating potential United States patent holders of each component and negotiating licensing agreements with them or (2) neglect due diligence and accept infringement litigation as an acceptable business risk. Either decision presents a no-win situation for free trade.

In the first scenario, the presence of a geographical limitation creates market inefficiency. The time the laptop manufacturer takes to determine the patent rights of each component and secure the appropriate licenses extends the time required to bring the product to market. The additional resources the laptop manufacturer must expend will also inflate the laptop's price point to cover the extra expense incurred from paying licenses to components manufacturers. This cost is passed on to the consumer. In sum, the consumer pays more, the laptop manufacturer's profit margins remain the same, and the components manufacturer gets a second bite of the royalty apple.¹³¹

The result is no different in the second scenario. The laptop manufacturer may increase the laptop prices in anticipation of the costs of litigation. Litigation may harm the manufacturer's reputation, shaking the confidence of investors and consumers alike. Similarly, adverse results in litigation will disrupt the manufacturer's supply chain, forcing it to seek substitutes in the United States market. This will also slow the time to market of the patented good.

The *Kirtsaeng* Court understood the challenges that technology companies faced in the context of copyrighted software programs and packages.¹³² The same goods the Court mentioned also incor-

130. Cf. *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S. Ct. 1351, 1364 (2013) (implying authors may have bargaining power to negotiate higher fees than when they originally sold a copyright).

131. In more elastic markets, the laptop manufacturer may be unable to pass expenses through to the consumer. In this scenario, the manufacturer's profit margins decrease while consumer prices level. The components manufacturer dips into the laptop manufacturer's profits directly. The less profitable the venture, the more suspect its viability becomes. This also frees up less capital for the laptop manufacturer to invest in innovative improvements. The act of collecting a second royalty through license undermines the economic incentives of the downstream market player to innovate.

132. *Kirtsaeng*, 133 S. Ct. at 1365 ("Technology companies tell us that 'automobiles,

porate patented components.¹³³ The Court recognized the reality that many of these goods were manufactured abroad with the United States "copyright holder's permission and then sold and imported . . . to the United States."¹³⁴ A geographical limitation on the exhaustion doctrine would create "intolerable consequences," including the "absurd result that the copyright owner can exercise downstream control even when it authorized the import or first sale."¹³⁵ The Court also recognized the bargaining power of an intellectual property right holder.¹³⁶

International exhaustion, backed by contract law, short-circuits these concerns. Downstream market players need not expend additional resources in a license-vetting program.¹³⁷ Nor could they be held captive by the coercive threat of litigation by the patent holders. Patent holders will receive a single reward for their patented good congruent with the need to incentivize the patent holder to innovate and no more. Patent holders may instead use contract law to limit the uses of patented goods and mitigate the problem of parallel importations that directly compete with their goods. Restricted sales, under a licensing model, do not necessarily exhaust patent rights.

Contract law may solve the manufacturer's concerns because manufacturers may bargain with components manufacturers for the patent rights to use their components in certain geographic markets. But, while the manufacturers may counteract uncertainties through contract law for the initial sales, the true problem arises with regard to notice in the context of the second-sale market and the consumer's liability.

2. Consumer Liability

A geographical limitation on the exhaustion doctrine exposes consumers to potential liability when the patent holder retains

microwaves, calculators, mobile phones, tablets, and personal computers' contain copyrightable software programs or packaging . . . made abroad with the American copyright holder's permission and then sold and imported (with that permission) to the United States.") (internal citations omitted).

133. See Google Inc. et al. as Amici Curiae, *supra* note 129, at 14.

134. *Kirtsaeng*, 133 S. Ct. at 1365.

135. *Id.* at 1366.

136. *Id.* at 1364 ("And, even where addresses can be found, the costs of finding them, contacting owners, and negotiating may be high indeed.")

137. See *id.* at 1366.

the exclusive right authorized for sale through regular

Consider an example: a company holds rights in components; the company sells components in the United States; a consumer purchases the laptop; the Chinese consumer sells her laptop to a reseller.

Under a territorial exhaustion theory, the reseller is not infringing on the patent holder's rights in three separate sales: the initial sale to the Chinese consumer, the resale to the Chinese consumer, and the resale to the reseller. She is not infringing on the patent holder's rights in the laptop within the United States because of sale by reselling.

This system is problematic because it lacks notice that, when she disposes of her laptop, she is liable. The action is not for commercial uses (e.g., for transportation). The action is that resale infringes on the patent holder's rights that she could not have known that she could infringe. In that sense, her action is a reasonable expectation.

The notice problem is exacerbated when the patent holder sells components and the consumer is faced with the finished good. The scope of the patent holder's rights is that she is a single person who controls the records of the source

138. See 35 U.S.C. § 2703.

139. See *id.*

140. See *id.*

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the exclusive right to make, use, and sell patented goods already authorized for sale abroad. A consumer may unwittingly infringe through regular use and resale of his or her purchases.

Consider an extension of the last hypothetical. A United States company holds multiple patents on various internal laptop components; the company authorizes a Chinese company to use its components in the manufacture of its laptop. A Chinese consumer purchases the laptop from the Chinese laptop manufacturer. The Chinese consumer later immigrates to the United States and sells her laptop to a refurbishing firm for petty cash.

Under a territorial exhaustion regime, the Chinese consumer infringed on the United States component maker's patent rights in three separate ways *despite* the maker's authorization of first-sale to the Chinese laptop manufacturer. The moment the Chinese consumer entered the United States with the laptop, she infringed on the United States component maker's right to import.¹³⁸ She infringed the right of use by mere possession of the laptop within the United States.¹³⁹ Finally, she infringed the right of sale by reselling the laptop to the refurbishing firm.¹⁴⁰

This system is fundamentally unfair to the consumer. She lacks notice that, because of *where* she purchased the laptop, how she disposes of her personal property affects her infringement liability. The actions that could trigger liability involve both commercial uses (e.g., resale) and personal uses (e.g., transnational transportation). Where a consumer may strain to understand that resale infringes patent rights, she would hardly anticipate that she could infringe from typical everyday use of that good. In that sense, her actual personal property rights are divorced from reasonable expectations.

The notice problem is complicated further because the infringing components are not open to inspection. Even if they were, the consumer is faced with the same dilemma as the manufacturer of the finished good except she is hopelessly less equipped to handle it. The scope of possible infringing components is the same, but she is a single person. Unlike the manufacturer, she has no records of the source of each component beyond possible part labels.

138. See 35 U.S.C. § 271(a) (2012).

139. See *id.*

140. See *id.*

To discern this information requires her to compromise the physical integrity of the patented good, perhaps robbing it of its value in the process. This exercise is hardly feasible with other goods (e.g., vehicles). Presumably, the only way to determine her potential liability is to contact the finished product manufacturer and request the information.

This problem is much more magnified than the one in *Kirtsaeng*. Each textbook Kirtsaeng purchased contained a single copyright, registered to the publisher.¹⁴¹ He was exposed to a single infringement suit.¹⁴² He was unaware that his resale of the textbook infringed on Wiley's copyrights, nor would he expect his actions to do so.¹⁴³ Conversely, the consumer of patented goods risks a separate infringement suit for each manufacturer along the good's supply chain, including internal components. The liability against the patent infringer is exponentially more than that against the copyright infringer.

Contract law may provide an out for the consumer under a territorial exhaustion model. Companies may mitigate liability risks to the consumer by including indemnification provisions in contracts with components manufacturers that pass on to the consumer. The company must still bargain for such coverage, which translates to costs for the patented goods. The company, however, is trading consumer uncertainty for its own and then must bear the risk of the consumer's subsequent activities that may violate the component manufacturer's patent rights.

International exhaustion removes the need to bargain and the net uncertainty to both the consumer and the manufacturer. Under this model, the threat of litigation does not loom large for consumers purchasing goods from foreign companies, nor the foreign company that indemnifies the consumer. Nor must the foreign customer concern herself with how she disposes of her property if she travels to the United States. Consumer confidence is restored, and the consumer's personal property rights will match the reasonable expectations that she may use her property the way she

141. See *Kirtsaeng*, 133 S. Ct. at 1356.

142. *Id.* at 1357.

143. Kirtsaeng researched the first-sale doctrine prior to purchasing the textbooks and reselling them later. See Brief for Petitioner at 8, *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S. Ct. 1351 (2013) (No. 11-697). He found sources explaining the first-sale doctrine under international exhaustion principles and, as such, did not realize the circuit court split prior to taking action. *Id.*

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3. Location of Sale

The refurbishing of a second-hand layer of used goods in a business dealing is difficult to discern. These goods are moved along the supply chain from the manufacturer, making the liability of the manufacturer more tenuo

In the hypothetical, the separate sources of used goods are the consumer originating from purchasing the laptop and the consumer facing the consumer who purchased the laptop infringing parts contain serial numbers down the original components. But the finished goods

This situation is observed in museums, libraries, and bookstores. As observed that these entities have exhausted their exhaustion doctrine [their] practices."¹⁴⁴ For example, used libraries charge a fee to contribute for each book to the library holder, just as in patent law. For used books, the publisher, there is a wrinkle. Geographical exhaustion of used books by refurbishers to try t

144. See *Kirtsaeng*, 133 S. Ct. at 1366.

145. *Id.* at 1366.

146. *Id.* at 1364.

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wishes. Limiting the consumer's liability encourages the consumer to purchase abroad, promoting free trade. It also strengthens the buyer-seller relationship.

3. Location of Sale for the Used Good Reseller

The refurbishing firm in the hypothetical encounters an additional layer of uncertainty under territorial exhaustion. For a business dealing in used goods, the location of sale will be harder to discern. These resellers stand in a place many times more removed along the supply chain than the finished good manufacturer, making the justification for downstream control by patent holders more tenuous.

In the hypothetical, the refurbishing firm is subject to two separate sources of uncertainty. First, the firm is unaware of where the consumer originally purchased the laptop. Second, by purchasing the laptop, the refurbishing firm inherits the uncertainty facing the consumer in determining whether any components of the laptop infringe a U.S. patent right. Presumably, the laptop parts contain serial numbers allowing the refurbisher to track down the original manufacturers and the patent rights of the components. But then the firm runs into the same problems as the finished goods manufacturer.

This situation parallels the *Kirtsaeng* Court's concerns with museums, libraries, and used book sellers.¹⁴⁴ The *Kirtsaeng* Court observed that these organizations rely on the protections of the exhaustion doctrine; its application was "deeply embedded in [their] practices."¹⁴⁵ A geographical limitation would require, for example, used libraries to obtain individual permissions to distribute for each book in its collection.¹⁴⁶ Finding the copyright holder, just as in patent, can be a laborious task of breathtaking scope. For used booksellers, an analogous business class to the refurbisher, there lies the same challenge, with one important wrinkle. Geographical limitations force used booksellers and refurbishers to try to predict what the intellectual property right

144. See *Kirtsaeng*, 133 S. Ct. at 1364–65.

145. *Id.* at 1366.

146. *Id.* at 1364.

holder "may think about a [consumer's] effort to sell a used [good]."¹⁴⁷ This is an impractical expectation levied on the reseller.

International exhaustion allays these concerns as well. When the exhaustion of patent rights turns on the authorization of sale rather than its location, the reseller need only contact a single source, the original manufacturer, to determine whether sale was authorized. The component issue subsides, for it is unlikely that finished goods manufacturers secure a steady stream of components from the black market. Ultimately, the used good reseller conducts its business unimpeded, and consumers benefit from the availability and lower prices of the used goods.

CONCLUSION

Overall, a territorial approach to patent exhaustion undermines the careful balance patent law attempts to strike between incentivizing the patent holder to disclose and promoting disclosure of inventions for the public benefit. Territorial exhaustion favors the rights of the patent holder when the Constitution commands the opposite. Traditional justifications for territorial exhaustion—enabling businesses to price discriminate and preventing grey-market competition—are overshadowed by the threat such a doctrine poses to free trade and market stability. The *Kirtsaeng* Court highlighted the consequences of territorial exhaustion in the context of the first-sale doctrine in copyright. These practical consequences are as relevant in patent law as they are in copyright. Accordingly, the Federal Circuit's anomalous decision in *Jazz Photo Corp.* cannot be reconciled with the Supreme Court's pronouncements in *Kirtsaeng*.

Absent territorial exhaustion, patent holders may still protect their patent rights and maximize their returns. Private enforcement of patent rights through licensing and contract benefits consumers and enables patent holders to enforce their rights with greater control and faster results. Patent holders may also still price discriminate by exploring alternate methods to segment their markets based on product design. Overall, patent holders can achieve their desired business outcomes without relying on territorial exhaustion. After all, the exhaustion doctrine is meant

147. See *id.* at 1365.

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An international approach to patent exhaustion better serves the policy goals of patent law. Without a geographical limitation, patent law will operate within the common sense expectations of buyers and sellers alike. Patent rights will exhaust according to a uniform and predictable "single-reward" principle that incentivizes inventors only so far as to encourage them to continue innovating. The Intellectual Property Clause of the Constitution empowers Congress to award inventors a limited monopoly "[t]o promote the Progress of Science and useful Arts."¹⁴⁸ The plain language prioritizes the benefits of public disclosure over the rights of the patent holder, and an international exhaustion approach keeps the focus precisely where the Founders intended it to be.

*Dustin M. Knight **

148. U.S. CONST. art. 1, § 8, cl. 8.

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