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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.

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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 Circuit[3] 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 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-

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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-

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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 carrie[s] 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 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

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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. Tinling, 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 Aircraft Engineering Corp. elaborated on the application of international exhaustion theory to parallel imports.[35] In *Curtiss*, a U.S. company owned both U.S. and Canadian 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 components.[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 rationale, 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 monopolies, his sale frees the article from them all."[41] The *Curtiss* court emphasized that location of sale is immaterial to the exhaustion doctrine, even where the possibility exists that subsequent 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 international 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 article, 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 patents, the sale frees the article from the monopoly of both his foreign and his domestic patents, 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 of gray goods in parallel importation.[51] Supporters of territorial exhaustion theory generally cite three cases supporting application of the doctrine; the Federal Circuit's decision in *Jazz Photo Corp. v. ITC* shows its most recent application.[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 Circuit, 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* Helferich 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 LIGHT FROM COPYRIGHT: *KIRTSAENG 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

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.*, Sebastion 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-

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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.

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)).

er can extract from the good.[101] It must only be sufficient to reward 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 patrolling imported goods (e.g., hiring customs officials) to police a patent 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 incongruous with the goal of balancing patent monopoly rights with social 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 circumstances) 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 parties involved.

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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).

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 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.

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 horribles 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 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 the 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 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.

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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

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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.*

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.

to protect consumers rather than permit patent holders to exercise downstream control.

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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