

QUANTA VS. LGE: A DECISION CONCERNING LICENSING

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Generally, when a patent owner sells a patented product to a first buyer, the purchaser is free to use or sell that patented product without having to worry about being sued for infringement by the patent holder. This is referred to as the doctrine of “patent exhaustion”.

In a case opposing the Korean company, LG Electronics (“LGE”), and the Taiwanese company Quanta Computers (“Quanta”), the Supreme Court of the United States recently ruled on the sensitive subject of the applicability of the doctrine of patent exhaustion on method patents (*Quanta Computer, Inc. v. LG Electronics, Inc.*, no. 06-937, 2008 U.S. LEXIS 4702 (June 9th, 2008)).

The Supreme Court unanimously overruled the Federal Circuit’s decision and held that (i) the doctrine of patent exhaustion applies to method patents, and that (ii) once a product is unconditionally authorized for sale, and that this product comprises the essential elements of a patented invention, with no other intended use than to practice the patent, the doctrine of patent exhaustion applies and the patent owner can no longer invoke patent law in an attempt to receive additional royalties or limit the rights of the licensee’s subcontractors and the latter’s clients, since, by doing so, the patent owner would extend the patent’s scope and the rights which the patent confers without due cause.

In reaching this decision, the Supreme Court reaffirmed its support of a doctrine which, according to its advocates, serves to maintain a competitive market. However, the Court did not rule upon the contractual aspect of the dispute between the parties as it did not discuss or limit the rights of the patent owners to impose restrictions/conditions to the sale of their products by way of a license agreement. Therefore, it follows that when patent law cannot be used to prohibit or limit the use of a product, contractual law may come into play to achieve the intended result.

The impact of this decision goes well beyond the issue of the scope of applicability of the doctrine of patent exhaustion, since patent owners will have every interest, before marketing their product, to review the wording of their license agreements (at

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least with respect to, directly or indirectly, the territory of the United States), for instance by:

1- drafting license agreements which clearly restrict the right of the licensee to re-sell patented articles only to purchasers authorized by the licensor, while preventing anti-competitive practices. As such, (i) the sale will be deemed conditional and the doctrine of patent exhaustion will not apply, (ii) every third party purchaser will also have to enter into a license agreement with the patent owner, allowing the latter to supervise and restrict the use of the patented article, (iii) the patent owner will thereby retain a certain degree of control over gains stemming from the use of the patent by imposing a royalty to be paid by every licensee; or

2- fully negotiating the amount of the royalty to retain the maximum value of the patented rights, when the license is granted to the first buyer.

Although patent owners appear to be able to limit the impact of the Supreme Court's decision by using contractual clauses to their advantage, potential licensees might be reluctant to enter into a license agreement which imposes substantial obligations upon them. It will be interesting to see how licensors and licensees will strike a balance between their respective interests.

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