

INTELLECTUAL PROPERTY & LIFE SCIENCES

Patent Exhaustion/ First Sale/Misuse as Affirmative Claims

By Yee Wah Chin

The doctrines of patent exhaustion, or first sale, and of patent misuse are generally considered only affirmative defenses to patent infringement claims. However, under *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118 (2007), where patent misuse caused or threatened injury to an entity, that entity may assert misuse as an independent claim. Moreover, several recent precedents indicate that patent exhaustion or first sale may also be affirmative claims.

MedImmune, which had been paying royalties under a license agreement, sought declaratory judgment that the patent was invalid and unenforceable so that no royalties are due. Genentech answered that there was no case or controversy because MedImmune was paying royalties, had therefore not infringed Genentech's patents, and Genentech was not threatening suit. The Supreme Court held that a declaratory judgment action was proper,

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and MedImmune "was not required, insofar as Article III is concerned, to break or terminate its 1997 license agreement before seeking a declaratory judgment in federal court that the underlying patent is invalid, unenforceable, or not infringed." The crucial factors are whether the dispute is "definite and concrete, touching the legal relations of parties having adverse interests" and "real and substantial," such that it will permit "specific relief through a decree of a conclusive character."

This is consistent with the Court's earlier holding in *Altvater v. Freeman*, 319 U.S. 359, 364, 365 (1943), that:

The fact that royalties are being paid did not make this a 'difference or dispute of a hypothetical or abstract character.'... the requirements of case or controversy are met where payment of a claim is demanded as of right and where payment is made, but where the involuntary or coercive nature of the exaction preserves the right to recover

the sums paid or to challenge the legality of the claim.

In *B. Braun Medical, Inc. v. Abbott Laboratories*, 124 F.3d 1419, 1427 (Fed. Cir. 1997), the Federal Circuit affirmed the holding of a damages trial following a finding of patent misuse, based on the trial court's discretion under the Declaratory Judgment Act to grant "further necessary or proper relief based on a declaratory judgment." "[T]he same actions by a patentee that result in patent misuse may also serve as an element of an affirmative claim for damages." Thus the court's earlier comment in *Windsurfing International, Inc. v. AMF, Inc.*, 782 F.2d 995, 1001 (Fed. Cir. 1986), that "patent misuse is an affirmative defense to a suit for patent infringement," does not exclude misuse being an affirmative claim.

ExcelStor Technology, Inc. v. Papst Licensing GmbH & Co. KG, 541 F.3d 1373 (Fed. Cir. 2008), may indicate a different result for patent exhaustion/first sale affirmative claims. ExcelStor made and sold hard-disk drives under license from Papst. It sold HDDs to Hitachi. Both ExcelStor and Hitachi agreed to pay royalties to Papst on drives covered by Papst's patents. ExcelStor's agreement allegedly also required Papst to notify ExcelStor if another entity was paying royalties to Papst on HDDs that ExcelStor manufactured. Upon learning that Hitachi was apparently paying royalties to Papst under an agreement that pre-

dates ExcelStor's, for HDDs that Hitachi bought from ExcelStor, ExcelStor sued for a declaration that Papst violated the patent exhaustion doctrine and its agreement with Papst violated patent exhaustion, and for fraud and breach of contract.

The Federal Circuit affirmed dismissal for lack of subject matter jurisdiction. It concluded that ExcelStor's complaint failed to meet the requirements of *Christianson v. Colt Industries Operating Corp.*, 486 U.S. 800 (2005), that federal question jurisdiction involving patent law must involve a claim under the patent law or a right to relief that requires resolution of a patent law issue. "[P]atent exhaustion is a defense to patent infringement, not a cause of action... Thus, ExcelStor's claims, which merely invoke defenses to hypothetical claims of patent infringement, do not 'arise under' the patent laws."

The court stated that:

ExcelStor's claims do not establish federal subject matter jurisdiction because they do not require resolution of a substantial question of federal patent law. The exhaustion doctrine prohibits patent holders from selling a patented article and then 'invoking patent law to control postsale use of the article.' ... ExcelStor's amended complaint does not allege that Papst invoked the patent laws to control the post-sale use of the hard disk drives. ... ExcelStor's amended complaint alleges that Papst violated the patent exhaustion doctrine by 'collecting two different royalties from the same patented product.' ... But there is no federal cause of action for collecting royalties twice on the same goods.

ExcelStor's reasoning regarding the

hypothetical nature of the dispute, which underlies its conclusion, seems inconsistent with *MedImmune* and *Altwater v. Freeman*.

In fact, several district courts have recognized that patent misuse and patent exhaustion/first sale may be affirmative claims.

For example, in *Delano Farms Co. v. The California Table Grape Commission*, 623 F. Supp. 2d 1144 (E.D. Ca. 2009), the California Table Grape Commission, after coordinating the development by the U.S. Department of Agriculture of grape varieties funded by growers and distributing the new varieties free to growers for years, persuaded the USDA to patent the new varieties and license them to the commission. The commission then licensed the varieties to three nurseries, permitting the nurseries in turn to license to growers, subject to royalties that they pass through to growers and to restrictions on propagating the plant and reselling to third parties. Growers also pay the commission an assessment on each box of grapes sold. Some growers sued for patent inequitable conduct, patent misuse, and Sherman Act Section 2 and state law violations. The court granted on the merits a motion to dismiss patent misuse claims based on the propagation restrictions, clearly assuming that an affirmative misuse claim is appropriate.

In *In re Gabapentin Patent Litig.*, 649 F. Supp. 2d 340 (D.N.J. 2009), a generic drug maker sued for infringement by the brand name manufacturer counterclaimed for declaratory judgment of patent misuse, unclean hands, monopolization and unfair competition. The court denied a motion to dismiss the patent misuse counterclaim, finding "patent misuse, unlike unclean hands, to be a proper basis for declaratory relief."

In *Broadcom Corp. v. Qualcomm Inc.*, 2009 WL 684835 (S.D. Ca. 2009), Broadcom sought declaratory judgment of patent misuse from violation of the patent

exhaustion/first sale doctrine. It claimed that Qualcomm had misused its patents covering chipsets for wireless communications devices, by seeking royalties in violation of the patent exhaustion/first sale doctrine from both chipset makers and makers of handsets that incorporate those chipsets. The complaint was dismissed without prejudice because Broadcom had not identified which of Qualcomm's many patents had been exhausted and its alleged injuries were speculative. The court apparently assumed that such an affirmative claim is permissible.

In *Linzer Products Corp. v. Sekar*, 499 F. Supp. 2d 540 (S.D.N.Y. 2007), the licensee alleged contract and patent claims, and sought declaratory judgment that an exclusive dealing condition was patent misuse. The court rejected the argument that patent misuse cannot be an independent cause of action, stating that "B. Braun did not proscribe claims seeking a declaratory judgment of patent misuse. Indeed, in later actions, the Federal Circuit has allowed such claims without comment."

Minebea Co., Ltd. v. Papst, 444 F. Supp. 2d 68 (D.D.C. 2006), and *In re Papst Licensing, GmbH Patent Litigation*, 2000 WL 1859013 (E.D. La. 2000), involved a joint venture to produce computer hard-disk drive motors. The licensee sought declaratory judgment for patent exhaustion, equitable estoppel/legal estoppel/implied license and patent misuse, while the patent holder moved in the Eastern District of Louisiana and the District of D.C. to dismiss for lack of subject matter jurisdiction. Both courts found jurisdiction.

Thus, patent misuse and patent exhaustion/first sale may be available as affirmative claims in addition to as affirmative defenses and litigators should consider them when making claims in a patent dispute in which misuse or exhaustion/first sale may be involved. ■