No. 06-937

IN THE

Supreme Court of the United States

QUANTA COMPUTER, INC. *et al.*,

Petitioners,

—v.—

LG ELECTRONICS, INC.,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF OF AMERICAN INTELLECTUAL PROPERTY LAW ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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INTEREST OF AMICUS CURIAE[1]

The American Intellectual Property Law Association (AIPLA) is a voluntary bar association of over 17,000 members who work daily with all manner of intellectual property, *e.g.*, patents, trademarks, copyrights and trade secrets, and the legal issues that they present. Members include attorneys in private and corporate practice as well as government service. AIPLA's membership is intimately involved with the legal and business issues underlying the development, commercialization and exploitation of intellectual property, including enforceability, antitrust, and licensing issues.

AIPLA members are often on both sides of any matter, representing both plaintiffs and defendants for litigation and both licensors and licensees for transactions. As part of its central mission, AIPLA

[1] The parties have consented to the filing of this brief. No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members, or its counsel made a monetary contribution to its preparation or submission.

After reasonable investigation, AIPLA believes that no member of its Board or Amicus Committee who voted to prepare this brief on its behalf, or any attorney in the law firm or corporation of such a Board or committee member or attorney who aided in preparing this brief, represents a party with respect to this litigation. Some committee members or attorneys in their respective law firms or corporations may represent entities which have an interest in other matters which may be affected by the outcome of this litigation.

is dedicated to encouraging the healthy development of intellectual property law. Accordingly, AIPLA has a vital interest in the issues presented by this case, which will have a far-reaching impact on intellectual property rights and their exploitation.

SUMMARY OF ARGUMENT

AIPLA believes that a patentee may, with adequate notice, require separate licenses at various stages along the downstream chain of sophisticated purchasers and users of its patented invention. Not only does this create market efficiencies, but it also allows for the appropriate and proper exploitation of intellectual property rights. There is no *per se* anticompetitive effect in allowing licensors and licensees the freedom to create such agreements.

The parties and *Amici* have characterized the relationship between LG and Intel as essentially that of licensor and licensee. And while that is literally correct, and frames much of the analysis set forth below, AIPLA submits that it mischaracterizes a significant portion of the transaction at issue. More fundamentally, it skews the analysis and even the Question Presented to this Court for review by ignoring the real-world context of what occurred. Any decision must account for the Constitutional balance between the public's interest in accessing technology and promoting innovation. AIPLA believes that license obligations can require an agreed-upon allocation of burdens to obtain specific additional agreements as between sophisticated parties.

Generally speaking, infringement occurs when a party makes, uses or sells the invention claimed in a patent without authorization. 35 U.S.C. § 271. As set forth more fully below, LG sued Intel both for direct infringement (35 U.S.C. § 271(a)) and contributory infringement (35 U.S.C. § 271(c)). Intel settled both claims with a set of agreements that have a different impact on each claim (these agreements include licenses and will be referred to in the singular as the "LG-Intel License" for convenience). By express terms, Intel received a license that immunizes its making, using and selling of components from literal infringement. But, for contributory infringement Intel's license is nothing more than a covenant not to sue Intel (only) for aiding its customers' infringement. It is through this prism that the transaction, and therefore the dispute, must be viewed.

Notably, the submissions in this case to date ignore the statutory segregation of patent infringement from antitrust and fail to highlight the areas of contributory infringement and patent misuse. *See* 35 U.S.C. § 271. There are three discrete yet integrated legal concepts at play here: (i) patent exhaustion (sometimes called first sale), (ii) implied license, and – based upon citations to this Court – (iii) price-fixing. The first two must be analyzed under the Patent Act and are directly addressed by many of the briefs before the Court; the third is an antitrust issue.

As for this third issue, all filers seemingly agree, at least implicitly, that this is not a case where antitrust analysis is warranted. Nevertheless, patent and antitrust laws are interrelated and both "share the common purpose of promoting innovation and enhancing consumer welfare." U.S. DEPARTMENT OF JUSTICE AND FEDERAL TRADE COMMISSION ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL

PROPERTY (1995)[2] (the "DOJ-FTC Antitrust IP Licensing Guidelines") § 1 (citing *Atari Games Corp. v. Nintendo of America, Inc.*, 897 F.2d 1572, 1576 (Fed. Cir. 1990)). AIPLA therefore submits this brief *amicus curiae*, in large part, to reinforce each legal doctrine and explain why they must remain independent since each serves its own necessary purpose.

AIPLA, however, demurs on the factual issues due to the limited public record. AIPLA understands that Intel was LG's direct, first-instance licensee but that the license required downstream users to obtain their own licenses from LG. The decisions below rely on the notice letter from Intel to its downstream customers (the so-called "OEMs," which for this brief include subsystem suppliers) purporting to inform them of this requirement (the "Intel Notice Letter"). AIPLA does not have sufficient information to evaluate the effectiveness of that notice nor to dispute or support the findings below on this point, so AIPLA will not comment on that issue (and does not believe it to be ripe for consideration by this Court).

Nonetheless, as a general matter AIPLA believes that where sufficient notice has been given, strong market efficiencies support allowing a licensor to establish royalty rates at more than one key point in the distribution chain. This can take into account many factors, including:

- Possible uses and differences in licensed inventions,
- Proper allocation of resources,

[2] http://www.usdoj.gov/atr/public/guidelines/0558.pdf.

- Incomplete knowledge by the first-instance licensee of how devices or components will be used by downstream purchasers,
- The actual structure of the transaction, and
- Sophistication of the parties in optimizing transactions.

The reality is that some items of manufacture, exemplified in this case by electronic components, can have different value – and therefore rationally command different royalties – based upon their use.

This becomes clearer when it is considered in a real-world context. In the biologic field an antibody can be used either as a diagnostic tool (lower royalty) or as a therapeutic for treating patients (higher royalty). It would be inefficient to charge the higher therapeutic royalty rate to the diagnostic market, and yet that is precisely the result that Petitioners' proposed doctrine in this case would demand. Similarly, the brief *Amicus Curiae* of Croplife International at 10-12, explains why limiting licensing arrangements, *e.g.*, those not requiring exhaustion, avoid "astronomical prices." *See also* brief *Amicus Curiae* of Biotechnology Industry Organization at 5-6.

These examples reinforce that allowing sophisticated parties to structure transactions with different royalties for different uses – without attempting to define all uses and royalty rates in the first-instance license – is pro-competitive and creates increased market efficiencies.[3]

AIPLA accepts for purposes of this brief that there are two groups of patent claims implicated by the Intel-LG License, one group covering "components" (items manufactured by Intel) and the other covering "end-products" (methods or devices utilizing those components such as those made by the OEMs). AIPLA further understands that the Intel-LG License permits Intel to make, use and sell components and immunizes Intel for its role in supplying components used in multiple applications in the end-products (at least some uses of which are covered by separate patent claims).[4] What is at issue in this case is whether or not downstream OEMs are liable for infringement because they used these Intel components in their end-products.

AIPLA also understands that there are two relevant time periods when the OEMs purchased components from Intel: (1) prior to the LG-Intel License and (2) after the license and receipt of the Intel Notice Letter. Each period must be considered separately, keeping in mind that the Intel-LG License released Intel's customers retroactively "from liability

[3] *See* DOJ-FTC Antitrust IP Licensing Guidelines § 2, Ex. 1 (showing example where "charg[ing] different royalties for ... different uses" was likely procompetitive).

[4] One of the factual confusions AIPLA faces is the role of the so-called Microsoft License. *E.g.*, *LG Elecs., Inc. v. Bizcom Elecs., Inc.*, 453 F.3d 1364, 1371 (Fed. Cir. 2006). For convenience, AIPLA addressed only the Intel-LG License to the extent necessary.

for any claim of patent infringement that arose prior to the effective date...." *LG Elecs., Inc. v. Asustek Computer, Inc.*, 248 F. Supp. 2d 912, 917 (N.D. Cal. 2003).

The courts below made much of the difference between a product patent claim (which covers the manufacture and general use of components as such) and a method claim (which covers a specific use of a component in the larger end-product). *E.g.*, 453 F.3d at 1370. For purposes of analyzing these legal doctrines, however, AIPLA sees little difference in their application by these facts: the component is being used for one of the intended, claimed methods. Thus, AIPLA does not subscribe to the distinction below (453 F.3d at 1370) applying the law differently to *these* method and product claims on the present facts.

Another point that the lower courts considered was whether or not there are substantial non-infringing uses for the Intel components, *i.e.*, are there uses that do not require additional licenses from LG? *E.g.*, *LG Elecs., Inc. v. Asustek Computer, Inc.*, Nos. C 01-00326 CW et al., 2002 WL 31996860, at *11-13 (N.D. Cal. Aug. 20, 2002). Although this issue might be relevant in some cases, such as an unconditional sale, AIPLA submits that it is a *red herring* in the context of this dispute. Intel, the OEMs and even LG are all sophisticated consumers and each knew the intended uses of the components (even if not the specifics) and that they were covered by LG's patents. (This is not a situation where the components have *only* one possible use each.) Each of the contracting parties knew there were limitations on any licenses to the components vis-à-vis any use in end products, having engaged in these transactions with notice to this effect. Therefore, whether or not there are other uses is not relevant. Reasonable license terms, such as the allocation of responsibility to obtain licenses between sophisticated parties to a transaction, should not raise fears of exhaustion breaking the licensing chain. At issue here are not "off the shelf" items bought in a storefront transaction, where the details of sales contracts among up-stream merchants are unknown; in such situations the U.C.C. would apply and it is reasonable and appropriate for the patent rights to be exhausted since the consumer is a *bona fide* purchaser free of infringement risk.[5] The sophistication and transparency of the present transaction to all involved therefore renders the issue of non-infringing uses irrelevant for purposes of this case.

Finally, there are a number of factual issues that must be accounted for in synthesizing the cases relied upon by Petitioners and *Amici*, which render some arguments inapposite. For instance, this is not a situation where the patentee is trying to leverage

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[5] By way of contrast, this case does not involve a sale governed by the Uniform Commercial Code, such as for an off-the-shelf commodity. Such sales carry a covenant of non-infringement:

> (3) Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement …

U.C.C. § 2-312(3) (2004). A sale by the licensee subject to this covenant would force the licensee to limit any downstream patent liability by structuring any license to avoid infringement. It also allows *bona fide* purchasers the opportunity to buy goods without fear of suit.

control over unpatented components by sale of patented items;[6] here, the uses and devices are strictly within the scope of the patents-in-suit.

Principal among the misapplied cases is *United States v. Univis Lens Co.*, 316 U.S. 241 (1942), a case that is primarily focused on pricing and distribution controls (and has routinely been recognized as such[7]). It is also a case where there was only one use for the licensed product, as the Court noted the lens blank and finished lens were essentially the same for patent purposes. *Id.* at 248-49, 251. In *Univis* the patentee violated the Sherman Act by trying to enforce the patent beyond the scope of the grant, *i.e.*, to control pricing. In doing so, the pat-

[6] Such tying cases involve the use of a patented invention (such as a mechanism for playing motion pictures) to control the purchase or use of unpatented work pieces or related objects (like the rental of motion pictures). *See Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502, 506-07 (1917). Thus, arguments that this case is a modern-day version of *Henry v. A.B. Dick Co.*, 224 U.S. 1 (1912), overruled by *Motion Picture Patents*, or that attempt a *per se* analysis for tying based upon older cases are misdirected. *See Illinois Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 35 (2006) ("Over the years … this Court's strong disapproval of tying arrangements has substantially diminished. Rather than relying on assumptions, in its more recent opinions the Court has required a showing of market power in the tying product.").

[7] *See Armstrong v. Motorola, Inc.*, 374 F.2d 764, 775 (7th Cir. 1967) (*Univis* "was a Sherman Act case in which the patentee had been using his patent to achieve resale price maintenance and therefore the case is not in point."); *American Indus. Fastener Corp. v. Flushing Enters., Inc.*, 362 F. Supp. 32, 36 (N.D. Ohio 1973) ("*Univis* … involves price restrictions…."); *see also* DOJ-FTC Antitrust IP Licensing Guidelines § 5.2.

entee also prevented licensees from challenging the licensed patent, thereby further extending the grant.[8] Thus, a significant part of the scheme in *Univis* not only controlled pricing but also prevented patent challenges. While the *dicta* in *Univis* arguably relates to patent exhaustion, the holding does not rest on that doctrine nor should the case be extended to a post-1969 patent license dispute. This is not an instance where there is an allegation of price fixing; there is no attempt to control downstream users nor is there an attempt to mandate minimum price obligations.

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[8] In *U.S. Phillips Corp. v. Int'l Trade Comm'n*, 424 F.3d 1179 (Fed. Cir. 2005), Judge Bryson explained how this Court changed that law:

> The effect of a nonexclusive license was different before the Supreme Court, in *Lear, Inc. v. Adkins*, 395 U.S. 653 … (1969), abolished the patent doctrine of licensee estoppel. **Before *Lear*, a nonexclusive license had a legal effect that made it more than a mere covenant by the licensee not to sue. Acceptance of the license barred the licensee from challenging the validity of the patent.** Some of the early decisions regarding patent-to-patent tying arrangements appear to have been based, at least in part, on that feature of pre-L*ear* patent licenses. *See, e.g.*, *Am. Securit Co. v. Shatterproof Glass Corp.*, 268 F.2d 769, 777 (3d Cir. 1959); *Int'l Mfg. Co. v. Landon*, 336 F.2d 723, 731 (9th Cir. 1964); *see also Duplan Corp. v. Deering Milliken, Inc.*, 444 F.Supp. 648, 699 (D.S.C. 1977), *aff'd in pertinent part*, 594 F.2d 979 (4th Cir. 1979). In the post-*Lear* era, the "acceptance" of a license has no such restrictive effect on the licensee's freedom.

424 F.3d at 1190 n.3 (emphasis supplied).

Accordingly, AIPLA submits this brief generally in support of Respondent on the Question Presented for these facts. AIPLA believes that a licensor may, with adequate notice, require separate licenses at various stages within the chain of downstream, sophisticated purchasers and users of its patented invention. Not only does this create market efficiencies, but it also allows for the appropriate and proper exploitation of intellectual property rights.

ARGUMENT

The United States Constitution, Art. I, Sec. 8, ¶8, authorizes Congress 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." The resulting patent system has been widely characterized as a legal, limited monopoly which serves as an incentive to innovation and disclosure such that the public learns from the disclosure and may even improve upon it.[9] This balances the property interest of a patentee with the public's interest in a fair and legal market-

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[9] Contrast the often-debated example of the infamous Chamberlen family, who kept their invention of the obstetric forceps secret for generations thereby maintaining their income based upon their successes in child delivery and reduced death-rates. *See* P.M. Dunn, *The Chamberlen Family (1560-1728) and Obstetric Forceps*, 81 ARCH. DIS. CHILD FETAL NEONATAL ED. 232-35 (1999), http://fn.bmjjournals.com/cgi/content/full/81/3/F232. Presumably, if patents had been available to reward and protect their invention, the Chamberlen family would have patented and publicly disclosed it, thereby putting the forceps into wider use to save more lives while still rewarding the inventors with financial gains.

place.[10] The role advanced by Petitioners, however, would upset that balance.

1. REVIEW OF THE LAW

I. Patent Rights

AIPLA begins its analysis with the basic mechanism for exploiting patent rights: the ability to exclude unauthorized users from using the innovation. The right to exclude is "[t]he heart of [a patentee's] legal monopoly," *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 135 (1969), which "enable[s the patentee] to secure the financial rewards for his invention," *Univis*, 316 U.S. at 250. *See Pennock v. Dialogue*, 27 U.S. 1, 19 (1829) (patentee's right to exclude provides a "reasonable reward to inventors" for disclosing their inventions).[11]

As this Court stated in *Adams v. Burke*, 84 U.S. 453, 456 (1873), "[t]he right to manufacture, the right to sell, and the right to use are each substantive rights, and may be granted or conferred separately by the patentee." *See Continental Paper Bag*,

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[10] *Carl Schenck, A.G. v. Nortran Corp.*, 713 F.2d 782, 786 n.3 (Fed. Cir. 1983) ("The antitrust laws, enacted long after the original patent laws, deal with appropriation of what should belong to others. A valid patent gives the public what it did not earlier have."); *Continental Paper Bag Co. v. Eastern Paper Bag Co.*, 210 U.S. 405, 424-25 (1908).

[11] 35 U.S.C. §§ 154(a)(1), 271, 283; *Bloomer v. McQuewan*, 55 U.S. 539, 549 (1852) ("The franchise which the patent grants, consists altogether in the right to exclude every one from making, using, or vending the thing patented, without the permission of the patentee. This is all [the patentee] obtains by the patent.").

210 U.S. at 423-24; *accord eBay Inc. v. MercExchange, L.L.C.*, __ U.S. __, 126 S. Ct. 1837, 1840-41 (2006); *see also Special Eqm't Co. v. Coe*, 324 U.S. 370, 376 (1945) ("[W]e think it plainly is legitimate to use a patent ... as a means of preventing appropriation by others of petitioner's more important complete invention which he is using ...."). The ability to sue and thereby exclude others is the patentee's right, c*f. Continental Paper Bag*, 210 U.S. at 430, such that a patent license is a mere waiver of the right to sue the licensee, *De Forest Radio Tel. Co. v. United States*, 273 U.S. 236, 242 (1927).

A. Patent Licenses

One way to exploit a patent is to make and sell the patented invention. Another is to license others to do so. A patentee's refusal to license the patent at all, however, does not constitute a "misuse or illegal extension of the patent right." 35 U.S.C. § 271(d)(4); *see* DOJ-FTC Antitrust IP Licensing Guidelines § 2.2. Similarly, a patentee that decides to license may limit the licensee to a particular defined field of use[12] or to sales in a particular region.[13] These are

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[12] *See, e.g., General Talking Pictures Corp. v. Western Elec. Co.*, 305 U.S. 124, 126-27 (1938).

[13] A first-instance licensee is subject to a geographically-restricted license, but products that are then properly sold by the licensee can be moved out of the licensed area by the buyer so long as there is no contractual limitation. *See Adams v. Burke*, 84 U.S. 453, 455-57 (1873) (affirming dismissal of a patent suit against a customer of a licensee with a restricted territory; the customer had purchased the product within the territory and moved it outside of the territory); *Hobbie v. Jennison*, 149 U.S. 355, 361-63 (1893) (affirming dismissal of suit against

(footnote continued ...)

not improper actions, and can be procompetitive. *See* DOJ-FTC Antitrust IP Licensing Guidelines § 2.3 ("Field-of-use, territorial, and other limitations on intellectual property licenses may serve procompetitive ends by allowing the licensor to exploit its property as efficiently and effectively as possible.").

Typically, a license is stated explicitly in a document setting forth what rights are granted, *see De Forest*, 273 U.S. at 241, but it also can be created in other ways. Two examples are:

- implied license, an equitable doctrine that requires examining the totality of the circumstances; and
- first sale, also called patent exhaustion, which is a legal doctrine arising out of policy-imposed limitations on the rights granted by a patent that provides *bona fide* purchasers with a right to use and resell without fear of suit.

Both are relevant here.

i. Implied License

An implied license to a patent is a form of estoppel. It arises "by acquiescence, by conduct, by equitable estoppel (estoppel in pais), or by legal estop-

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a geographically-restricted licensee who sold products within his territory knowing they were to be shipped and used in another licensee's territory); *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659, 664-67 (1895) (reversing judgment against purchaser of products from licensee who transported them into another licensee's territory and offered them for sale there).

pel." *Wang Labs., Inc. v. Mitsubishi Elecs. Am. Inc.*, 103 F.3d 1571, 1580 (Fed. Cir. 1997); *accord Kieruff v. Metro. Stevedore Co.*, 315 F.2d 839, 842 (9th Cir. 1963); *see St. Joseph Iron Works v. Farmers Mfg. Co.*, 106 F.2d 294, 298 (4th Cir. 1939) (finding implied license to make patented article by agreement to modify production machinery); *Goss v. Henry McCleary Co.*, 92 F.2d 444, 444-45 (9th Cir. 1937) (contract to modify machines to practice patented process granted implied license to practice process subsequent to a necessary rebuilding of the machine); *see also Dickerson v. Colgrove,* 100 U.S. 578, 580 (1880) ("[H]e who by his language or conduct leads another to do what he would not otherwise have done, shall not subject such person to loss or injury by disappointing the expectations upon which he acted.").

An implied license arises from the entire context of a transaction, particularly the patent owner's conduct, and not just from the unilateral expectations of a party. *Carborundum Co. v. Molten Metal Equip. Innovations, Inc.*, 72 F.3d 872, 878 (Fed. Cir. 1995); *Stickle v. Heublein, Inc.,* 716 F.2d 1550 (Fed. Cir. 1983) (citing *De Forest*, 273 U.S. at 236, 241); *AMP Inc. v. United States*, 389 F.2d 448, 451 n.3 (1968) (patent owner's "motive does not have any probative weight"). Moreover, since it is equitable in nature, the implied license may extend to patents not literally involved in a transaction. *E.g.*, *Minnesota Mining & Mfg. Co. v. E.I. du Pont de Nemours & Co.*, 448 F.2d 54, 57-58 (7th Cir. 1971) (addressing undisclosed dominant patent application that later issues as patent).

ii. Patent Exhaustion - First Sale

Patent exhaustion is a legal doctrine, whereby certain transactions entered into by the patentee exhaust or terminate any patent rights in the item purchased based upon the unfettered transfer of an authorized item. *See Lisle v. Edwards*, 777 F.2d 693, 695 (Fed. Cir. 1985) (sale of tool is complete relinquishment even allowing repackaging without need of a sublicense). It is, in effect, a complete license to all subsequent purchasers.

The sale of a patented article in the absence of contractual restraints on the purchaser terminates – or exhausts – the patent right to exclude:

> Where the patentee has not parted, by assignment, with any of his original rights, but chooses himself to make and vend a patented article of manufacture, it is obvious that a purchaser can use the article in any part of the United States, and, ***unless restrained by contract with the patentee***, can sell or dispose of the same. It has passed outside of the monopoly, and is no longer under the peculiar protection granted to patented rights.

Keeler v. Standard Folding Bed Co., 157 U.S. 659, 661 (1895) (emphasis supplied); *see Mitchell v. Hawley*, 83 U.S. 544, 547 (1873) (a patentee who sells or authorizes a sale "*without any conditions* … must be understood to have parted to that extent with all his exclusive right … in the patented machine…" (emphasis supplied)); *Adams*, 84 U.S. at 456 (following a sale by "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 patentees" (emphasis supplied)); *Cf. Lisle*, 777 F.2d at 695 (licensed sales).

Unlike implied license, patent exhaustion arises solely by the actions of the patentee or those in privity with him; it does not require detrimental reliance on the part of another, nor does it even inquire into the buyer's state of mind. *See Keeler*, 157 U.S. at 666.

Patent exhaustion allows free commerce of patented articles, without the excessive "regulation" caused by patent owners imposing restrictions on downstream uses and sales, unless the buyer has agreed to them. Its serves the goal of eliminating uncertainty once a product is bought; sound policy endorses transactions being free of further obligation unless there is an agreement to the contrary. On the other hand, if there is an agreement that limits its use, such as a geographic restriction or field of use (see notes 12-13, *supra*), then that limitation, assuming proper notice to subsequent purchasers, is followed. In this way, informed and sophisticated buyers may reach a commercially favorable arrangement that includes restrictions, while *bona fide* purchasers – such as consumers buying off the shelf – can purchase items without fear of suit. (*See* note 5, *supra*.) It also eliminates the possibility that remote purchasers, having purchased patented goods without notice or appreciation of any restraints, will be unfairly restricted in their ability to use or resell patented products.

II. Contributory Patent Infringement and the 1952 Patent Act

Notably, most briefs so far filed have failed to discuss contributory patent infringement as well as its interaction with doctrines such as patent misuse. That, however, is the prism for understanding the Intel-LG transaction and for understanding (as well as dismissing) many of the pre-1952 citations relied on by Petitioners and *Amici*.

A. Contributory Infringement

Contributory infringement is defined by 35 U.S.C. § 271(c). It occurs when there is an unauthorized sale of "a component of a patented machine ... or apparatus for use in practicing a patented process, **constituting a material part of the invention**" that is especially made for that use and is not a staple article of commerce. *Id.* (emphasis supplied).

This doctrine can easily be understood by varying the instant facts for a hypothetical:[14] <u>If</u> there were no license between LG and Intel, then Intel could be charged as a direct infringer (35 U.S.C. § 271(a)) for patent claims covering the components themselves. Since Intel's components only constitute a portion of each end-product, however, Intel could not be charged as a direct infringer of the end-product or methods-of-use claims; nonetheless, Intel could be charged as a contributory infringer of those patent

[14] For simplicity, this hypothetical assumes all activities are domestic.

claims if its components are essential, non-staple portions of the end-products.[15]

The LG-Intel License in the present case, however, immunizes Intel from an allegation of contributory infringement. It is this same license that gives rise to the exhaustion arguments, but in making that argument Petitioners and their supporters rely on antitrust case law that mostly precedes enactment of § 271(c). That enactment and its legislation history are vital to the analysis of the infringement and patent misuse doctrines.

This Court in *Dawson Chemical Co. v. Rohm and Haas Co.*, 448 U.S. 176 (1980), noted that "emerg[ing] from [a] review of judicial development is a fairly complicated picture, in which the rights and obligations of patentees as against contributory infringers has varied over time." *Id.* at 197; *see id.* at 204 (balancing contributory infringement and patent misuse). Based upon this review, the Court clarified that § 271(d) immunizes certain sale and licensing requirements from charges of patent misuse, and "permits patentees to exercise control over nonstaple articles used in their inventions" by being able to assert contributory infringement. *Dawson*, 448 U.S. at 200.

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[15] Although some *Amici* have compared the instant factual scenario to tying, in many ways this case is "anti-tying." Here, the issue is <u>not</u> that a license to one set of rights requires taking a license to additional rights. Instead, the Intel-LG license covers less than it could have. It is, in fact, a separation of rights requiring further downstream licenses, such that the tying/bundling analysis is inappropriate.

The Fifth Circuit's *In re Yarn Processing Patent Validity Litigation* decision, 541 F.2d 1127 (5th Cir. 1976), also considered the balance between any extension of the patent monopoly to additional products and the scope of patent protection. It did so in the context of contributory infringement, understanding that the scope of a license can and should take infringement into account. As the Fifth Circuit concluded, "the restrictions on sale were within the scope of the patent grant because they ... did no more than to prevent contributory infringement by resale to unlicensed users." *Id.* at 1135. The patentee in that case, Leesona, could appropriately require licenses to "throwsters" at various vertical stages.

> There is no real question that under the terms of the machinery manufacturing licenses, the manufacturers were not allowed to sell to a throwster not licensed by Leesona. We fail to see how this is an illegal extension of the patent monopoly. The patents are assumed to be valid. Leesona had the right to license the use of the machinery separately from its manufacture and sale.

Id.; *see also Arizona Cartridge Remanufacturers Assoc. v. LexMark Int'l Inc.*, 421 F.3d 981, 986-88 (9th Cir. 2005).

On the facts of this case, it appears that the so-called license to Intel operates, in fact, as a non-assertion clause (also called a covenant not to sue).[16] Intel will not be sued for contributory infringement but Intel's customers – Petitioners – must seek their own licenses from LG. (The only difference between this case and *Yarn Processing* appears to be the insignificant *Yarn Processing* requirement that sales be only to licensees as opposed to the LG-Intel License's silence as to purchasers.) As the Government noted in its report Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition,[17] at pp. 88-89:

> [N]on-assertion clauses serve one of the same functions as a license or cross license, *i.e.*, they permit the contracting parties to avoid costly litigation over the use of an IP right.

For that reason, the Government concluded that such non-assertion agreements and other variations of standard licensing "either will not raise any competitive concerns or that the efficiencies of these types of agreements will be sufficient to alleviate competitive concerns." *Id.* at 99 (listing factors to consider).

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[16] There are, of course, differences between licenses (which require mutual consideration) and covenants not to sue (which can be unilateral) that are not material to the instant analysis but should be recognized.

[17] U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS (2007), available at www.usdoj.gov/atr/public/hearings/ip/222655.pdf.

B. Patent Misuse

Nothing in the instant facts suggests that the patentee has overreached. The parties are sophisticated transactors in patents and licenses, and Congress has recognized the importance of immunizing certain patent-related controls and transactions from a charge of patent misuse. Nonetheless, misuse has been injected into this case at least conceptually.

Historically, accused infringers asserted patent misuse as an affirmative defense to infringement based upon license terms. The gravamen of the misuse allegation was inappropriate exploitation of a patent beyond its legal bounds.[18] In many ways, this is similar to the exhaustion claim asserted here – the limiting of exploitation.

In 1952, however, the patent laws were amended to add 35 U.S.C. § 271(d), which narrowed the equitable doctrine of misuse. Section § 271(d) reads, in its entirety:

> **No patent owner** otherwise entitled to relief for infringement or contributory infringement of a patent **shall be denied relief or deemed guilty of misuse or illegal extension**

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[18] For instance, in a pre-1952 case, *B.B. Chem. Co. v. Ellis*, 314 U.S. 495, 495-98 (1942), patent misuse barred relief for infringement even where the infringement had been actively induced by the defendant. The Court said that practical difficulties in marketing a patented invention could not justify patent misuse. *See Dawson*, 448 U.S. at 193-94, n.12 (summarizing *B.B. Chem.*).

> **of the patent right by** reason of his having done one or more of the following:
>
> (1) derived revenue from acts which if performed by another without his consent would constitute contributory infringement of the patent;
>
> (2) **licensed or authorized another to perform acts which** if performed without his consent **would constitute contributory infringement** of the patent;
>
> (3) sought to enforce his patent rights against infringement or contributory infringement;
>
> (4) **refused to license or use any rights** to the patent; or
>
> (5) **conditioned the license of any rights to the patent or the sale of the patented product on the acquisition of a license to rights in another patent or purchase of a separate product**, unless, in view of the circumstances, the patent owner has market power in the relevant market for the patent or patented product on which the license or sale is conditioned.

35 U.S.C. § 271(d) (emphasis supplied).[19]

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[19] The charging language and subparagraphs 1 to 3 were enacted in 1952. Subparagraphs 4 and 5 were added by amendment in 1988 in response to the "migrat[ion]" of concepts from patent law to antitrust law. S*ee Illinois Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 38 (2006). Congress therefore amended § 271(d) to exclude some conduct from attack and un-

(footnote continued ...)

As this Court has noted, the legislative history "strongly reinforce[d] the conclusion that § 271(d) was designed to immunize" patentees from charges of patent misuse and antitrust violations based upon licensing conditions. *Dawson*, 448 U.S. at 204. "[T]he relevant legislative materials abundantly demonstrate an intent both to change the law and to expand significantly the ability of patentees to protect their rights against contributory infringement." *Id.* at 203; *see* Hearings on H.R. 3760 before Subcomm. No. 3 of the H. Comm. on the Judiciary, 82d Cong., 1st Sess., 161 (1951) (1951 Hearings) (testimony of Giles S. Rich).[20]

The statute was designed to prevent patent misuse and the antitrust laws from eclipsing the doctrine of contributory infringement while Congressionally overruling this Court's two 1944 *Mercoid* decisions: *Mercoid Corp. v. Mid-Continent Inv. Co.*, 320 U.S. 661 (1944) ("*Mercoid I*") and *Mercoid Corp. v. Minneapolis-Honeywell Regulator Co.*, 320 U.S. 680 (1944) ("*Mercoid II*"). *See Illinois Tool Works*, 547 U.S. at 41; *Dawson*, 448 U.S. at 213.

The *Mercoid* cases had effectively abolished the doctrine of contributory infringement. They held

ravel the doctrines of antitrust and patent law from each other. *Id.* at 42.

[20] The Government's Brief supporting the *Petition for Certiorari*, at 20 n.7, simply states that § 271(d) is inapplicable because this case concerns patent exhaustion instead of misuse or contributory infringement. For the reasons noted above, this is an oversimplification of the balance created by these legal doctrines, as can be seen from the 1952 Act and its legislative history.

that the sale of non-patented goods could not be tied to a patented combination, even where the goods were not staple articles of commerce but had been manufactured solely to assist purchasers in directly infringing the claims of the patent. In such cases, patent enforcement for contributory infringement represented *per se* misuse (*Mercoid I*) and provided the predicate for an antitrust violation (*Mercoid II*). *See Dawson*, 448 U.S. at 204-05.

The Government "vigorously opposed" enacting § 271(d). *Id.* at 204. Its position was that the proposed enforcement of patents to prevent contributory infringement would create an exemption to the antitrust laws. As the proponents told the Committee, however, the bill:

- "strikes a proper balance between the field of patent law on the one hand and the field of general law in which antitrust laws operate on the other hand." 1948 Hearings[21] at 11 (statement of Giles S. Rich, representing NYPLA).
- "will eliminate a lot of headaches and a lot of alleged violations of the antitrust laws" 1949 Hearings[22] at 30 (statement of Giles S. Rich, representing NYPLA).

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[21] Contributory Infringement in Patents, Definition of Invention: Hearings Before Subcomm. on Pat., Trade-Marks, and Copyrights of the H. Comm. on the Judiciary, 80th Cong. (1948) ("1948 Hearings").

[22] Contributory Infringement: Hearings on H.R. 3866 before Subcomm. No. 4 of the H. Comm. on the Judiciary, 80th Cong. (1949) ("1949 Hearings").

- "will be a help not only to the patentee but to the Antitrust Department because in this branch of patent law at least it draws as distinct a law as you can in language.... [I]t shows the Department of Justice whom they aught to prosecute and shows the patentee what he may safely do to enforce the rights that the Government has given him." 1948 Hearings at 16 (statement of Robert W. Byerly, Chairman, Comn. on Pat., Ass'n of the Bar of the City of New York).
- "draws a sharp line of demarcation between the patent law and the antitrust law. This will enable patentees to protect their property without inadvertent violation of the Sherman Act, and will also simplify the work of the Department of Justice by defining a field in which restraint of trade cannot be justified under the patent law." 1948 Hearings at 19-20 (statement of Ass'n of the Bar of the City of New York).

Ultimately, Congress rejected the Government's opposition and enacted § 271(d).

In *Dawson*, this Court expressly recognized that, although the "policy of free competition runs deep in our law," "the policy of stimulating invention that underlies the entire patent system runs no less deep." 448 U.S. at 221. There was no need to determine "whether the principles of free competition could justify" the potential reduction of the incentive to invent by complete eradication of the contributory infringement doctrine. *Id.* at 223. The reason for this was because "Congress' enactment of § 271(d) resolved these issues in favor of a broader scope of patent protection." *Id.*

III. The Government's Position in *McFarling*

In this case, the Government seemingly is seeking a rule that would prevent patentees from ever controlling downstream uses or licenses outside of contract law. *Brief for the United States as Amicus Curiae Supporting Petitioners*, at pp. 7, 9, 24, 28-30. This is at odds with what it recently advocated. The *Petition for Certiorari* in *McFarling v. Monsanto Co.*, No. 04-31, and more particularly the Government's brief opposing *Certiorari* there ("Gov't McFarling Br.")[23] are instructive (and AIPLA believes correct).

In that case, Monsanto's licensees sold certain modified, patented seed (called "Round-Up Ready") to farmers like McFarling with the express license to each farmer that any harvested seed ("second generation") would not be saved for replanting. *See Monsanto Co. v. McFarling*, 363 F.3d 1336 (Fed. Cir. 2004). Monsanto patents covered both initially purchased and second generation seed. Gov't McFarling Br. at 11-12. Notwithstanding his express agreement, McFarling saved harvested seed for replanting and, when sued for infringement, claimed patent exhaustion for the second generation seed as well as patent misuse and Sherman Act violations.

The Government opposed *certiorari* and told this Court that limiting the licensee to one-time use,

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[23] http://www.usdoj.gov/atr/cases/f209200/209268.htm

thereby preventing McFarling from replanting harvested seed, "did not constitute misuse." Gov't McFarling Br. at 10 (conflating misuse with exhaustion).[24]

> In order to demonstrate patent misuse, however, petitioner was required to show that respondent's restrictions on the use of second-generation seeds "impermissibly broadened the scope of the patent grant." *C.R. Bard*, [*Inc. v. M3 Sys., Inc.*,] 157 F.3d [1340, 1372 (Fed. Cir. 1998)]. No such showing could be made here, because included within "the scope of the patent grant" is "the right to exclude others from … using … the invention." 35 U.S.C. 154(a)(1). As this case comes before the Court, respondent's refusal to license petitioner to plant second-generation (and hence patented) Roundup Ready seed merely constitutes an exercise of that statutory right, and thus cannot be patent misuse. *See* 35 U.S.C. 271(d).

Gov't McFarling Br. at 13-14.[25] The Government said that there was no improper tying in the Monsanto license requiring that there be no replanting:

> [P]etitioner's "tying" theory reduces to the notion that he is entitled to purchase re-

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[24] Seemingly, the Government discusses misuse because any failure to recognize exhaustion, in the Government's view, would be misuse.

[25] In its brief, the Government does seemingly indicate a separate analysis because the invention, seeds, is self-replicating. Gov't McFarling Br. at 13-14.

> spondent's patented invention without also honoring limits imposed on the use of the product in which that invention finds its useful, tangible expression. Petitioner points to no authority for that novel proposition, and for good reason: it is contrary both to the fundamental nature of the patent grant, which confers on the patentee the right to refuse to license its invention, *see* 35 U.S.C. 154(a)(1), 271(d),* and to the fundamental competitive concerns underlying antitrust laws.... The patent grant *itself* prohibits petitioner from saving and replanting patented seed without a license. Respondent's license restrictions thus do not constitute an unreasonable restraint of trade under Section 1 of the Sherman Act – just as they do not constitute patent misuse.
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> * Accord *Hartford-Empire Co. v. United States*, 323 U.S. 386, 432 (1945) ("A patent owner is not in the position of a quasi-trustee for the public or under any obligation to see that the public acquires the free right to use the invention. He has no obligation either to use it or to grant its use to others."); *Bement v. National Harrow Co.*, 186 U.S. 70, 90 (1902) ("[The patentee's] title is exclusive, and so clearly within the constitutional provisions in respect of private property that he is neither bound to use his discovery himself nor permit others to use it.").

Gov't McFarling Br. at 16-17 (some citations omitted).

More particularly, the Government also argued that a system which allows purchasers to plant second-generation seed would not necessarily be economically beneficial; *i.e.*, the restrictions make economic sense.

> [R]espondent could charge a fee for allowing farmers to save and replant seed.... Moreover ... requiring respondent to issue such self-renewing licenses (with attendant monitoring costs) could create disincentives for seed manufacturers to produce Roundup Ready seed, with the result that the price of such seed could actually increase, net of the new fee charged by respondent under petitioner's proposed rule. The absence of any clear evidence that it would be procompetitive to require respondent to issue a license on petitioner's desired terms provides further support for the conclusion that petitioner cannot assert a valid Section 1 claim.

Id. at 18-19. This is consistent with the position the Government took in formulating the DOJ-FTC Antitrust IP Licensing Guidelines:

> A non-exclusive license of intellectual property that does not contain any restraints on the competitive conduct of the licensor or the licensee generally does not present antitrust concerns even if the parties to the license are in a horizontal relationship, because the non-exclusive license normally does not diminish competition that would occur in its absence.

DOJ-FTC Antitrust IP Licensing Guidelines § 4.1.2.

2. APPLICATION OF LAW TO THIS CASE

I. Negative Effects of a Blanket Exhaustion Doctrine

A *per se* exhaustion doctrine, like that espoused by Petitioners (or McFarling), fails to achieve the appropriate balance between public interest and marketplace efficiencies. It would create an overwhelming chill for technology transfer. If, for instance, a patented invention were useful in multiple technology areas, only one of which was practiced by the patentee, then under Petitioners' scheme the patentee would never license the invention for use in other fields for fear that exhaustion would allow cannibalization of its primary market. *See, e.g.*, *Continental Paper Bag*, 210 U.S. at 423-25; *Special Eqm't*, 324 U.S. at 378-79.

Instead, the public interest is best served by allowing patentees to arrange commercially-appropriate licenses (based upon the sophistication of the transaction, for instance) that allow them to recoup their investments in an efficient manner and appropriately condition the sale of a patented article – which may, itself, be useful in a subsequent method – as part of a limited bundle of patent rights mandating downstream agreements.

For those reasons, AIPLA believes that allowing a patentee to collect royalties commensurate with the value conferred by the invention from multiple entities, whether they are in a vertical chain of distributors or among horizontal manufacturers serving different end-users, gives sophisticated parties the flexibility to distribute the royalty burden appropriately. This creates mutually-beneficial financial arrangements that ultimately promote competition and serve the marketplace.

The alternative is inefficient and unacceptable. If a patentee were required to recoup its entire investment of potential profit in the first license for sale, as advocated by Petitioners, first-instance licenses would be priced for the highest royalty-bearing use only – at best, weighted for the highest return based upon diversion. And if there were other uses that would yield lower royalties, then they could not be licensed for fear of exhaustion defeating the higher royalty return. *See* Jean Tirole, *The Theory of Industrial Organization*, 134, 141 (1988) (discussing arbitrage where pricing is different for different sectors or uses). This would obviously have an adverse effect on any market, but AIPLA submits it would be magnified for an emerging market where uses may not be fully known at the outset. Alternatively, allowing the royalty to be established at multiple levels in the distribution chain allows appropriate royalty allocation based upon the chosen use of the patented invention. This is the most efficient, and reasonable, financial scenario.

Petitioners would have this Court believe that contracts, and contract remedies, are an appropriate vehicle to achieve this result. Similarly, the Government stated that "the right to place such downstream restrictions should be resolved as a matter of contract, not patent law." Government Br. Supporting *Certiorari* at p. 18.

In fact, contract remedies are not helpful since they are often inadequate to accomplish the objectives because they require privity and because of the ineffectiveness of administering multiple contracts each of which would be dependent upon the one above it. Patent laws allow the patent owner to enforce its rights against anyone in the distribution chain, subject only to doctrines like exhaustion and license, so there would still be an infringement remedy in the absence of agreements linking patentee to defendant/infringer. In fact, the most market-efficient standard is one that allows appropriate application of governing patent law.

Requiring patent owners to take their *entire* financial reward in the first transaction forces patent owners and licensees into transactions that are less efficient. Thus, the first licensee, subject to issues of contributory infringement or inducement of infringement, will be required to pay a royalty for <u>all</u> uses of the component regardless of whether, in a sub-market, there may be a royalty-bearing need. Instead, allowing direct negotiation between the patent owner and the user of the patented invention, the most important economic actor exploiting the patent, will be more efficient than trying to negotiate with the initial component manufacturer serving as a proxy for the downstream economics. (If transactional costs render sublicenses inefficient, a patentee can always allow rights to exhaust at first sale.)

It is against this framework that a right of patent exploitation, such as licensing, must be considered. There are, therefore, separate yet related concepts that must be analyzed.

II. This Court Should Continue to Protect the Legal Doctrines at Issue

Petitioners conceded in the court below that the patent owner "could have granted Intel only the right to sell Licensed Products to those customers who had obtained a separate license from LGE." Combined Petition for Panel Rehearing and Rehearing en banc of Defendants-Cross-Appellants at 7 (Fed. Cir. Jul. 21, 2006), 2006 WL 2351226. This is consistent with the Fifth Circuit's *Yarn Processing* decision, 541 F.2d at 1135 (discussed *supra* at 20-21).

As a starting point, this Court should reaffirm that position. It is consistent with *Univis.* There the relevant sales, made both by wholesalers to prescription retailers and by finishing retailers to consumers, were authorized sales. The restriction at issue in *Univis*, however, was the requirement that they be done at a mandatory price for a product that only had one use (as even the Government agreed, *see* DOJ-FTC Antitrust IP Licensing Guidelines § 5.2). In contrast, in this case there is no pricing condition or requirement.

Unlike *Univis*, nothing in the agreement at issue in this case in any way restrains competition. Here the accused infringers, Petitioners, are sophisticated manufacturers (OEMs) who are primary users of the patented invention. They are the most direct infringers of the patent at issue. Thus, it is neither unfair nor would it interfere with downstream product distribution, if they were required to separately license any patented invention. It appears that LG's licensing program is limited to principal implementers of the patented area. Its efforts are focused on, for purposes of the patents-in-suit in this case, a potential contributory infringer (Intel) and direct infringers (the OEMs). Intel, in effect, received a covenant not to sue for contributory infringement; its components are now licensed to the extent direct infringers separately obtain a license, but Intel is free from threat of litigation.

For purposes of *Univis*, there appears to be a distinction in language between "unauthorized sales" and "conditional sales." AIPLA submits these distinctions are largely semantic. LG could just as easily achieve the same result by drafting its license to Intel prohibiting sales to unlicensed purchasers as what actually occurred, requiring purchasers to obtain a separate license. And to the extent some suggest that *Univis* should be read to state that LG would have preserved its rights to obtain royalties from Petitioners had its license to Intel been royalty-free, this option should be dismissed as irrational.

On the facts of this case, AIPLA respectfully submits that the issue of exhaustion and implied license should be decided as follows:

A. Pre-License Sales

AIPLA's understanding of the facts, based upon the limited record available, indicates that pre-license sales were released in the Intel-LG License. *See* 248 F. Supp. 2d at 917 (quoted *supra* at 6-7). *If* that is the case, then AIPLA sees this as a complete release and all claimed uses of the components are licensed to LG's patents.

B. Post-License Sales

As noted above, AIPLA is unable to say whether the Intel Notice Letter was sufficient to put purchasers on notice that they required additional licenses. *If* the Notice Letter is deemed sufficient, which is presumed for these purposes, then patent exhaustion should not apply. Petitioners, all sophisticated purchasers, would have had adequate notice that they required additional licenses to use the Intel components and purchased them with that understanding. Moreover, *if* the Notice Letter is deemed sufficient then based upon the circumstances as a whole there would be no reason to imply an equitable license.

CONCLUSION

The Court should decide this case in a manner that preserves the principles that have been developed for each doctrine. Exhaustion does not preclude an infringement action against a purchaser where the sale made clear that downstream licenses are not being granted but rather must be separately negotiated. Thus, when an accused infringer has clear notice before entering into any purchase of potential liability as an infringer, his actions should not be exculpated. The effect of any such restrictions or conditions imposed by the patent owner or its licensees is not violative of the antitrust laws.

Where these notice provisions are met, it should not matter whether the patent owner chose to maximize return by charging the parties at each level of supply an individualized royalty or by requiring a complete royalty payment from the first licensee (thereby exhausting patent rights). Whether the first transaction is a sale or license or covenant not to sue, it should not change these conditions or render a sale unauthorized.

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