Patent Exhaustion in Japan & Impression v. Lexmark

I. Patent Exhaustion in Japan

In July 1997, the Japanese Supreme Court ruled[1] that a patent is considered to be exhausted domestically when a patentee or rights holder transfers the patented invention or product (hereinafter, simply referred to as the "patented product" or the "product") in Japan. This ensures the smooth distribution of the patented product in Japan and does not permit the patentee to obtain a double benefit (one upon transferring or licensing the patented product, and another benefit upon the sale of the patented product by the transferee or the licensee).

However, the situation regarding international patent exhaustion is less clear. The Japanese Supreme Court ruled[2] that a domestic patent right is exhausted for a rights holder in Japan who assigns their patented product to another person outside of Japan, unless the assignee has agreed to not sell or use the product in Japan. While it is understood that by assigning a product to the assignee, the patentee is relinquishing the right to wholly control the product, patentees often wish to retain enforcement of their patent(s) in Japan even if the patented product is assigned elsewhere in the world. If the assignee agrees that Japan is to be excluded as a point of sale or use of the product (and this should be indicated on the product itself or on the packaging and/or manual accompanying the product), a subsequent assignee would be aware of this and would be free to determine whether to purchase the patented product based thereon. This was considered to be limited to assignees which were subsidiaries or companies affiliated with the patentee.

Thus, unless an agreement to not import the patented product into Japan was in place prior to or on the date the assignment of rights was made to the assignee, the patentee is not permitted to exclude the assignee from importing the product into Japan, and the patent is deemed to be exhausted internationally.

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[1] BBS Case. Case No. Heisei, 7(o)1988, Collected Civil Cases vol. 51, sec. 6, p. 2299 (July 1, 1997)

[2] *Id*

The act of refilling the plastic housing of a disposable camera with either film and/or batteries [Konica Camera Case (June 6, 2000, Tokyo District Court, p. 175, No. 1712, Hanrei jihou)] was deemed to be a case in which the patent right was not exhausted. While it was noted that once the original product is available in the market, the assignee has the right to use the product for its intended purpose(s), but the assignee is not granted an unqualified or unlimited license to use and reassign the product as the assignee sees fit. The addition of new film and/or batteries to the disposable camera was deemed to be beyond the scope of activity predicted by the rights holder and thus, the Utility Model and Design Model rights were not exhausted in this case.

In a case similar to the Konica Case, Fujifilm (August 31, 2000 Tokyo District Court) found that the right to use and reassign a product may be transferred to an assignee based on the concept that the function of the product does not change. In this case, the IP right is not exhausted even after the function of the product has ceased (in this case, the camera has run out of film), as the camera is not supposed to be/cannot be properly used after the function has ceased. If a third party was to replace the film (an essential part) and a non-equivalent product is produced, the IP right would also not be exhausted. Extending the lifespan by the replacement of a part that is relatively short-lived relative to the product's anticipated lifespan is within the realm of what constitutes a repair or replacement.

In a case involving a pharmaceutical composition (November 29, 2001 Tokyo High Court, p.89, No.1779, Hanrei Jihou)), the Acyclovir contained in a pharmaceutical composition was extracted, and then formulated as a new pharmaceutical composition containing the extracted, but otherwise unmodified Acyclovir. This case is clearly different from the Fujifilm case, as the function of the product was not depleted, nor was the essential part replaced. The court held that as no manufacturing process resulting in a chemical reaction producing a new form of Acyclovir. The existing product had merely been purified and reconstituted, and no new product was

produced, thus, there was no infringement as the patent right had been exhausted.

In the Brother ink ribbon case, a separate company actively refilled and sold replacement ink ribbons and sold the replacements in boxes that included trademarked logos belonging to Brother, but indicated that the replacement ink ribbons were from the separate company. The Tokyo District Court (HEI-15 (Wa) 29488) and Tokyo High Court[3] ruled that such sale by the separate company of recycled goods derived from Brother products was deemed to be a non-trademark use of the Brother mark. It was deemed that the use of the Brother mark was to let consumers know that the recycled product is compatible with Brother's printers and products.

In 2007, Canon's injunction against Recycle Assist, a third-party importer of Canon's printer ink cartridges, was upheld by the Japanese Supreme Court. The Japanese Supreme Court ruled[4] that Canon's printer ink cartridge was a single-use product, thus, the modification by a third-party constituted the recovery of the initial function of the product and hence, would restore the initial patent claims. While it is a common practice for a company and/or an assignee to attempt to extend the operating life of a purchased or licensed patented product through repairs and installation of new components, a grey-area existed in the law regarding recycling of components for which the original function has ceased due to exhaustion of a critical or essential component.

The remanufactured product (new product) may be different (non-identical) from the original patented product, and numerous criteria such as the properties, state, materials used and content of the product, the modification (and methods to undertake the modification) to the original patented product, etc., should be excogitated in order to determine whether the modified product in question qualifies as a new patented product.

If the patentee had assigned the original patented product

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[3] Tokyo High Court, 13 January 2005, in: IIC 37 (2006) 609 – "Brother Ink Ribbon"

[4] Case No. Heisei 18(jyu)826 (November 8, 2007)

to be sold in a country other than Japan, and the original patented product is modified (including the replacement, refurbishing, etc., of components), it may be deemed to be a novel production of a new product which is non-identical to the original patented product. If it can be deemed that the new product is reused or recycled after the effect as a product has disappeared (functional depletion) or if an essential part (in this case, the ink) is modified, replaced, or in this case, refilled, the patent shall not be deemed as being exhausted and the patentee/rights holder would be permitted to enforce their IP rights should this new product be imported for sale and use in Japan.

In the case of the Canon printer ink cartridge, it was deemed[5] that Recycle Assist had, by refilling ink into the cartridge, allowed for the recovery of the cartridge's function. Therefore, the effect of the patented product was also recovered, and the patent right could be enforced by the patentee. The refilling of ink into the cartridge was deemed to be in excess of the simple replacement of a battery, filter or other short-lived component of the patented product, which would be a reasonable repair or recycling necessary so that the patented product could realize the full lifetime of expected use.

In summary, the Canon case determined that while assignment in Japan will lead to patent exhaustion, in the case where the assignment is made for sale and/or use in another country, it must be considered as to whether the patented product has been modified and/or the essential element(s) have been replaced, thereby resulting in a completely new patented product. Essentially, the act of refilling an ink tank is not considered to be a step of (re)manufacturing, and thus, there is no infringement. However, refilling does constitute replacing or reprocessing of an essential part of the patented product, and thus, there may be infringement.

Whether the action of assignee constitutes (re)manufacturing would be determined based on the function,

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[5] Tokyo High Court, 31 January 2006, in: IIC 37 (2006) 867 "Canon Ink Jet"

purpose, lifespan, and materials used in order to restore the function of the patented product. The patentee can also take steps to limit the scope of what may constitute reasonable recycling (no infringement) through notices, labels, and descriptions on the product website and/or the packaging or in the accompanying manual stating that the patented product is “one use” or “disposable”. The patentee may suggest on the product website and/or the packaging or in the accompanying manual that customers purchase a “new” patented product when the previously purchased patented product reaches the end of its service life.

The issue of patent exhaustion is quite far from being conclusively settled, not only in Japan, but also in other countries. Modern electronic devices (smartphones, etc) are comprised of numerous components often from numerous companies covered by numerous IP rights. These electronic devices and their components are manufactured and then shipped throughout the world, and are often combined with other components to manufacture other electronic devices. It is highly likely that the smartphone being imported for sale, for example, into Japan from China or another manufacturing market contains components originally manufactured in Japan which might, in the new electronic device be non-exhausted. This would force the importer of the electronic device to know the contents, origin, and IP status of all of the components of the device(s) that are being importing for sale, or at the very least require the establishment of extremely complex licensing agreements.

Two topics which are currently being debated with regards to patent exhaustion are summarized below.

1) The patentee/rights owner expects to receive full value of the patented product upon assignment of the patented product. If the value has been received, then the patent should be deemed as being exhausted in regards to the assigned product. However, it has been deemed that replacing and/or reprocessing for reuse after the function has ceased (functionally depleted) constitutes infringement, as a manufacturing step is involved resulting in a non-identical invention or product.

2) What constitutes allowable repairs and what constitutes impermissible (re)manufacturing (infringement)? If the patentee/rights owner explicitly granted permission for the assignee or consumer to conduct activities deemed to be (re)manufacturing, then there is no infringement.

II. Impression Products Inc. v. Lexmark International Inc.

On May 30, 2017, the United States Supreme Court handed down a decision in the Impression Products Inc. v. Lexmark International Inc. case (US. No 15-1189). The Court concluded "…a patentee's decision to sell a product exhausts all of its patent rights in that item, regardless of any restrictions the patentee purports to impose or the location of the sale…Restrictions and location are irrelevant."

According to the ruling, the sale of a product exhausts any and all patent rights originally protecting the product. Even if the patentee attempts to restrict the location where the sale may take place, the sale of the product exhausts the patent rights both domestically and internationally (following *Kirtsaeng v. John Wiley & Sons, Inc.*, 568 U.S. 519).

It was the opinion of Judge Roberts that "…the sale transfers the right to use, sell, or import because those are the rights that come with ownership, and the buyer is free and clear…because there is no exclusionary right left to enforce". Judge Robert's decision seems guided by the fundamental principles of property rights, essentially stating that once a sale is completed and compensation has been obtained by the patentee, the patent right is exhausted and the purchaser is free to do as they wish with the product (following the first sale doctrine).

For Lexmark International Inc., this decision means that the company does not retain patent rights for their printer ink cartridges which were previously sold, even if Lexmark attempted to impose a one-use only restriction or prevent the resale of the product. The original sale of the cartridge exhausts the patent and if Lexmark wishes to retain some rights, that is a contractual or licensing issue between Lexmark and those who purchase their

products. In short, the patent right is exhausted, but a licensing agreement is not exhausted by the sale of a product.

With regards to the importation into the United States of products initially sold abroad, the Court ruled that sale outside the United States exhausts the patent right as the patentee has received payment in order to relinquish the title to the product. In short, the Court (with the sole dissension of Justice Ginsburg) makes no distinction between domestic and international sales.

Implications for International Trade

In third-world nations, American and EU pharmaceutical firms tend to sell their products at lower prices than they do domestically. According to the Lexmark decision, there is no longer a distinction between a domestic and an international sale in terms of patent exhaustion, thus, some pharmaceutical firms see the Lexmark decision as opening up the floodgates for third parties to (re-)import pharmaceuticals manufactured and/or purchased overseas, for example, into the United States at prices far lower than the same pharmaceutical purchased domestically. This may have the effect of limiting the differences in the terms (for example, the cost) at which the same product is sold in different countries.

Implications for Japan

As the Japanese courts have also been grappling with the issue of patent exhaustion, the Impression Products Inc. v. Lexmark International Inc. case and fall-out resulting therefrom may influence future decisions regarding similar cases in Japan.