

Transfer of Indirect Infringing Items and Patent Right “Exhaustion” (and Consideration of Licensing Agreements and Claims to Avoid Patent Exhaustion)

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Synopsis

This article will compare and review the requirements for finding “exhaustion” (or “implied consent”) of patent rights in cases where a patent right holder, etc. transfers indirect infringing items, based on court decisions in Japan and the United States. A summary of the important court precedents that are reviewed here are listed in Section VI of this article. Please refer to it as necessary.

In Section VII of this article, the precedents of lower courts in Japan and the United States are considered and license agreements with conditions to avoid patent right “exhaustion” are also considered. With regard to the conditions of a license agreement, there are conditions that can avoid “exhaustion” and conditions that cannot avoid “exhaustion” in Japan or in the United States. With regard to a claim drafting, in cases where the patent right pertaining to the invention of a product (finished products) is exhausted, the patent right pertaining to the invention of a simple process for using said goods (finished products) may not be exhausted in Japan. This is the difference with the United States.

I. Exhaustion Doctrine in Japan (Two Supreme Court Decisions)

1. Supreme Court Decision in the BBS Case¹ (July 1, 1997)

(1) Transfer in Japan → Exhaustion Doctrine

The Supreme Court Decision in the BBS Case affirmed the exhaustion of the patent right with regard to the invention of a product in Japan on the grounds of: “(i) harmonizing the protection of invention under the Patent Act with the social and public interest; (ii) ensuring the free distribution of goods and the smooth distribution of patented products, thereby protecting the interests of the patent right holders, and achieving the purpose of the Patent Act; and (iii) the fact that it is not necessary to allow patent right holders to acquire dual gain.”

The Supreme Court Decision in the BBS Case held, although it is dicta, that in cases where a patent right holder or its licensee transfers a patented product in Japan, the patent right is exhausted and the act of the transferee or subsequent acquirer to transfer, use, etc. the patented

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product as business shall not infringe the patent right.

(2) Transfer in Japan – Denying exhaustion of the patent right internationally
→ Doctrine of Implied Delegation of the Right

The Supreme Court Decision in the BBS Case indicated that “In cases where a patent right holder transfers a patented product outside Japan... and the patent right holder holds the corresponding patent right in the country where the patented product is transferred,... even if the patent right holder enforces the right based on the patent right of the product pertaining to the corresponding patent right in Japan, this act cannot directly mean that the patent right holder acquired dual gain, based on the fact that the patent right held in Japan and the corresponding patent right are different rights.” Then the Supreme Court held that “[i]n cases where a patent right holder in Japan or a person equivalent thereto transfers a patented product outside Japan, the patent right holder is not allowed to enforce the patent right with respect to the product in Japan against the transferee except in cases where it is agreed with the transferee that Japan is excluded from the destination to which the product is sold or the area where the product is used, and against a third person or the subsequent acquirer who receives the patented product from the transferee excluding cases where the aforementioned agreement is made with the transferee and to that effect is indicated clearly on the patented product.”

The Supreme Court Decision in the BBS Case set forth the grounds thereof as follows: “If a patent right holder transfers a patented product without imposing

conditions to retain the property right, it should be construed that the patent right holder granted the right to dominate the product implicitly to the transferee and subsequent acquirer without restriction of the patent right held by the transferor in Japan.” and others.

As mentioned above, the Supreme Court Decision in the BBS Case adopted the theoretical construction of “implied delegation of the right” in cases of transfer by the patent right holder, etc. outside Japan, which is different from the “exhaustion” of the patent right in cases of transfer in Japan.

Therefore, if a patent right holder agrees with the transferee to exclude Japan from the destinations to which the product is sold or the area where the product is used and retains the property right, the “implied delegation of the right” is denied. The difference between the “exhaustion” and “implied delegation of the right” as indicated by the Supreme Court Decision in the BBS Case has substantive meaning in the sense that the patent right holder can enforce the patent right against the transferee and subsequent acquirer.

(3) The Supreme Court Decision in the BBS Case is a decision for cases where the patent right holder, etc. transfers “direct infringing items.”

On the other hand, whether the doctrine of exhaustion and the implied delegation of the right are also applied in cases where the patent right holder, etc. transfers the indirect infringing items in or outside Japan is a different matter.

In this regard, the Intellectual Property High Court Grand Panel Decision, 2013 (Ne) 10043 (hereinafter referred to as the “Grand Panel Decision in the

iPhone Case”) heard a case where the patent right holder, etc. pertaining to an invention of a product transfers “indirect infringing items” in or outside Japan.

On the other hand, the Intellectual Property High Court Grand Panel Decision, 2005 (Ne) 10021 (hereinafter referred to as the “Grand Panel Decision in the Ink Tank Case”) heard a case where the patent right holder, etc. pertaining to the invention of a process transfers “indirect infringing items” in or outside Japan. The part of the decision of the Grand Panel Decision in the Ink Tank Case related to exhaustion of the patent right pertaining to the invention of a product was reversed by a Supreme Court Decision (2006 (Ju) 826); however, its meaning as a rule of law has not been overturned since the part of the decision related to the invention of a process has not been reviewed by an appeals hearing.

These two decisions of the Grand Panel of the Intellectual Property Court will be reviewed in detail in Sections III and IV below.

2. The Supreme Court Decision on the Ink Tank Case² (November 8, 2007)

(1) The case of the Supreme Court Decision in the BBS Case was a typical one where a patented product transferred by the patent right holder, etc. was directly transferred to a third party.

Conversely, in cases where a patented product is transferred by the patent right holder, etc., then processed or exchanged for its parts, and then transferred again, there is an issue as to whether the act of the transferee, etc. to transfer, or use, etc. the patented product as a business also infringes the patent right, due to the exhaustion or implied

delegation of the right.

The Supreme Court Decision in the Ink Tank Case is a case where a third party who collected patented products (ink tanks) transferred by a patent right holder that were used by consumers and from which ink was consumed, re-filled with ink and sold them again. It is a case where it was disputed whether said act of selling infringed the patent right by exhaustion or implied delegation of the right.

Said Supreme Court Decision quoted the Supreme Court Decision in the BBS Case and held that “The subject for which the enforcement of the patent right is restricted by the exhaustion of the patent right is limited to the patented product itself that the patent right holder, etc. transferred in Japan. If it is found, with regard to a patented product that is transferred by the patent right holder, etc. in Japan, that a patented product which has no identity with the original patented product, is newly manufactured by processing or replacing parts of said patented product, the patent right holder is allowed to enforce the patent right for the newly manufactured patented product.”

In this way, the Supreme Court Decision in the Ink Tank Case showed that in cases where it is found that “a patented product without the identity of the original patented product is newly manufactured, it is not considered as a case of exhaustion of the patent right or implied delegation of the right and the patent right is allowed to be enforced.

The Supreme Court Decision in the Ink Tank Case held as follows after the aforementioned decision: “Whether the case corresponds to a new manufacturing of the patented product should be judged comprehensively in consideration of the

properties of the patented product, the content of the patented invention, conditions of the processing and replacement of parts, actual conditions of the transaction, etc. The function, structure, materials, purpose of use, life, and use conditions of the product shall be considered as the property of the patented product; and the conditions of the patented product when it is processed, content and degree of the processing, life of replaced parts and materials, technical function and economical value of the parts and materials in question in the patented product shall be considered as the conditions of processing and replacement of parts and materials.”

(2) Now, I would like to mention briefly the treatment of exhaustion by court precedents in the United States in cases where, with regard to a patented product transferred by the patent right holder, etc., a product manufactured by processing or replacing parts of said patented product is transferred, etc.

In the case where Bowman, who acquired a license to crop seeds purchased from Monsanto for only one season, planted the harvested seeds for the next season, the U.S. Supreme Court Decision on *Bowman v. Monsanto Co. et al* on May 13, 2013³ allowed the enforcement of the patent right on the following grounds: cited “the authorized sale of a patented article gives the purchaser, or any subsequent owner, a right to use or resell that article. Such a sale, however, does not allow the purchaser to make new copies of the patented invention..

Consequently, to the extent that the doctrine of exhaustion does not extend to newly manufacturing a patented product which has no identity with the (trans-

ferred or licensed) patented products, there is no discrepancy between court holdings in Japan and the United States.

II. Indirect Infringement under the Japanese Patent Act (Article 101 of the Japanese Patent Act)

1. “Invention” includes “invention of a product,” “invention of a process,” and “invention of a process for producing a product” (Article 2 (1) (iii) of the Patent Act).

“Indirect infringement” is stipulated in Article 101 of the Patent Act and roughly categorized into “invention of a product” and “invention of a process” (including invention of a process for manufacturing a product). Each of them is divided into provisions for “exclusive requirements” and “indispensable requirements” respectively.

2. The following acts are stipulated as indirect infringement by Article 101 of the Patent Act.

(1) Indirect infringement of the patent right pertaining to “invention of a product”

(i) “Exclusive” requirements

“where a patent has been granted for an invention of a product, acts of producing, assigning, etc., importing or offering for assignment, etc. any product to be used exclusively for the producing of said product as a business” (Article 101 (i))

(ii) “Indispensable” requirements

“where a patent has been granted for an invention of a product, acts of producing, assigning, etc., importing or offering for assignment, etc. any product (excluding those widely distributed within Japan) to be used for the producing of said prod-

uct and indispensable for the resolution of the problem by said invention as a business, knowing that said invention is a patented invention and said product is used for the working of the invention” (Article 101 (ii))

(2) Indirect infringing of patent right pertaining to “invention of a process”

(i) “Exclusive” requirements

“where a patent has been granted for an invention of a process, acts of producing, assigning, etc., importing or offering for assignment, etc. any product to be used exclusively for the use of said process as a business” (Article 101, (iv))

(ii) “Indispensable” requirements

“where a patent has been granted for an invention of a process, acts of producing, assigning, etc., importing or offering for assignment, etc. any product (excluding those widely distributed within Japan) to be used for the use of said process and indispensable for the resolution of the problem by said invention, knowing that said invention is a patented invention and said product is used for the working of the invention as a business” (Article 101, (v))

3. In cases where a patent right holder, etc. transfers an “indirect infringing item (an item for which the transfer, etc. causes an indirect infringing of a patent right pertaining to the invention of a product or invention of a process),” an issue arises as to whether the patent right pertaining to the invention of a product can be enforced over the transfer, etc. of direct infringing items that are manufactured by using said indirect infringing items or whether the

patent right pertaining to the invention of a process can be enforced over the act of the transferee to use said indirect infringing items.

The “exclusive” requirement (Article 101, (i) and (iv) of the Patent Act) is construed as “said product has no other economical, commercial, or practical use.”⁴

The “indispensable” requirement (Article 101, (ii) and (v) of the Patent Act) is construed as “parts and materials that directly bring about a unique composition characterizing the distinctive technical means which is newly disclosed by the invention as a process in order to resolve a problem of the previous technology.”⁵

Other interpretations of the requirements are omitted because they will depart from the theme of this article.

III. Exhaustion of Patent Right pertaining to Invention of a Product by Transfer of Indirect Infringing Items (Intellectual Property High Court Grand Panel Decision in the iPhone Case)

1. Introduction

The Intellectual Property High Court Grand Panel Decision in the iPhone Case⁶ (May 16, 2014) covers a broad range of issues. In particular, there is a focus on the FRAND defense and the theory of damages. Although it is dicta, the decision is also important in the respect that it shows a general rule for exhaustion of a patent right pertaining to the invention of a product by transfer of indirect infringing items by the patent right holder.

The issues covered by the Intellectual Property High Court Grand Panel

Decision in the iPhone Case are the following, (i) through (vii). In this article, only the decision related to the issue (iv) is reviewed.

The Intellectual Property High Court Grand Panel Decision in the iPhone Case indicated that issue (i) related to the invention of a product and issue (ii) related to the invention of a process “are in a selective relationship and the decision on issue (iii) and after is common to issue (i) and therefore indirect infringement shall not be held.”

However, (as the Intellectual Property High Court Grand Panel Decision in the Ink Tank Case indicated) the invention of a process is different from the invention of a product; namely, the discussion of the exhaustion of the patent right pertaining to the invention of a product does not apply directly to the act of working the invention of a process that is the act of using a process pertaining to a patented invention since it is impossible to imagine a case where a patent right holder transfers the patented product as an act of working the invention and the product, which is the subject matter of the act, is distributed in the market. Therefore, the Intellectual Property High Court Grand Panel Decision in the iPhone Case is not interpreted as judging that the rule indicated in issue (iv) related to the transfer of indirect infringing items related to the invention of a product and the patent right exhaustion applies in entirely the same way to the invention of a process.

<<Issues in the Intellectual Property High Court Grand Panel Decision on iPhone Case>>

(i) Infringement decision on the technical scope of Invention 1 with regard to

each product in this case.

(ii) Decision on indirect infringement (Article 101 (iv) and (v) of the Patent Act) of the patent right pertaining to Invention 2.

(iii) Decision on the restriction on enforcing the patent right pertaining to each invention in this case pursuant to the provisions of Article 104-3 (1) of the Patent Act.

(iv) Existence of exhaustion of the patent right pertaining to each product in this case (transfer of indirect infringing items and doctrine of exhaustion)

(v) Effectiveness of the license agreement of the patent right between Apple and appellant based on the FRAND declaration in question of the appellant.

(vi) Decision on abuse of the right to enforce the right to claim damages based on the patent right by the appellant.

(vii) Amount of damage (with regard to the patent right for which the FRAND declaration is made).

The decision on issue (iii) related to exhaustion is reviewed below.

2. In Cases where a “Patent Right Holder or Exclusive Licensee” pertaining to the Invention of a Product Transfers Indirect Infringing Items

(1) In cases where a patent right holder or exclusive licensee transfers items (meaning items that correspond to Article 101 (i) of the Patent Act if a third party produces, transfers, etc.; hereinafter referred to as “Product (i)”) to be used for production of the patented invention of a product in Japan, the Grand Panel Decision in the iPhone Case held that “The patent right is considered to have

achieved its purpose and is exhausted with regard to Product (i) and the effectiveness of the patent right no longer extends to the use, transfer, etc. of Product (i). It is held that the patent right holder is not allowed to enforce the patent right over Product (i) as long as Product (i) maintains its form without change” and that the patent right shall not be enforced over the act where the transferee transfers the transferred indirect infringing item itself in a form without change, based on the doctrine of exhaustion.

(2) The problem arises with cases where a third party manufactures a patented product using Product (i). In this case, the Grand Panel Decision in the iPhone Case quoted the Supreme Court Decisions in the BBS Case and Ink Tank Case as cited above, held that “However, in cases where a third party manufactures the patented product by using Product (i) subsequently, since an item within the technical scope of the patented invention is newly created by using an item outside the technical scope of the patented invention, it is reasonable to consider that the enforcement of the patent right shall not be restricted over the act of the production in question, and the use, transfer, etc. of the patented product,” and then defined that the patent right is not exhausted in this case.

The Grand Panel Decision in the iPhone Case held that cases of producing the patented product by using Product (i) correspond to cases where “a patented product which has no identity is newly manufactured” as indicated by the Supreme Court Decision in the Ink Tank case, on the grounds that “an item within the technical scope of the patented invention is newly created by using an item

outside the technical scope of the patented invention.” A problem arises when construing this theory formally, as the patent right will not be exhausted even if the Product (i) has almost all compositions of the patented invention, but not minor composition. The consistency with the U.S. Supreme Court Decision in *Quanta Computer, Inc. v. LG Electronics, Inc.* becomes a problem.

The Grand Panel Decision in the iPhone Case held the indirect infringing items set forth in Article 101 (i) of the Patent Act pertaining to the “exclusive” requirement. It is considered that the same discussion applies to the indirect infringing items set forth in Article 101 (ii) of the Patent Act pertaining to “indispensable” requirements. It means that it applies in the same way to cases where a patent right holder or exclusive licensee transfers something indispensable in order to resolve an issue related to the patented invention of a product in Japan (excluding those widely distributed in Japan) (items that correspond to Article 101 (ii) of the Patent Act if a third party manufactures, transfers, etc.; hereinafter referred to as “Product (ii)”⁷.

(3) Subsequently, the Grand Panel Decision in the iPhone Case held, “Even in this case, if it is found that a patent right holder or exclusive licensee consented implicitly to production of the patented product by using Product (i), it is reasonable to judge that the effectiveness of the patent right does not extend to the production of a patented product by using Product (i), and the use, transfer, etc. of the patented product produced.”

In other words, according to the Grand Panel Decision in the iPhone Case, in cases where a patent right holder or

exclusive licensee pertaining to the invention of a product transfers Product (i), the patent right will not be exhausted, but there are cases where implied consent is found. It is practically helpful to review what facts are considered when judging the existence of implied consent, and therefore the part of the decision applying the theory to the case in question is indicated below.

The Grand Panel Decision in the iPhone Case held that the patent right holder (Samsung) did not give implied consent to the production of the patented product. It indicated the following as proactive grounds: "It is difficult to construe that the appellant gave implied consent to all of the wide variety of products that may be produced by using "Goods Subject to Intel License," which were subject to a comprehensive cross-license. In order to manufacture a "device to transmit data" or "data transmission device" by using the base-band chip transferred by Intel, additional parts, including RF chips, power-management chips, antennas, batteries, etc., are necessary. These parts are considered to have an important value technically or economically. There are dozens of differences between the price of the base-band chip and the product in question. The product in question is not included in the 'Goods Subject to Intel License.'" On the other hand, it held as follows as inactive grounds, "Even if it is construed in this way, the enforcement of the patent right is not allowed as long as the base-band chip is distributed without change. Therefore, if it is construed that it is necessary to obtain the approval of the relevant patent right holder when producing the product in question by using the base-band chip, it cannot be considered directly that

distribution of the base-band chip itself is inhibited. Based on the fact that the amended license agreement between the appellant and Intel does not specify the price focusing on the value of individual patent right that is subject to the agreement, it does not allow the appellant to acquire dual gain."

(4) The Grand Panel Decision in the iPhone Case quoted the Supreme Court Decision in the BBS Case and held the transfer by a patent right holder or exclusive licensee outside Japan that "it is construed that this logic applies in the same way to cases where a patent right holder (including a person equivalent to the patent right holder, such as a relevant company) in Japan transfers Product (i) outside Japan." and indicated clearly that there are cases where "implied consent" is found in the case of transfer outside Japan as well as cases of transfer in Japan.

It should be noted here that the burden of proof for the "implied consent" pertaining to the patented invention of a product (finished product) in cases where the patent right holder transfers Product (i) outside Japan is opposite to the Supreme Court Decision in the BBS Case and said "implied consent" is a fact to be proved by the suspected patent infringer.

As mentioned above, the Supreme Court Decision in the BBS Case held in regard to the transfer outside Japan that "It is not allowed to enforce the patent right excluding in cases where it is agreed with the transferee to exclude Japan from the destination to which the product is sold or the area where the product is used" and that the patent right holder shall claim and bear the burden of proving that it is the case where enforcement of the patent is allowed exceptionally. On

the other hand, the Grand Panel Decision in the iPhone Case situated the existence of “implied consent” in the claim that the suspected patent infringer should make and bear the burden of proof.

These differences are considered to be generated because “implied consent” is projected factually in cases where the patent right holder, etc. transfers the patented products, but it is not so in cases of transferring indirect infringing items.

3. In Cases where a “Non-exclusive Licensee” pertaining to the Invention of a Product Transfers Indirect Infringing Items

Regarding whether patent exhaustion is admitted or not, the Grand Panel Decision in the iPhone Case held that the case where a non-exclusive licensee transfers Product (i) in or outside Japan and the case where the patent holder or exclusive licensee transfers are the same. To this extent, it is not necessary to review by distinguishing the person who transfers Product (i), whether the person is any of a patent right holder, exclusive licensee, or non-exclusive licensee.

With regard to the subject of “implied consent,” the Grand Panel Decision in the iPhone Case held, “The decision on whether it is found that the implied consent is given or not should be reviewed with respect to the patent right holder. However, in cases where a non-exclusive licensee who transfers Product (i), has been granted the authority to approve the subsequent production of the patented product by using Product (i) by a third party, the decision on whether it is found that the implied consent is given or not also requires review with respect to the non-exclusive licensee separately.” In short, in cases where the authority to pro-

vide “implied consent” is granted to a non-exclusive licensee, the non-exclusive licensee becomes a subject of “implied consent.”

IV. “Exhaustion” of the Patent Right pertaining to the Invention of a Process by Transfer of Indirect Infringing Items (Intellectual High Court Grand Panel Decision in the Ink Tank Case⁸)

1. Introduction

(1) As mentioned above, the final appeal against the Grand Panel Decision in the Ink Tank Case was accepted and the part of the decision related to the exhaustion of the patent right pertaining to the invention of a product was overturned by the Supreme Court Decision (2006 (Ju) 826).

However, the part of the decision related to the invention of a process from the Grand Panel Decision in the Ink Tank Case was not examined by the appeal hearing. Therefore, the meaning of that part as a rule of law is still effective.

(2) The Grand Panel Decision in the Ink Tank Case held that it is not allowed to enforce the right based on the patent right in the following cases after indicating the following background: “The discussion of the exhaustion of the patent right pertaining to the invention of a product does not apply directly to the act of working the invention of a process as prescribed in Article 2 (3) (ii) of the Patent Act that is the act of using a process pertaining to a patented invention since it is impossible to imagine a case where a patent right holder transfers the patented product as an act of working the

invention and the product, which is the subject matter of the act, is distributed in the market.”

The Grand Panel Decision in the Ink Tank Case held directly the “invention pertaining to a process of manufacturing a product.” This decision was made based on the facts in the case. The part indicated in 3. below from the decision is considered to apply to a “simple process” in the same way.

In fact, the part in question of the decision started with the background, “With regard to the act of working the invention of a process as prescribed in Article 2 (3) (ii) of the Patent Act, which means an act to use a process pertaining to the patented invention...” It indicated Article 2 (3) (ii) of the Patent Act pertaining to the “simple process,” but not Article 2 (3) (iii) of the Patent Act pertaining to the “invention of a process of manufacturing a product.”

(3) The Japanese Patent Act was amended and Article 101 (iii) and (iv) of the Japanese Patent Act at the day of the Grand Panel Decision in the Ink Tank Case correspond to Article 101 (iv) and (v) of the current Japanese Patent Act respectively. The terms “Product (iv)” and “Product (v)” as used in the following are based on the current Patent Act.

2. In Cases where a Product Manufactured by the Invention of a Process of Manufacturing a Product is also a Subject of Invention of a Product

First, the Grand Panel Decision in the Ink Tank Case held as follows: “In cases where a product manufactured by a process pertaining to the invention of a process of manufacturing a product is

also a subject of invention of a product and when the invention of a process of manufacturing a product does not include a different technical concept from the invention of a product, which means when the content of the practical technology is the same and the same invention is indicated simply as the invention of a product and the invention of a process of manufacturing a product on the statement of the scope of the patent claim and specification, if the patent right pertaining to the invention of a product is exhausted, it is reasonable to construe that it is not allowed to enforce the right based on the patent right pertaining to the invention of a process of manufacturing a product. Therefore, in order to manufacture patented products by using the invention of a process of manufacturing a product, in cases of using used products that were manufactured by said patented invention, if the patent right pertaining to the invention of the product is exhausted, the patent holder is not allowed to enforce the right based on the patent right pertaining to the invention of a process of manufacturing a product.”

3. Transfer of Indirect Infringing Items and Exhaustion of Patent Right pertaining to the Invention of a Process

(1) Subsequently, the Grand Panel Decision in the Ink Tank Case held, “In cases where a patent right holder or a licensee who is authorized by the patent right holder transfers an item that is used only for the use of a process pertaining to the patented invention or used for the use of the process (excluding items that are widely and generally distributed in Japan) and that is indispensable to solve a problem with the invention, the patent right

holder is not allowed to enforce the right to demand an injunction, etc. based on the patent right over the act that the transferee or subsequent acquirer uses the process pertaining to the invention of a process by using the item and the act that the transferee or subsequent acquirer uses, transfers, etc. the item produced by the process pertaining to the patented invention by using the item.”

In other words, this decision means that in cases where “a patent right holder, exclusive licensee, or non-exclusive licensee” transfers a product that corresponds to Article 101 (iv) of the Patent Act (Product (iv)) or a product that corresponds to Article 101 (v) of the Patent Act (Product (v)) if a third party manufactures, transfers, etc. with regard to the patented invention of the process, the patent right pertaining to the invention of a process cannot be enforced.

The Grand Panel Decision in the Ink Tank Case indicated the grounds as follows: “(i) In this case, a transferee receives these items from the patent holder on the assumption that the transferee can use the process pertaining to the patented invention by using these items, which means manufacturing equipment used only for manufacturing products by the process pertaining to the patented invention and raw materials, etc. indispensable to manufacturing items using the process. The same applies to the subsequent acquirer. If the permission of the patent right holder is required when using the process by using these items, it disturbs the free distribution of goods in the market. (ii) A patent right holder monopolizes the right to transfer these items (see Article 101 of the Patent Act) and therefore the patent right holder can determine the price of transferring these

items including prices for the use of the process pertaining to the patented invention by future transferees or subsequent acquirers. Consequently, the patent right holder’s opportunity to secure compensation for disclosure of the patented invention is guaranteed”

As mentioned above, this part of the decision is made directly in regards to “inventions pertaining to a process of manufacturing a product”; however, the grounds stated here are considered to apply to a “simple process” as well.

There are arguments regarding the aforementioned decision of the Grand Panel Decision in the Ink Tank Case that since parts, etc. related to a very limited portion of the invention of a process are included in Product (iv) that fulfills the “exclusive” requirements and Product (v) that fulfills the “indispensable” requirements, whether it is possible to construe that a patent right holder can acquire enough value pertaining to the invention of a process only by providing said parts. There is a theory that criticizes the decision because it does not allow enforcement of the right uniformly.⁹

(2) The Grand Panel Decision in the Ink Tank Case indicated as follows as a legal theory for “not allowing enforcement of the patent right pertaining to the invention of a process,” “In this case, the patent right holder does not transfer a product manufactured by using the patented invention and it is not allowed to enforce the right based on the patent right regardless of the intention of the patent right holder. It is called ‘exhaustion’ of the patent right, including these cases. Whether it is called ‘implied consent’ is just an issue of expression.”

This concept is in contrast with the Grand Panel Decision in the iPhone Case, which used “exhaustion” and “implied consent” differently intentionally as follows: in cases where a patent right holder or exclusive licensee pertaining to the invention of a product transfers Product (i), the patent right is not exhausted, but there are cases where it is found that “implied consent” is given.

The “implied consent” as used in the Grand Panel Decision in the Ink Tank Case means “it is not allowed to enforce the right based on the patent right regardless of the intention of the patent right holder.” Therefore, it has a legally different meaning from “implied delegation of the right” in cases of transfer outside Japan as indicated by the Supreme Court Decision in the BBS Case and “implied consent” in cases of transfer of Product (i) indicated by the Grand Panel Decision in the iPhone Case based on the assumption that the “implied consent” is overturned by expressing the contrary intention. It is considered to have substantially the same legal meaning as “exhaustion” as indicated in the Supreme Court Decision in the BBS Case and the Grand Panel Decision in the iPhone Case.

V. Transfer of Indirect Infringing Items and Doctrine of Exhaustion in the United States (The U.S. Supreme Court Decision in the Quanta Case¹⁰, 2008)

1. Outline of the U.S. Supreme Court Decision in the Quanta Case

(1) The patent right holder (LG Electronics Inc.) who had a patent of a part, patent of a product (finished product), and patent of a process, licensed these

patents to Intel to manufacture, and sell, etc. parts (microprocessors and chip sets) to a third party.

(2) LG and Intel concluded a master agreement in addition to the patent license agreement.

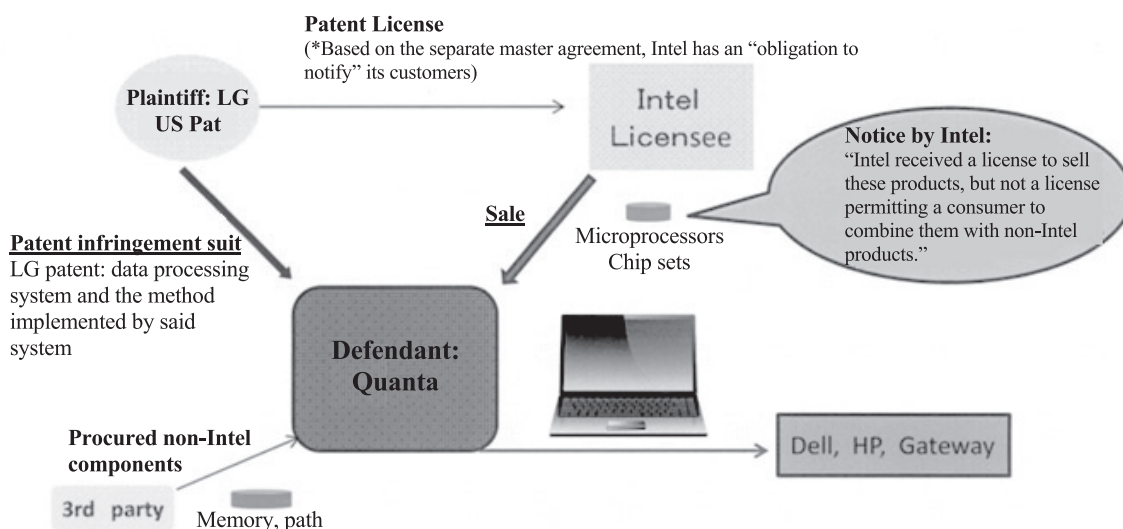
This master agreement imposes on Intel the obligation to give the following written notice to its customers: “Any Intel product that you purchase is licensed by LGE and thus does not infringe any patent held by LGE; the license does not extend, expressly or by implication, to any product that you make by combining an Intel product with any non-Intel product.”

This master agreement also provided that “a breach of this Agreement shall have no effect on and shall not be grounds for termination of the Patent License.”

In this case, Quanta who purchased parts (microprocessors and chip sets) from Intel received the notice from Intel.

(3) Quanta sold PCs by combining parts purchased from Intel and non-Intel products. Said PC was within the technical scope of the invention of a patent of a product (finished product) and the use of the PC was within the technical scope of the patented invention of a process.

(4) LG filed a complaint accusing Quanta of patent right infringement pertaining to the invention of a product (finished product) and invention of a process. In response to this, Quanta alleged exhaustion of each patent right.



2. Is the U.S. Patent Right Exhausted by Transactions Outside the U.S.?

(1) This issue was not discussed expressly in the decision of the U.S. Supreme Court Decision in the Quanta Case; however, the decision did not focus on whether the site where Intel sold Quanta the parts (microprocessors and chip sets) was in the U.S. or not, but on whether the act of Intel selling to Quanta corresponds to the transfer (sale) authorized by the patent right holder (LG).

Previously, transfer in the U.S. was the major premise for "exhaustion" in terms of U.S. court practice¹¹; however, after the decision in the Quanta case, some lower courts found the "exhaustion" of the patent right in its decision on the grounds of "authorized transfer outside the U.S." (U.S District Court for the Northern District of California in the Hitachi Case in 2009)¹² and (Fed. Cir. in the Tessera Case in 1997).¹³

On the other hand, after the Quanta Case, there are judgments of other lower courts, that the patent right is not "exhausted" by the "authorized transfer outside the U.S." (U.S District Court for the Eastern District of Kentucky in the

Static Control Case in 2009)¹⁴, (Fed. Cir. in the Fujifilm v. Benum Case in 2010)¹⁵ and (Fed. Cir. in the Ninestar Tech. Case in 2012).¹⁶ Precedents of lower courts are not uniform.

In this regard, the U.S. Supreme Court Decision in the Kirtsaeng v. John Wiley Case¹⁷ held that Section 109 (a) of the U.S. Copyright Law providing "first sale doctrine" applies to legal sales outside the U.S. and admitted the international exhaustion of the copyright. The decision was given based on the grounds that it is impossible to interpret geographical restriction of the site of transfer based on the expression, "lawfully made under this title," of Section 109 (a) of the U.S. Copyright Law and that inconvenience if international exhaustion of the copyright is not admitted.

With regard to exhaustion under the Copyright Law (first sale doctrine) and exhaustion of the patent right, it is necessary to note that exhaustion under the Copyright Law is specified in the articles, while there are no articles providing for exhaustion under the Patent Act; and that it requires a review of whether the aforementioned grounds indicated by the U.S.

Supreme Court Decision in the *Kirtsaeng v. John Wiley Case* applies to the patent right directly. Since it is reasonable to consider them in parallel, it can be used as a reference.

(2) In Japan, as mentioned above, the Supreme Court Decision in the *BBS Case* defined that “exhaustion” is admitted only for transfers in Japan. After this decision, there were no lower court decisions against it.

The Supreme Court Decision in the *BBS Case* admitted “implied delegation of the right” in cases of transfer outside Japan in principle and held that the patent right cannot be enforced over the product in Japan excluding cases where it is clearly indicated that it is agreed with the transferee to exclude Japan from the destinations in which the transferred product or the area where the transferred product is used.

“Implied delegation of the right” as used in the Supreme Court Decision in the *BBS Case* is different from “exhaustion” to the extent that it can be avoided by the agreement between the transferor, who is a patent right holder, and transferee. Therefore, it is difficult to compare it with the court precedents in the U.S.

3. “Patent Right pertaining to Invention of a Process” is also “Exhausted.”

(1) The original decision (CAFC) held that the patent of a process is not exhausted as a category; however, the U.S. Supreme Court Decision in the *Quanta Case* held that the patent right pertaining to the invention of a process is also exhausted, by indicating adverse effects that the original decision is against the precedent of the U.S. Supreme Court Decision,

Univis, 316 U.S.¹⁸, and that it substantially allows avoiding exhaustion of the patent right by filing a process claim instead of an equipment claim or by including part of the process claim.

(2) In Japan, the Grand Panel Decision in the *Ink Tank Case* held that a patent right pertaining to the invention of a process is exhausted in specific cases. It is the same as those in the U.S.

4. Transfer of Indirect Infringing Items and Exhaustions of a “Patent Right pertaining to the Invention of a Product” and “Patent Right pertaining to the Invention of a Process”

(1) Previous U.S. Supreme Court decisions did not distinguish the doctrine of exhaustion between “invention of a product” and “invention of a process.”¹⁹ The same applies to the decision in the *Quanta Case*. (In Japan, the part related to exhaustion of the patent right pertaining to the invention of a product out of the Intellectual Property High Court Grand Panel Decision in the *Ink Tank Case* was overturned on final appeal. Therefore, there is no decision indicating both requirements for exhaustion of a patent right pertaining to “the invention of a product” and “the invention of a process.”)

The case examined by the U.S. Supreme Court Decision in the *Quanta Case* is that a licensee transferred parts (microprocessors and chip sets), but not the patented products pertaining to the invention of a product (finished product). The U.S. Supreme Court indicated the decision of *Univis*, 316 U.S.²⁰ had the value of a precedent and then held that in cases where the components “substan-

tially embodied” the patent right (patent of a product (finished product) and patent of a process), the patent right is exhausted by the sale of parts by the licensee.

Cases where the sale of components “substantially embodied” the patent as used here means “(i) [when the component’s] only reasonable and intended use [is] to practice the patent”; and “(ii) [when the component] embodie[s] essential features of [the] patented invention.”

(2) When comparing the U.S. Supreme Court Decision in the Quanta Case and Japanese court precedents with respect to the transfer of indirect infringing items and exhaustion, it should be as follows.

(i) Exhaustion of the patent right pertaining to the invention of a process

As indicated above, the Grand Panel Decision in the Ink Tank Case in Japan held for the patented invention of a process that in cases where a “patent right holder, exclusive licensee, or non-exclusive licensee” transfers an item which corresponds to Article 101 (iv) of the Patent Act (Product (iv)) or Article 101 (v) of the Patent Act (Product (v)) if a third party manufactures, or transfers, etc. it, it is not allowed to enforce the patent right pertaining to the invention of a process.

As mentioned above, the “exclusive” requirements set forth in Article 101 (iv) of the Japanese Patent Act are interpreted as stating that “the item has no other economical, commercial, or practical use” and the “indispensable” requirements set forth in item (v) of said Article are understood as “parts and materials that directly bring about a unique composition characterizing the distinctive technical means which are newly disclosed by the invention as a process in order to resolve a

problem in the previous technology.”

If so, it is possible to construe that the requirement indicated by the U.S. Supreme Court Decision in the Quanta Case, (i) “[when the component’s] only reasonable and intended use [is] to practice the patent,” corresponds to the “exclusive” requirements set forth in Article 101 (iv) of the Japanese Patent Act, and (ii) “[when the component] embodie[s] essential features of [the] patented invention” corresponds to the “indispensable” requirements set forth in Article 101 (v) of the Japanese Patent Act.

Consequently, with regard to the exhaustion of a patent pertaining to the invention of a process, either of the aforementioned requirements (i) and (ii) is required in Japan and both are required in the U.S.A.; however, it is considered that there are no discrepancies between the requirements themselves.

(ii) Exhaustion of a patent right pertaining to the invention of a product (finished product)

However, with regard to the exhaustion of a patent right pertaining to the invention of a product, it is slightly different between the U.S. Supreme Court Decision in the Quanta Case and the Japanese Grand Panel Decision in the iPhone Case.

As mentioned above, the Japanese Grand Panel Decision in the iPhone Case held that cases where patented products are manufactured by using Product (i), correspond to cases “where a patented product without identity is newly manufactured,” which was indicated by the Supreme Court Decision in the Ink Tank Case, on the grounds that “an item within the technical scope of the patented invention is newly created by using an item

that is outside the technical scope of the patented invention.” If this theory is understood formally, the patent right will not be exhausted even in cases where Product (i) has almost all of the structure of the patented invention, but not a trivial structure. Therefore, in cases of “substantially embodying” the patented invention of a product (finished product), it has formal discrepancies with the U.S. Supreme Court Decision in the Quanta Case, which held that the patent right is exhausted by the sale of parts by the licensee.

The Grand Panel Decision in the iPhone Case, as mentioned above, leaves room for “implied consent” to be admitted with the patent right of a product (finished product) by the transfer of Product (i) (items that use patented products pertaining to the invention of a product (finished product) only for production from commercial and economical perspectives); however, it can be overturned by expressing the contrary intention. In this regard, it is different from the fact that the U.S. Supreme Court Decision in the Quanta Case admitted “exhaustion.”

Just in case, I will examine whether the exception of exhaustion that is the assumption of the discussion, in cases where “a patented product without identity is newly manufactured” as indicated by the Supreme Court Decision in the Ink Tank Case, is practiced in the same way by U.S. courts. The U.S. Supreme Court Decision in the *Bowman v. Monsanto* Case, as mentioned above, held that the exhaustion does not extend to newly “making” the patented product and allows enforcement of the patent right. Said assumption has no discrepancy between Japan and the U.S.

It may be possible to consider that

the case of the Grand Panel Decision in the iPhone Case is not the case of “substantially embodying” the patented invention of a product (finished product). In this case, if said case becomes an issue in the future, Japanese courts may present a new legal theory to admit “exhaustion.”

5. Can “Exhaustion” be Avoided by an Agreement between the Patent Right Holder and Transferee?

The U.S. Supreme Court Decision in the Quanta Case held that the “exhaustion” of the patent right caused by approved sales could not be avoided at least in the case in question.

This issue will be reviewed in Section VII, including a comparison of court holdings with those in Japan.

VI. Classifying Court Precedents in Japan and the U.S. Related to the Transfer of Indirect Infringement and Patent Exhaustion

The court decisions that are reviewed in this article with regard to “exhaustion” and “implied consent” relate to patents pertaining to the invention of a product (finished product) and patents pertaining to the invention of a process are classified as follows:

(i) With regard to the “implied delegation of the right” indicated by the Supreme Court Decision in the BBS Case, the patent right holder has the burden of proof that the contrary intention has been expressed. If the patent right holder proves it, the presumption of fact will be overturned.

(ii) With regard to the “implied consent” indicated by the Grand Panel Decision in the iPhone Case, the burden of

proof is imposed on the suspected infringer.

(iv) With regard to the “implied consent” indicated by the Grand Panel Deci-

sion in the Ink Tank Case, it is held that “It is not allowed to enforce the right based on the patent right regardless of the intention of the patent right holder.” It is

| | | Patent pertaining to the invention of a product (finished product) | Patent pertaining to the invention of a process |
|-------|--|--|---|
| (i) | The Supreme Court Decision in the BBS Case (1997) | <p>A patent right holder, etc. transfers a patented product in Japan → “Exhaustion”</p> <p>A patent right holder, etc. transfers a patented product outside Japan → “Implied delegation of the right”</p> <p><<Exception (i): Against transferee>> In cases where it is agreed with a transferee to exclude Japan from the destination to which said product is sold and area where said product is used.</p> <p><<Exception (ii): Against subsequent acquirer>> In cases where the aforementioned fact is agreed with a transferee and the fact is clearly indicated on the patented product.</p> | (Not indicated) |
| (ii) | The Supreme Court Decision in the Ink Tank Case (2007) | <p><<Exception of “Exhaustion” and “Implied Delegation of the Right”>> In cases where it is found that the patented product transferred by a patent right holder, etc. in or outside Japan is processed or for which parts are replaced and thereby a patented product, which is not identical to said patented product, is newly manufactured, the patent right holder is allowed to enforce the patent right over the patented product.</p> | (Not indicated) |
| (iii) | The Intellectual High Court Grand Panel Decision in the iPhone Case (2014) | <p>In cases where a patent right holder, etc. transfers an indirect infringing item in Japan, the transferee transfers said indirect infringing item itself → “Exhaustion”</p> <p>In cases where a transferee manufactures the patented product by using said indirect infringing item, the patent right is not exhausted, but “implied delegation of the right” may exist.</p> | (Not indicated) |
| (iv) | The Intellectual High Court Grand Panel Decision in the Ink Tank Case (2006) | (This was changed by (ii) the Supreme Court Decision in the Ink Tank Case.) | <p>- In cases where a patent right holder, etc. transfers an item that corresponds to Article 101 (iv) or (v) of the Patent Act if a third party manufactures or transfers, etc. (Product (iv) and Product (v)), it is not allowed to enforce the patent right pertaining to said invention of a process. (Whether it is called “exhaustion” or “implied delegation of the right” is just an issue of expression.)</p> <p>- “Regardless of the intention of the patent right holder, it is not allowed to enforce the right based on the patent right.”</p> |
| (v) | The U.S. Supreme Court Decision in the Quanta Case (2008) | <p>- It was considered that transfer in the U.S. was the major premise of “exhaustion” by U.S. court precedent holdings; however, the decision in the Quanta Case did not focus on whether the transfer site is in the U.S. or not, but on whether the transfer has been authorized by the patent right holder (After the Quanta Case, lower courts are not uniform).</p> <p>- The patent right pertaining to the invention of a process “is also exhausted.”</p> <p>- The requirement for “exhaustion” of the patent right is not distinguished by invention of a product or invention of a process.</p> <p>- In cases of transfer of an indirect infringing item, if the patent is substantially embodied, the patent right is exhausted by the sale of parts by the licensee.</p> <p>The phrase “substantially embodied” as used here means (i) “[when the component’s] only reasonable and intended use [is] to practice the patent,” and (ii) “[when the component] embodie[s] essential features of [the] patented invention”</p> <p>- The “exhaustion” of the patent right that is caused by the authorized sales was not able to be avoided at least in the case in question. This does not deny the avoidance of “exhaustion” by the conditional license agreement generally.</p> | |

considered to have substantially the same legal meaning as the “exhaustion” indicated by (i) the Supreme Court Decision in the BBS Case and (iii) the Grand Panel Decision in the iPhone Case.

VII. Consideration of License Agreement and Claim Drafting in Order to Avoid “Exhaustion”

1. The U.S. Court Holdings

(1) The U.S. Supreme Court Decision in the Quanta Case did not generally deny the holdings of the CAFC that the patent right “exhaustion” could be avoided by imposing conditions on the license agreement, which has been established after the decision in the Mallinckrodt Case in 1992, but it held that the “exhaustion” cannot be avoided in the case in question. (There is a contrary opinion which construes that the Supreme Court Decision in the Quanta Case generally denied the practice of CAFC on the grounds that it quoted the Supreme Court Decision in the Keeler Case^{21, 22})

In other words, the U.S. Supreme Court Decision in the Quanta Case held that the sale of parts (microprocessors and chip sets) to Quanta by Intel was “authorized sales”; however, this decision is different from the original decision (CAFC) and it stated that the master agreement concluded separately between LG and Intel was independent from the license agreement between LG and Intel, the master agreement was not a condition to restrict the license agreement, and the violations against the master agreement did not establish a violation of the license agreement. Therefore, there is no reason to interpret the decision as generally denying avoidance of “exhaustion” by a

conditional license.

(2) In fact, looking at CAFC decisions after the U.S. Supreme Court Decision in the Quanta Case, the CAFC Decision on April 8, 2009²³ is a case where exhaustion is admitted on the grounds of non-assertion commitment. The non-assertion provision in said case is unambiguous, “...not to bring any demand, claim, lawsuit, or action against Mark IV for future infringement,” and the decision ruled that it admitted all acts that would essentially have become patent right infringements (production, use, offer of sales, sales, and export).

The CAFC decision indicated the following as one of the grounds that it would have been possible to limit the non-assertion provisions for “use” or “production,” for example; however, said limitation was not imposed.

According to the CAFC decision after the U.S. Supreme Court Decision in the Quanta Case, CAFC seems to be considering that “exhaustion” can be avoided by a conditional license and it is worthy for patent practitioners to devise a license agreement based on the aforementioned premise.

Said CAFC decision stated, in the case in question, the provisions for retainment, “No express or implied license or future release whatsoever is granted to MARK IV or to any third party...” would not affect the conclusion.

(3) Based on the above, it no longer has meaning for U.S. court holdings that the previous measures allow filing a claim as the invention of a process or concluding non-assertion commitments (commitment not to enforce the right) instead of a license.

However, even today, after the U.S. Supreme Court Decision in the Quanta Case, it may contribute to avoiding “exhaustion,” for example, to impose conditions, such as limiting “use” or “production,” etc., to the content of the license (at least according to the CAFC decision).

Yet it is not clear whether the limitation of frequency of use in order to prevent recycling items is admitted as “conditions” to avoid the patent right “exhaustion,” such as “single use only,” which became an issue in the Mallinckrodt Case.

(4) It must be noted that the conditions to limit the content of a license require consistent intentions between the licensor and licensee. (In cases of a sales contract, it is necessary to have consistent intentions between the seller and buyer on the conditions related to the use form, etc. of the item subject to sale and purchase.)

For example, in the Hewlett-Packard Case in 1997, in the case where the conditions can be found for the first time after reading the enclosed notice after opening the outer box, the decision denied the consistence of intentions on the conditions and “exhaustion” cannot be avoided.²⁴ The same applies to the decision in the case of Jazz Photo in 2001.²⁵

In this regard, although it is not a case of patent right infringement, the 7th Circuit Court of Appeals admitted the effectiveness of the shrink-wrap contract in its decision in the ProCD Case in 1996.²⁶ Therefore, it is helpful to conclude an appropriate shrink-wrap contract (a review of which type of shrink-wrap contract is effective is omitted in this paper). As other court precedents that admit the consistency of intentions with conditions and “exhaustion” are avoided

by the shrink-wrap contract, for example, there is the decision in the Lexmark Case by the U.S. District Court of Northern District of California in 2003²⁷ and other decisions.

Of course, the consistency of intentions is admitted also by having a buyer sign the license agreement at the moment of the transaction.²⁸

The U.S. District Court of Northern District of Iowa held that the following method is effective: a patent right holder attaches a bag tag on a bag where the license is indicated when selling seeds of plants and if a buyer receives the seeds, the buyer is deemed to have agreed with the license.²⁹ In this case, it is held that it cannot be used as a plea that the buyer did not read the content of the license display.

2. Japanese Court Holdings

(1) With regard to patent right “exhaustion” in Japan related to the invention of a product, the Supreme Court Decision in the BBS Case did not indicate the possibility of being able to avoid it depending on the existence of agreements between the parties, while, with regard to “implied delegation of the right” by the transfer outside Japan, it indicated that it can be avoided in specific cases and it is possible to enforce the right. As mentioned above, the Supreme Court Decision in the BBS Case uses “exhaustion” and “implied consent” separately by indicating that “exhaustion” cannot be avoided depending on the existence of agreements between the parties, while “implied consent” can be avoided depending on the existence of an agreement between the parties.

The Grand Panel Decision in the iPhone Case cited the Supreme Court

Decision in the BBS Case held with regard to the transfer of Product (i) by the patent right holder that, in cases where the transferee transfers Product (i) to a third party in an unchanged form, the patent right pertaining to the invention of a product will “be exhausted,” and in cases where the transferee manufactures, etc. the patented product by using Product (i), the patent right is not “exhausted” and it is an issue of “implied consent” which can be avoided.

On the other hand, with regard to “exhaustion” related to a patent pertaining to the invention of a process, as mentioned above, the Grand Panel Decision in the Ink Tank Case held that “it is not allowed to enforce a right based on the patent right regardless of the intention of the patent right holder” and that “exhaustion” cannot be avoided depending on the existence of an agreement between the parties.

Therefore, under Japanese court holdings, with regard to both the patent right pertaining to the invention of a product and the patent right pertaining to the invention of a process, it is considered that patent right “exhaustion” due to authorized transfer in Japan cannot be avoided by the agreement³⁰ of the parties and there are no objections from scholars.

The following two measures can be considered: (i) measures to avoid exhaustion by imposing “conditions” on the license agreement and deeming that it is not a “authorized” transfer; and (ii) measures to avoid exhaustion by retaining the property right and deeming that there is no “transfer.” These measures are reviewed below respectively.

(2) As (i) measures to avoid exhaustion by imposing “conditions” on the license

agreement and deeming that it is not a “authorized” transfer, the decision in the seedling pot case³¹ can be used as a reference.

The decision in the seedling pot case held that, “as limitations [of a license], there are limitation by time, limitation by location, and limitation by content. With regard to the limitation by content, the following cases are considered: in cases of limiting to one or more licensing forms, out of production, use, transfer, etc. as provided by Article 2 (3) of the Patent Act; in cases of limiting to only part of the licenses out of multiple claims within the scope of the patent claims; in cases of limiting by field the patents that can be used for products in multiple fields, etc. When a non-exclusive licensee uses the patented invention beyond the limitation scope as a business, it infringes the patent right. On the other hand, even if various provisions are concluded with regard to a supplier of raw materials, product specifications, distribution routes, use of signs, etc. under an actual non-exclusive license agreement, these provisions are not directly related to the act of using the patented invention and they are just imposing conditions associated thereto, and a violation against these provisions is only a default under the agreement.”

The decision in the seedling pot case indicated in regard to the case in question that “the issue of where the seedling pots are supplied to has no direct relationship with the act of using the invention in question. According to the fact that it is a matter to be determined by the appellee independently of the patent right in question, the prohibition clause does not limit the scope of non-exclusive license, but a different provision. With regard to the violation of the prohibition clause,

there is no question that it is a default under the leasing contract, and unless the leasing contract is terminated on the grounds of violation, etc. of the prohibition clause, it is impossible to find that the appellee uses the invention as a business without justifiable right and therefore it is impossible to say that it infringes the patent right in question.”

As mentioned above, the decision in the seedling pot case indicated that exhaustion can be avoided by saying that it is not a “authorized” transfer depending on the content of the “conditions” imposed on the license agreement. In concrete terms, the “conditions” of limitation by time, limitation by location, and limitation by content (in cases of limiting to one or more of the licensing forms, such as production, use, transfer, etc. as provided by Article 2 (3) of the Patent Act; in cases of limiting to only part of licenses out of multiple claims within the patent claims; in cases of limiting by field the patents that can be used with products in multiple fields, etc.) can avoid the patent right “exhaustion.”

The judgment in the seedling pot case also indicated that even in cases where the prohibition clause imposes just conditions associated with the license agreement and the violation thereof is only a simple default under the agreement, if the license agreement is canceled, it becomes an infringement of the patent right. Therefore, when a patentee cancels a license agreement, even though the effect of cancellation of the license agreement does not take retroactive effect, the patentee can enforce the patent right at least after the cancellation. In this regard, there are no court precedents related to patent right exhaustion at this

moment; however, there is a case where the distribution right exhaustion under the Copyright Act became an issue. It was held that in cases where the transfer agreement is canceled after the copyright work is transferred, the distribution right is not exhausted based on the retroactive effect of the cancellation (in this case, a transferring agreement was canceled, retroactive effect was admitted) and the act of the transferee to transfer the copyright work to a third party infringed the copyright (distribution right).³² In this case, the court did not find intent or negligence of the third party who received the copyright work before terminating the agreement and rejected the claim for damage. (Since there are no provisions related to the presumption of negligence under the Copyright Act, it cannot be considered in parallel with the patent right infringement for which a provision related to the presumption of negligence exists (Article 103 of the Patent Act); however, it can be used as a reference.)

As a similar court precedent, for example, there is the decision in the far-infrared ray radiation bulb case.³³ In this case, the patent right holder (transferor) affirmed that the purpose of the transfer of the heater in question was to develop a dryer and the use of the finished dryer as a product was not authorized. The judgment indicated that even if there was said agreement, the provision of “purpose of use” cannot avoid patent right “exhaustion.” Looking at other lower court precedents, there are no decisions against this decision.

(3) With regard to (ii) measures to avoid exhaustion by the agreement of retaining the property right and therefore deeming

that there is no “transfer.” two decisions in the case of the core of the drug packing machine sheet can be used as references.

The first decision in the case of the core of the drug packing machine sheet³⁴ examined the cases where a utility model right holder of the core of the drug packing machine sheet transfers a product that is manufactured by using the utility model right, the right holder indicated that it is not for sale and that unauthorized use of the product infringes the right. The court (overturned the original decision³⁵ and) did not find the agreement to retain the property right and the utility model right exhausted on the grounds that the collection rate of the core remains at 20 to 30 percent and it is after receiving the product when a buyer recognizes the indication of not-for-sale.

Regarding the second decision in the case of the core of the drug packing machine sheet,³⁶ it is found that “When [the plaintiff, who is the patent right holder], sold the plaintiff’s equipment, the plaintiff explained to the customer that (i) the core of the plaintiff’s product is lent without charge for the period until the packing sheet is finished; (ii) the core will be collected after use; and (iii) it is prohibited to transfer, lend, etc. the core to a third party. The customer expressed the intention of agreement for these three matters”; “the same content as the aforementioned (i) through (iii) are indicated on the circumferential surface of the core of the plaintiff’s product, at the top and side of the outer package, and on the surface of the box to pack the plaintiff’s product”; “the same explanation is indicated on the plaintiff’s website and the catalog to introduce the plaintiff’s equipment”; “the plaintiff is implementing a service to give points if the customer re-

turns the core of the plaintiff’s product and when the total points reach a specified number, the customer can exchange the points for gifts and the explanation is indicated on the advertisement of said service”; and that the collection rate of the core of the plaintiff’s product by the plaintiff was 97% or more. And then the decision held that “it is found that the plaintiff transferred to the customer the packing sheet of the plaintiff’s product; however, it is difficult to find that the core of the plaintiff’s product was also transferred (the plaintiff’s product can be divided into the core and the packing sheet; the plaintiff transferred only the packing sheet rolled on the core; it is reasonable to find that the plaintiff retains the property right to the core and the core is lent for use). Therefore, as the packing sheet from the plaintiff’s product is consumed by the customer, there is no question about the patent right exhaustion for that portion; and, with regard to the core, it has no assumption for patent right exhaustion.” And the decision found infringement of the patent right.

Based on these court precedents, it is interpreted that patent right “exhaustion” can be avoided if there are agreements between the transferor who is the right holder, and the transferee on retaining the property right.

3. Consideration of License Agreement in Order to Avoid Patent Right “Exhaustion” (Based on the court holdings in Japan and the U.S.)

As mentioned above, according to U.S. court precedents, to impose conditions on the content of the license, for example, limiting “use” or “production,” etc., may be contributing to avoiding

patent right “exhaustion.”

According to Japanese court precedents, the “conditions” of limitation by time, limitation by location, and limitation by content (in cases of limiting to one or more licensing forms, such as production, use, transfer, etc. as provided by Article 2 (3) of the Patent Act; in cases of limiting only part of the licenses out of multiple claims within the patent claims; in cases of limiting by field, the patents that can be used with products in multiple field) can avoid patent right exhaustion.

In this way, court holdings in Japan and the U.S. are not far apart to the extent that there are possibilities to avoid patent right “exhaustion” by not imposing conditions associated with the license agreement, such as the company to which the transferred product is delivered, the purpose of use of the product, etc., but conditions to limit the license agreement itself by time, by location, and by content.

It is naturally required that the transferee agrees with said conditions both in Japan and the U.S.; however, the agreement is denied in many cases in particular under the shrink-wrap agreement. Attention must be paid to this point when concluding a license agreement.

According to Japanese court holdings, it is effective to obtain an agreement to retain the property right (agreement for lending use of the subject product) as a measure to avoid patent right “exhaustion.” In this case, it is also important to secure the agreement without fail.

4. Increasing the Possibility of Avoiding “Exhaustion” with a Claim (only in Japan)

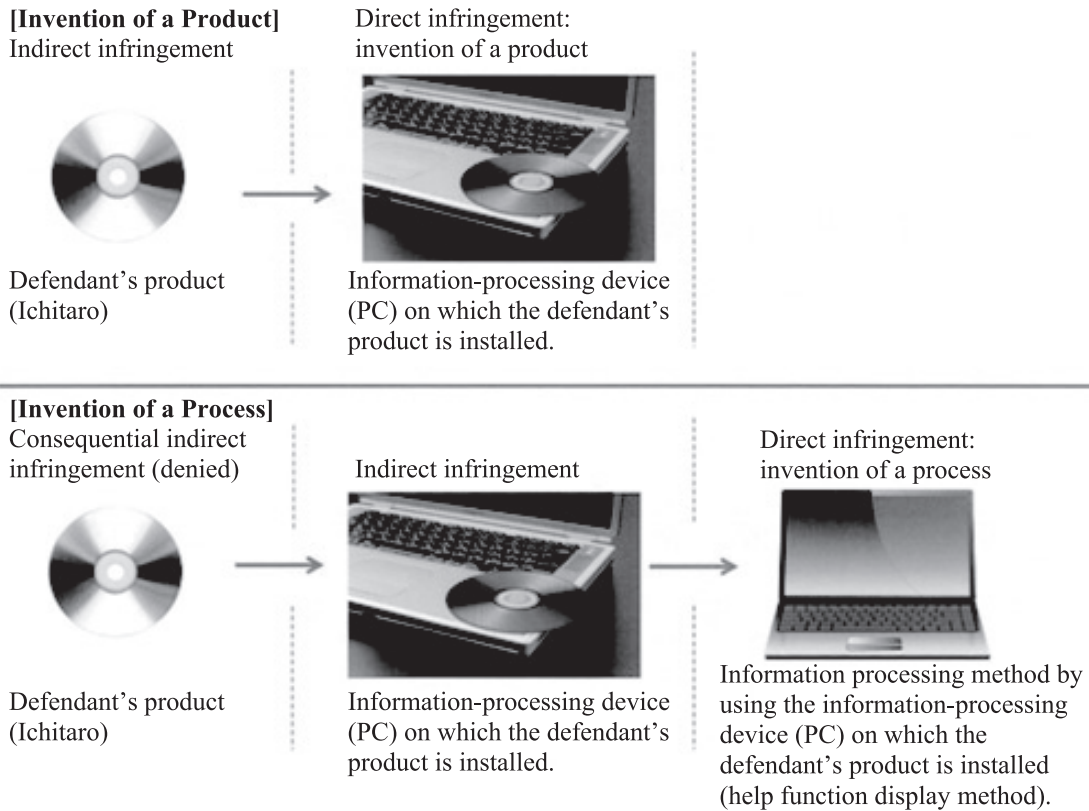
(1) In the previous discussion, I reviewed court precedents in relation to the requirements for patent right exhaustion

with regard to the invention of a product and invention of a process. In further review, there are two types of invention of a process here: (i) invention of a process of manufacturing a product (finished product), and (ii) invention of a simple process for using a product (finished product).

In the case examined by the U.S. Supreme Court Decision in the *Quanta* Case, the invention of a product (finished product) was a PC and the invention of a process was the invention of a simple process for using the PC, which is a product (finished product) (invention of a process (ii)). This decision did not distinguish the requirement for patent right exhaustion by the invention of a product and the invention of a process and held that in cases of “substantially embodying” the patent, the patent right is exhausted by the sale of parts by the licensee. Therefore, according to U.S. court practices, even if the claim is filed as an invention of a simple process for using a product (finished product), it does not contribute to avoiding patent right “exhaustion.”

On the contrary, there is room to consider it in Japanese courtholdings.

(2) In the Intellectual High Court Grand Panel Decision in the *Ichitaro* Case³⁷, with regard to patents pertaining to the invention of a product (finished product), a “PC which displays the help function,” and the invention of a simple process for using a product (finished product), a “display method of the help function,” (invention of a process (ii)), an issue arose on whether the sales, etc. of a CD-ROM (product name: *Ichitaro*) to install the help function correspond to indirect infringement or not.



In conclusion, the decision in the Ichitaro case found that with regard to the act of selling said CD-ROM, indirect infringement occurred of the invention of a product (finished product); however, consequential indirect infringement against the invention of a simple process to use a product (finished product) (invention of a process (ii)) is denied, and then held that indirect infringement did not occur in this case. In other words, in relation with the invention of a product (finished product), the CD-ROM in question is the indirect infringing item. On the other hand, in relation to the invention of a simple process for using a product (finished product), since the PC, a finished product, is the indirect infringing item, the CD-ROM is a “consequential indirect infringing item.” Therefore, “indirect infringement” as specified in the items of Article 101 of the Patent Act does not

include “consequential indirect infringing items.” These relationships can be shown in the figure as follows:

(3) As mentioned above, the Grand Panel Decision in the Ink Tank Case held that in cases where “a patent right holder, exclusive licensee, or a non-exclusive licensee” transfers an item that corresponds to Article 101 (iv) of the Patent Act (Product (iv)) or an item that corresponds to Article 101 (v) of the Patent Act (Product (v)) if a third party manufactures, or transfers, etc. it, it is not allowed to enforce the patent right pertaining to the invention of a process.

Since the invention of a process, which became an issue in the case of the Grand Panel Decision in the Ink Tank Case, was the invention of a process for manufacturing a product (finished product) (invention of a process (i)), it is

considered that the decision established such a rule; however, if the rule is applied formally, even if the “consequential indirect infringing item” is transferred, the patent right pertaining to the invention of a simple process for using a product (finished product) is not exhausted.

When applying the theory to the Ichitaro case, if the patent right holder transfers the CD-ROM, the patent right pertaining to the invention of a product (finished product), a “PC which displays the help function,” is exhausted; however, the invention of a simple process for using a product (finished product), “a display method of the help function,” is not exhausted.

In this case, the claim strategy based on Japanese court holdings, including the decision in the Ichitaro case, is that when filing a claim for an invention of a product (finished product), a claim for an invention of a simple process for using the product (finished product) should be filed too.

If such a case is in litigation, the court may establish a different rule as to the simple process and therefore it is difficult to say that said claim strategy is all-powerful. However, as long as presuming the previous Japanese court precedents, it is worthy to consider.

VIII. Conclusion

As a conclusion to this comparative review of court holdings in Japan and the U.S. with regard to the relationship of the transfer of indirect infringing items and “exhaustion,” various issues are held by multiple court precedents and eventually there are many parts that have no mutual discrepancies despite the different times of decision. Although there are some

formal discrepancies, they are decisions made for the individual case in question and if the same case is in litigation in Japan, it is expected that the court will advocate a new theory to resolve the discrepancies. In this context, it is necessary to watch the accumulation of future court precedents carefully both in Japan and the U.S.

With regard to the review of the proposal of a license agreement to avoid patent right “exhaustion,” the U.S. Supreme Court Decision in the Quanta Case is majorly understood that it denied avoiding patent right “exhaustion” only in the case in question. Therefore, it is helpful to continue studying and review of the conditional license based on the specialty of the agreement in the case and previous U.S. court precedents. With regard to holdings in Japan, court precedents have been accumulated and they have a certain extent of predictability. In this article, I considered the license agreement to avoid patent exhaustion by classifying court holdings in Japan and the U.S. related to patent exhaustion. The study of licensing holdings is never ending. I will continue the study in relation to various issues and report the results at an appropriate opportunity.

(Notes)

- ¹ The Supreme Court Decision on July 1, 1997; *Minshu* vol. 51, No.6, p.2999; 1995 (O) 1998
- ² The Supreme Court Decision on November 8, 2007; *Minshu* vol.61, No.8, p.2989; 2006 (Ju) 826
- ³ The U.S. Supreme Court Judgment on May 13, 2013 *Bowman v. Monsanto Co. et al.*
- ⁴ The Intellectual Property High Court Decision; 2010 (Ne) 10089
- ⁵ The Tokyo District Court Decision; 2002 (Wa) 6035
- ⁶ The Intellectual Property High Court Grand Panel Decision on May 16, 2014; 2013 (Ne)

- 10043
- ⁷ Yoichiro Komatsu, *Jurist* No.1475, p.56
- ⁸ The Intellectual Property High Court Grand Panel Decision on January 31, 2006; *Hanreijihou* No. 1922, p.30: 2005 (Ne) 10021
- ⁹ Hisayoshi Yokoyama, “Tokkyoseihin no Sairiyō to Shojinriron (Re-use of Patented Products and Doctrine of Exhaustion),” *Chizaikanri* vol.56, No.11, p.1675
- ¹⁰ *Quanta Computer, Inc. v. LG Electronics, Inc.*, 533 U.S.
- ¹¹ *Boesch v. Graff*, 133 U.S. 697 (1890); *Jazz Photo Corp. v. Int’l Trade Comm’n*, 264 F.3d 1094, (Fed. Cir. 2001); *FujiPhoto Film Co. v. Jazz Photo Corp.*, 394 F. 3d 1368 (Fed.Cir. 2005); *Fuji Photo Film Co., Ltd., v. International TradeCommission, Jack Benun v. International Trade Commission*, 474 F. 3d 1281 (Fed. Cir. 2007), et al.
- ¹² *LG Electronics Inc. v. Hitachi, Ltd.*, 655 F.Supp.2d 1036 (N.D. Cal. 2009)
- ¹³ *Tessera, Inc. v. ITC* 646 F.3d 1357 (Fed. Cir. 2011)
- ¹⁴ *Static Control Components. Inc. v. Lexmark Internatoinal, Inc.* 615 F.Supp.2d 575 (E.D. Ky. 2009)
- ¹⁵ *Fujifilm Corp. v. Beum*, 605 F.3d 1366 (Fed. Cir. 2010)
- ¹⁶ *Ninestar Tech. Co. v. ITC*, 667 F.3d 1373 (Fed. Cir. 2012)
- ¹⁷ *Kirtsaeng v. John Wiley & Sons, Inc.* 133 S. Ct. 1351 (2013)
- ¹⁸ *Univis*, 316 U.S., *Ethyl Gasoline Corp. v. United States*, 309 U. S. (1940)
- ¹⁹ Haruaki Murao, *NBL* No.887, p.29
- ²⁰ *Univis*, 316 U.S., *Ethyl Gasoline Corp. v. United States*, 309 U. S. (1940)
- ²¹ *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659 (1895)
- ²² Haruaki Murao, *NBL* No.887, p.29
- ²³ *Transcore, LP and TC License, Ltd., v. Electronic Transaction Consultants Corp.*, WL 929033
- ²⁴ *Hewlett-Packard Co. v. Repeat-O-Type Stencil Mfg. Corp.*, 123 F.3d 1445 (Fed. Cir. 1997)
- ²⁵ *Jazz Photo Corp. v. Int’l Trade Comm’n* 264 F.3d 1094 (Fed. Cir. 2001)
- ²⁶ *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996)
- ²⁷ *Ariz. Cartridge*, 290 F. Supp. 2d at 1037
- ²⁸ *Monsant*, 302 F.3d at 1291
- ²⁹ *PioneerHi-Bred Int’l Inc. v. Ottawa Plant Food, Inc.*, 283 F. Supp. 2d 1018 (N.D. Iowa 2003)
- ³⁰ The Tokyo High Court Decision; 2001 (Ne) 959 (Acyclovir case), etc.
- ³¹ The Osaka High Court Decision on May 27, 2003; 2003 (Ne) 320
- ³² The Tokyo District Court Decision on July 11, 2012; 2010 (Wa) 44305, *Hanreijihou* No.2175, No.98; *Hanrei Times* No.1388 p.344
- ³³ The Tokyo District Court Decision on November 30, 2001; 2001 (Wa) 6000
- ³⁴ The Osaka High Court Decision on December 1, 2000; *Hanrei Times* No.1072, p.234
- ³⁵ The Osaka District Court Decision; 1998 (Wa) 11089
- ³⁶ The Osaka District Court Decision on January 16, 2014; 2012 (Wa) 8071
- ³⁷ The Intellectual Property High Court Decision on September 30, 2005; *Hanrei Jihou* No.1904, p.47