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Litigation Alert

LG Electronics, Inc. v. Bizcom Electronics, Inc.

JULY 11, 2006

On July 7, 2006, the Federal Circuit ruled in the case of *LG Electronics, Inc. v. Bizcom Electronics, Inc.*, Civ. 05-1261, that a license agreement that disclaimed an implied license may also establish a conditional sale, thus defeating the application of patent exhaustion.

Facts

LG Electronics, Inc. (“LGE”) owns several patents relating to information management within personal computers and brought infringement suits against a number of defendants in the personal computer industry. Prior to launching suit, LGE had granted Intel a license that covered its entire portfolio of patents on computer systems and components. The license covered Intel’s microprocessors and chipsets. The defendants purchased the microprocessors and chipsets from Intel or its authorized distributors and installed them in computers. The LGE-Intel license expressly disclaimed any implied license to Intel’s customers who combined the microprocessor or chipsets with non-Intel products. The license also required Intel to notify its customers that they were not licensed to combine the Intel products with non-Intel products. The appeal involved Intel customers who each received such notice from Intel.

In its suit, LGE asserted that the combination of Intel manufactured microprocessors or chipsets with other computer components infringed its patents. In response, the defendants argued that LGE’s claims were barred because by licensing the patents in suit, implied licenses were created that covered the accused combinations, and the patent exhaustion doctrine was triggered. On motions for summary judgment, the District Court rejected the defendants’ implied license defense, but concluded that the patent exhaustion doctrine applied to each of the apparatus claims of the patents within the Intel license. LGE appealed the District Court’s resulting grant of summary judgment of noninfringement.

Decision

The Federal Circuit first addressed defendants’ implied license argument. To prevail on an implied license defense, defendants must establish that the products have no noninfringing uses and the circumstances of the sale “plainly indicate” that the grant of a license should be inferred. The Federal Circuit agreed with the District Court’s conclusion that the circumstances of the sale did not warrant the inference of a license in this case. The Federal Circuit found that, regardless of any noninfringing use, no implied license existed because Intel expressly informed defendants’ that its license with LGE did not extend to the combination of an Intel product with a non-Intel product.

The Federal Circuit next turned to the patent exhaustion doctrine. Under this doctrine, an unconditional sale of a patented device exhausts the patentee’s right to control a purchaser’s use of the device. Courts have reasoned that in such a transaction, the patentee has bargained for, and received, an amount equal to the full value of the goods. The exhaustion doctrine, however, does not apply to an expressly conditional sale or license. If a condition is placed on the sale or license, it is more reasonable to infer that the parties negotiated a price that reflects only the value of the ‘use’ rights conferred by the patentee.

Applying this doctrine, the District Court concluded that defendants’ purchase of the microprocessors and chipsets from Intel constituted an unconditional sale. In reaching its conclusion, the District Court noted that LGE was entitled to impose conditions, but failed to do so. The District Court concluded that Intel’s notification letter was not sufficient to transform an unconditional sale into a conditional one, because it did not demonstrate that defendants *agreed* as a condition of sale not to combine the microprocessors and chipsets with non-Intel products. Thus, the District Court found LGE’s patent rights exhausted because defendants’ purchases were in “no way conditioned” on their agreement not to combine the Intel products with other non-Intel parts.

The Federal Circuit disagreed. First, it stated that the LGE license itself constitutes a sale for exhaustion purposes. It created a conditional sale by disclaiming a license to combinations of Intel and non-Intel components and requiring Intel to notify its customers of the limited scope of the license. The Federal Circuit concluded that therefore, LGE's rights in asserting infringement of its system claims were not exhausted.

Impact

This decision establishes that a patent holder can avoid the application of both the implied license and the patent exhaustion doctrines to its apparatus claims by placing appropriate restrictions in the scope of the licenses it grants and requiring downstream notice by the licensee of those restrictions.

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