

# Germany: Revised Draft Law to Introduce Much Awaited Proportionality Requirement for Patent Injunctions

*September 15, 2020*

On September 1, 2020, the German Federal Ministry of Justice and Consumer Protection (“BMJV”) published a new draft amendment to the Patent Act to simplify and modernize German patent law. Among other things, it substantially improves amendments to German law on injunctive relief for patent infringements, introducing a proportionality criterion. The development is particularly important in light of the emerging debate on patent protection for standards for 5G and Internet of Things, affecting manufacturers EU-wide. Deadline for comment is September 23, 2020.

While questions remain, the current draft proposal is promising as it materially improves a previous draft, and offers the prospect of compensation for patentees in cases where an injunction is denied on the basis of a proportionality defense, while mitigating the risk of hold-up by patent holders. Car manufacturers, for example, are increasingly under pressure and face claims for injunctions on small components which, if granted, could cause a production shutdown for entire automobiles and thus threaten great losses. They are therefore vulnerable to attempts at extorting excessive license fees.

Germany is a particularly attractive jurisdiction for this approach. The right to an injunction under German patent law is currently not subject to requirements other than a patent infringement (validity being reviewed in a separate court); in particular, there is no proportionality threshold that would prevent at least the most extreme cases. While German courts have recognized that such a proportionality requirement is inherent to German law and does not have to be written out to be acknowledged, they have so far been very reluctant to apply it, in spite of the requirement to do so under the EU IP Enforcement Directive. The new draft amendment now contains an explicit proportionality requirement for patent injunctions.

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## 1. Current legal framework

Under German law, a patent right is regarded as an absolute right, i.e., a right that allows its holder to exclude any third party from using the patented invention. The right to an injunction pursuant to Section 139(1) German Patent Act therefore requires nothing more than a finding of use without permission. It has accordingly become known as a “quasi-automatic injunction” – validity is not assessed sine that is the competence of the Munich Patent Court. This holds true even if the claim for injunction is based on a single patent infringement for a negligible product component of a complex product, and if the injunction will have disproportionate effect on the infringer. Producers of complex products, such as car or mobile phone manufacturers, are a popular target for patent holders – the prospect of a production standstill can force a manufacturer to pay even unreasonable royalties.

German patent law has repeatedly been criticized for not having introduced a proportionality requirement for the patent injunction claim. EU law in fact demands such requirement: Article 3 and 10 of the Enforcement Directive<sup>1</sup> require measures following a patent infringement to be proportionate.<sup>2</sup> Article 3 (2) of the Enforcement Directive requires that “remedies shall be fair and equitable”, as well as “proportionate.”

However, the German legislator and the courts have so far taken the position that the characteristics of German law render an explicit proportionality requirement superfluous – the proportionality principle is an inherent element of German law and has to be observed by the courts in any event, whether written out or not. The concept of proportionality as stated in Article 19(4) and Article 14(2) of the German constitution is an expression of a principle that also extends to civil and patent law.

However, the German Federal Court of Justice (“FCJ”) has taken a rather conservative approach. In a landmark 2016 ruling, it held that even a grace period (i.e., time for the implementer to use up or sell existing products) in patent infringement cases can only be considered if the immediate enforcement of the patentee’s right to injunctive relief would constitute a disproportionate hardship for the infringer. Such hardship would need to be so severe as to be unjustified by the nature of the patent as an exclusive right, to such an extent that imposition of an injunction would be contrary to good faith.<sup>3</sup> In the case before it, the FCJ denied the requested grace period. This led observers to conclude that the proportionality criterion was irrelevant in practice.

The BMJV draft provides a much-needed clarification on these issues while implementing the Enforcement Directive.

## 2. Reform efforts of the BMJV

The first draft bill for amending the German Patent Act, published on January 14, 2020<sup>4</sup>, contained a stipulation that injunctive relief can be denied on the grounds of proportionality, but only in case of “special circumstances” and “unjustified hardship” for the infringer. Third-party rights were not considered.

After industry voiced criticism<sup>5</sup> that these restrictions would undermine the new proportionality criterion, the BMJV rephrased its proposal for Section 139 of the German Patent Act as follows:

*“The claim is excluded to the extent, due to the special circumstances of the individual case, enforcement would lead to disproportionate disadvantages for the infringer or third parties that are not justified by the exclusive right. In this case, the injured party can demand compensation in money if this appears appropriate. The claim for damages according to paragraph 2 remains unaffected.”*

<sup>1</sup> Directive 2004/48/EC of April 29, 2004 on the enforcement of intellectual property rights (OJ L 157, 30.4.2004).

<sup>2</sup> While the German legislator failed to meet the deadline of April 29, 2006 to implement the principle of proportionality, it is conceivable that Article 3 of the Enforcement Directive is precise enough to have direct effect and thus be applied by German courts.

<sup>3</sup> FCJ, judgment of May 10, 2016 – X ZR 114/13 (*Heat Exchanger*). See also, for example, Regional Court of Munich, judgment of June 13, 2019 – 7 O 10261/18.

<sup>4</sup> Available at [https://www.bmju.de/SharedDocs/Gesetzgebungsverfahren/Dokumente/DiskE\\_2\\_Pat-MoG.pdf?blob=publicationFile&v=1](https://www.bmju.de/SharedDocs/Gesetzgebungsverfahren/Dokumente/DiskE_2_Pat-MoG.pdf?blob=publicationFile&v=1).

<sup>5</sup> See, for example, [submissions by industry leaders](#) following the BMJV’s first draft law.

The BMJV refrains from listing criteria to determine “disproportionate disadvantages” that would warrant an exclusion of the injunction claim. However, in the accompanying materials to the draft bill, the BMJV does provide a non-exhaustive list of criteria that courts may consider when assessing the circumstances of the case.<sup>6</sup>

**a. Interests of the patent holder**

In the context of proportionality, it can be relevant whether the patent holder is active on the same market as the infringer, or is a non-practicing entity (“NPE”). In the past, some NPEs have created a business model out of purchasing patents for components in order to monetize them through license agreements, pressuring infringers into accepting excessive licensing terms to avoid an injunction. Since they were themselves not active on the market, they did not have to fear counterclaims. While the BMJV stresses that it shall not *per se* be held against the patent holder if it is an NPE<sup>7</sup>, it clarifies that the interest of a non-practicing entity may be more in monetizing its IP and less in securing its own production and market position, and might therefore carry less weight than the interests of a practicing entity.

**b. Economic effects of the injunction**

Granting a grace period to the infringer may be warranted under special circumstances. According to the BMJV, special circumstances exist where the economic consequences of immediate enforcement of the injunction would negatively impact and disadvantage the infringer in a particularly grave way (*e.g.*, if the infringer has made sizeable investments in product development and production that would be lost).

**c. Significance of the patent for complex products**

The BMJV recognizes that complex products can contain a large number of patent-protected components. The time and resources necessary for the implementers to avoid continued patent infringement (“design around”) may in exceptional cases be out of proportion to the patent holder’s interest in enforcing its injunction claim, especially where the product needs to comply with special regulations.

**d. Subjective elements**

The court may also consider the nature and extent of the infringement. The BMJV deemed relevant especially whether the infringer has taken possible and reasonable precautions to avoid patent infringement (*e.g.*, a “Freedom to Operate Analysis”) or has made adequate efforts to obtain a license. In this context, the patent holder’s conduct can also become relevant: for example, it would be contrary to good faith for a patent holder deliberately to refrain from raising its claim until after the implementer has made considerable investments.

**e. Third-party interests**

German courts have so far not recognized third-party interests as relevant in the context of patent injunctions. Notably, the Regional Court of Düsseldorf refused to grant a grace period to a producer of heart valves, even though the immediate injunction posed a high risk to patients.<sup>8</sup> In the accompanying material to its first draft bill, the BMJV shared the court’s view that a denial of an injunction based on third-party interests was not warranted.<sup>9</sup>

The BMJV has moved away from this stance, mentioning third-party rights in the proposed new wording of Section 139 Patent Act. In the accompanying

heart valve, that hospital personnel had been trained for it, and that re-training would take months. Nevertheless, the court held that, following the criteria set out by the Federal Court of Justice in the *Heat Exchanger* case, a grace period was not warranted, and that general proportionality considerations, third party (patient) interests or the public interest were not to be taken into consideration.

<sup>6</sup> Second draft amendment to the German Patent Act to simplify and modernize German patent law ([https://www.bmjbv.de/SharedDocs/Gesetzgebungsverfahren/DE/Modernisierung\\_Patentrecht\\_2.html](https://www.bmjbv.de/SharedDocs/Gesetzgebungsverfahren/DE/Modernisierung_Patentrecht_2.html)), p. 61-64.

<sup>7</sup> For example, the BMJV points out that the legitimate monetization interests of individual inventors, universities or SMEs deserve to be protected.

<sup>8</sup> Regional Court of Düsseldorf, cases 4a O 137/15 and 4a O 28/19. The defendant had argued that patients had already been prepared for implementation of that particular

<sup>9</sup> First draft amendment to the German Patent Act ([https://www.bmjbv.de/SharedDocs/Gesetzgebungsverfahren/Dokumente/DiskE\\_2\\_PatMoG.pdf?blob=publication-File&v=1](https://www.bmjbv.de/SharedDocs/Gesetzgebungsverfahren/Dokumente/DiskE_2_PatMoG.pdf?blob=publication-File&v=1)), p. 63.

material to the current draft, the BMJV refers, *inter alia*, to the European Commission’s Guidelines on the Enforcement Directive,<sup>10</sup> which require consideration of the constitutional rights of all parties involved as well as third parties that may be affected by injunctive measures.

### 3. Legal consequences of a successful proportionality defense

In the draft, the BMJV deliberately refrains from outlining specific legal consequences for cases in which an injunction is found to be disproportionate. It leaves the decision which measures are proportional in each individual case to the courts. Measures could entail a grace or transition period for the implementer, but also a long-time or permanent denial of the injunction claim. It will depend on what is reasonable in the specific circumstances of the case. At the same time, the court can grant a monetary compensation to the patent holder.

#### a. Grace or transition period

The court may grant the infringing party a reasonable transition period to develop a non-infringing product or a grace period to use up or sell the infringing product. While the BMJV does not rule out an indefinite exclusion of a patent injunction, it does consider this to be possible in only few cases, in which proportionality cannot be achieved by granting a grace period.

#### b. Appropriate compensation

If an injunction is denied, the court can award monetary compensation to the patent holder. This award is meant to compensate the patent holder for not being able to stop the implementer using its patent against its will; in contrast to a damages claim, it does not require fault on the part of the implementer. In a way, the monetary compensation is similar to a royalty; however, the BMJV stresses that the compensation does not entail a license and, therefore, does not legalize the use of the patent. The patent holder is therefore

free to claim damages in addition to the monetary compensation if the implementer acted intentionally or negligently. It is not entirely clear how the “compensation” would be calculated nor how far it would go beyond a damages claim (which under German law is also compensatory by nature, and not punitive).

### 4. Remarks and Outlook

With the current draft, the BMJV has taken a step towards ensuring implementation of the Enforcement Directive in German patent law. The next step is for the Government to confirm the proposal and lay it before Parliament. However, even if the draft is introduced into law without significant changes, it will still be up to the courts to carefully balance the interests of patent holders and implementers.

In that regard, it remains unclear to which extent the German courts will make use of the proportionality requirement. The impact of the amendment may in practice be minor if the courts uphold their stance that proportionality only warrants a limitation of the injunction in highly exceptional cases. While including proportionality in the statute, the BMJV expressly stated that the disproportionality of an injunction should still remain an exception.<sup>11</sup>

The instrument of “adequate compensation” to be paid by the implementer after a successful disproportionality defense may cause additional legal uncertainty. While it is reasonable to assume that courts will apply the methods normally used for royalty calculation to determine “adequate compensation”, the draft proposal does not contain any guidance on this point. It should at least be clear that concepts of deterrence or a punitive nature should not enter into the calculation, because (a) German law does not know punitive damages; and (b) Article 12 of the Enforcement Directive specifically states that a pecuniary compensation in lieu of an injunction shall be “reasonably satisfactory”, but not punitive.<sup>12</sup>

<sup>10</sup> Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee — Guidance on certain aspects of Directive 2004/48/EC of the European Parliament and of the Council on the enforcement of intellectual property rights (COM(2017) 708 final).

<sup>11</sup> Second draft amendment to the German Patent Act to simplify and modernize German patent law

([https://www.bmju.de/SharedDocs/Gesetzgebungsverfahren/DE/Modernisierung\\_Patentrecht\\_2.html](https://www.bmju.de/SharedDocs/Gesetzgebungsverfahren/DE/Modernisierung_Patentrecht_2.html)), p. 35.

<sup>12</sup> This is also confirmed in recital 26 of the Enforcement Directive which states that the Directive’s “aim is not to introduce an obligation to provide for punitive damages but to allow for compensation based on an objective criterion while taking account of the expenses incurred by the rightholder, such as the costs of identification and research.”

Finally, the draft law and the explanatory text do not mention FRAND cases.<sup>13</sup> It will be interesting to see how courts deal with the “compensation” in a FRAND context. If the owner of a standard-essential patent has made a FRAND promise, it is fair to argue that an injunction is disproportionate if the implementer is willing at the time the injunction is up for decision, and that any compensation awarded by the court should not exceed a FRAND rate.

Industry will have until September 23, 2020 to submit their response to the draft bill.

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<sup>13</sup> For more information on FRAND, please see our Alert Memorandum of July 23, 2020 regarding the FCJ’s FRAND Judgment in *Sisvel v. Haier* (<https://client.cleary-gottlieb.com/77/1800/uploads/2020-07-23-german->

[federal-court-of-justice-publishes-frand-judgment-in-sisvel-v.-haier.pdf](https://www.federalcourtofjustice.gov/press-releases/2020/07/23/federal-court-of-justice-publishes-frand-judgment-in-sisvel-v.-haier.pdf)).