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“Damages” – The German Perspective

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Enforcement Directive

- Directive 2004/48/EC of April 29, 2004
- In Germany implemented by September 1, 2008
- Relevant provisions are in particular:
 - Recital (26)
 - Article 3
 - Article 13
- Under German law, many of the requirements set forth in the Directive were in fact implemented by case law prior to formal implementation by amendment of the relevant statutes.
- For that reason, no substantial changes at least in damages law.



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General Principles (1/4)

- damages claim is a tort claim
- damages claim codified in Sec. 139 para. 2 Patent Act
- codification was changed in September 2008 for implementing the requirements set forth by the Enforcement Directive
- primary damage suffered is infringer's interference with patentee's exclusive right to use the invention (as such immaterial damage)
- type and amount of compensation for damages is determined by general damages law in Sec. 249 - 254 Civil Code



General Principles (2/4)

- Sec. 249 Civil Code:

Section 249

Nature and extent of damages

- (1) A person who is liable in damages must restore the position that would exist if the circumstance obliging him to pay damages had not occurred.
- (2) Where damages are payable for injury to a person or damage to a thing, the obligee may demand the required monetary amount in lieu of restoration. When a thing is damaged, the monetary amount required under sentence 1 only includes value-added tax if and to the extent that it is actually incurred.



General Principles (3/4)

- Sec. 249 para. 1 Civil Code means in fact that tortfeasor is obliged to compensate the damage he **caused**.
- Sec. 249 – 254 Civil Code require that the **entire loss** caused is compensated („*Totalreparation*“) but that the claimant is at the same time **not enriched** beyond what he would have had without the infringing act („*Bereicherungsverbot*“).
- Sec. 249 – 254 Civil Code cover two basic types of damages: **actual losses** and **lost profits**.
- primarily, compensation must be made **in kind**
- if that is not possible or not sufficient, compensation must be made by payment of money (Sec. 251 Civil Code)



General Principles (4/4)

- primary damage (interference with patentee's exclusive right) is as such immaterial damage which may have caused further monetary damages, in particular **lost profits**
- nevertheless compensation by payment of money already for that immaterial damage itself, regardless of lost profits, based on **reasonable royalty** or **infringer's profits**
- Three methods for assessing compensation for damages:
 - **lost profits** = further monetary damage caused by interference with patentee's exclusive right („*subjective damages*“)
 - **reasonable royalty** = compensation for the general value of the exclusive right interfered with („*objective damages*“)
 - **infringer's profits** = legal character unclear („*objective damages*“)



Three Methods (1/2)

- applied for all types of intellectual property rights (patents, trademarks, copyrights, designs, etc.)
- all three methods are supposed to assess compensation **for the same damage/loss**, i.e. they are supposed to look at the same damage but merely from different angles
- purpose: easier assessment of damages, help for patentee / no need for patentee to disclose his own costs & profits (required if lost profits are asked), no privileges for infringer
- courts may **estimate** amount of damages (Sec. 287 Code of Civil Procedure), but solid factual basis for estimation required



Three Methods (2/2)

- patentee may **choose** between methods and **change** his favored methods in the course of the proceedings, even on appeal if sufficient factual basis was introduced in time
- choice for one method becomes **binding** if claim is fulfilled or if patentee cannot further appeal the last court decision
- The principles of said three methods may **not be mixed**.
- „Mixing“ also happens if damages caused by some infringing acts (sales from A to B) would be assessed by one method and damages caused by other infringing acts (sales from A to C) would be assessed by a different method → **The entire damages claim must be assessed by the same method**



Lost Profits (1/3)

- In literal accordance with general damages law (Sec. 252 Civil Code)
- Typical cases of lost profits:
 - lost sales
 - price drops
 - missing rise in prices
- Patentee is required to have used the invention by himself or to have granted a license to third parties where the royalty is based on actual revenues
- Requires construction of a hypothetical scenario („*What would patentee have earned but for the infringement?*“)



Lost Profits (2/3)

- Two methods for construction of hypothetical scenario:
 - **„abstract method“:** Which profits could be expected in the typical course of business?
 - **„particular method“:** Which particular deals were lost and which particular losses were caused by such lost deals?
- Burden of proof:
 - Patentee must bring forward and prove facts showing that making of profits could reasonably be expected.
 - Infringer must bring forward and prove facts showing why such expectation would not have materialized.
 - In case of uncertainty, a minimum damage may be estimated by the court (Sec. 287 Code of Civil Procedure)



Lost Profits (3/3)

- Burden of proof (cont'd):
 - Circumstances excluding causation of lost profits must be brought forward and proven by infringer, e.g.
 - Patentee lacks manufacturing capacities for additional products;
 - Patentee has no access to the respective customers / markets;
 - Customers would have purchased third party's product instead (cheaper, better, higher reputation, etc.)
- Profits are calculated only with regard to the protected product. Only costs attributed to the respective piece must be deducted from revenues (similar to infringer's profits).
- Downside for patentee: Required to disclose own costs & profits and offer audit as evidence.



Reasonable Royalty (1/5)

- Royalties based on fictitious license agreement
- „*Minimum damages*“ according to Art. 13 No. 1. (a) ED?
- No evidence required that patentee actually suffered any monetary harm from infringement (insofar „*normative damages*“), i.e. compensation is to be paid for interference with exclusive right as such.
- **General guideline:** Which royalties could patentee have collected if he had tried to sell a license?
 - Assessing the objective market value of the right to use.
 - What would a reasonable licensor have asked and what would a reasonable licensee have offered?



Reasonable Royalty (2/5)

- **General guideline:** Which royalties could patentee have collected if he had tried to sell a license? (cont'd):
 - Typical license rates in the respective field?
 - Typical profit-turnover ratio in the respective market?
 - Previous license agreements for the same patent?

- Assess all factors relevant for the patent's value:
 - Alternative technologies available and affordable?
 - Economic relevance of the patent for the value of product?
 - Relevance of own patents of infringer for value of product?
 - Monopoly market position of patentee?
 - Maximum license fee burden bearable for product, in particular for products using several patents?



Reasonable Royalty (3/5)

- Applicable viewpoint for assessing these factors?
 - Federal Court of Justice, 1st Senate: *ex-ante* point of view
 - **Federal Court of Justice, 10th Senate:** *ex-post* point of view

- Basis to which apply royalty rate:
 - Number of sold products
 - Revenues / turnover
 - If only parts of the product are relevant for the patent's teaching and others are not, the revenues attributed to the infringing components may be used as a basis. If instead the entire revenues are used as a basis, the royalty rate (%) must be reduced accordingly.
 - Lump sum
 - Down payment



Reasonable Royalty (4/5)

- **Adjustment of royalty rates** compared to market prices:
Infringer has certain advantages compared to contractual licensees and should therefore pay some additional fee for such additional advantages (no privileges for infringer):
 - Infringement judgment shows that he actually uses the patent
 - No obligation to pay royalties in case patent is invalid (may turn out later due to bifurcation)
 - Other factors discussed but to a large extent not supported by case law.



Reasonable Royalty (5/5)

- No punitive damages:
 - No higher royalty rates for infringer merely for punitive reasons.
 - Patentee shall not be privileged compared to the situation he would be in but for the infringing acts.
 - **Doubled royalty rate** as no contract for mutual benefit (no sharing of benefits of the invention between licensor and licensee but benefits of the invention reserved for the patentee)?
 - Punitive damages allowed / required by Enforcement Directive?



Infringer's profits (1/4)

- Originally based on the concepts of civil law's „agency without authorization“ (Sec. 677 – 687 Civil Code), later accepted as customary law. Codified in Sec. 139 para. 2 Patent Act since September 2008 (implementation of Enforcement Directive).
- Legal character nevertheless still unclear (Unjust enrichment claim? Fictitious lost profit of patentee?)
- Is allegedly not directed to compensate for the damage actually suffered but rather to make sure that an equitable compensation is provided.
- Infringer must pay his profits **regardless** of whether patentee could have made these profits by himself at all (fictitious lost profit).



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Infringer's profits (2/4)

- Infringer's profits must be assessed based on his actual revenues and costs with regard to the infringing products.
 - Actual revenues generated;
 - Only costs attributable to each single product (costs per piece) **can be deducted** from revenues:
 - Costs for production and materials;
 - Costs for distribution, packaging, transportation;
 - Labor costs as far as work as actually directed to the specific product (labor spent on one specific piece, e.g. labor required for making one piece);
 - Costs for machines and premises to the extent they are actually used for making the product.
 - **Not deductible:**
 - General overhead costs, e.g. administration/management, accounting, product development, overproduction, etc.
 - Generally all costs that are independent of the number of pieces made or sold (burden of proof on infringer).



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Infringer's profits (3/4)

- Not all profits must be returned, but only such **profits that depend on infringement**:
 - Subject to estimation by the court (Sec. 287 Code of Civil Procedure)
 - To what extent is profit „caused“ by infringement? → *What does „causation“ mean in this case?*
 - Causation of customers' decision to buy infringing product instead of other products („*transaction causation*“)
 - Causation of customers' decision to pay more for the infringing product due to additional infringing feature („*price causation*“)?
 - Both?
 - Equity-based attribution of profits? (*To what extent can profits be considered to belong to patentee?*) → **probably yes**
 - Profits made by re-investing profits (e.g. purchase of startup-company that turns out to grow rapidly) are not „caused“ by infringement in terms of this concept and must therefore not be returned.



Infringer's profits (4/4)

- Not all profits must be returned, but only such **profits that depend on infringement**: (cont'd)
 - Other factors can only exclude causation if the invention is of minor relevance for the product and its market success. In that case, large extents of the profits may rather be attributed to the following factors:
 - Advertising efforts by infringer
 - Infringer's marketing and sales organization
 - Infringer's reputation (e.g. strong brand / trademark)
 - Alternative causes do generally **not exclude** causation of profits („*I would have sold as much if I had used a design around.*“)
 - Irrelevant whether patentee would have had the means for making the same revenues (production capacities, distribution and marketing capacities, etc.)



Distribution Chain

- In distribution chains, the patent may be infringed by several infringers on the various steps of distribution.
- Several infringers are not necessarily jointly and severally liable (Sec. 421 Civil Code).
- In such cases, the following applies:
 - Infringer's profits:
 - Each infringer on each step has to return his individual profits.
 - If supplier has to pay damages to purchaser because purchaser was required to pay damages for patent infringement, supplier may deduct said damages from the damages claim directed against him with regard to the same product.
 - Reasonable royalty:
 - Discussion whether royalty rate must be paid only once and then causes quasi-exhaustion for all levels of distribution
 - Lost profits:
 - Can only be claimed once.

Disclosure of Information (1/3)

- All three methods for assessing damages require information from the infringer, at least the following:
 - Lost profits:
 - Number of sold products.
 - Reasonable Royalty:
 - Number of sold products;
 - Amount of revenues generated.
 - Infringer's profits:
 - Number of sold products;
 - Amount of revenues generated;
 - Attributable costs (i.e. deductible costs).

Disclosure of Information (2/3)

- Infringer is therefore required according to Sec. 242 Civil Code to provide all information patentee needs for specifying his damages claim.
- This includes in particular:
 - Amounts of manufactured products and dates of production;
 - Individual supplies indicating amounts of supplied products, date, prices and recipients;
 - Advertising, including details about advertising media, time frames, etc.
 - Production costs indicating all relevant cost factors and the profit resulting from that.



Disclosure of Information (3/3)

- A further claim for information is codified in Sec. 140b Patent Act. However, the purpose of this claim is not to help patentee specify his damages claim, but rather to gather information about the sources/suppliers and the recipients/customers of infringing products in order to identify further potential infringers along the distribution chain.
- Information to be provided according to Sec. 140b Patent Act overlaps to a large extent with the information to be provided according to Sec. 242, 259 Civil Code:
- No specific restrictions for use of information (except plain abuse), so e.g. use of information for proceedings against same infringer in other jurisdictions possible.



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