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Monetary Remedies in Trademark Infringement Litigation

By Stanley P. Stephenson, Litigation Economics LLC (Tampa, Fla., USA), and Gauri Prakash-Canjels, Litigation Economics LLC (Washington, D.C., USA)

Editor's note: This article builds on a prior article, "Proving Damages in Trademark Cases," which appeared in the October 2012 issue of Business Valuation Update.

Remedies in the Lanham Act are used to punish wrongdoers in trademark infringement litigation, but courts applying that law have dealt differently with some key issues, especially monetary remedies. This article outlines some such problems and how the courts have dealt with them. Consider these examples:

- In trademark infringement cases, the plaintiff shall be entitled, subject to the provisions of sections 1111 and 1114 of the Lanham Act, and subject to the principles of equity, to recover: (1) defendant's profits; (2) any damages sustained by the plaintiff; and (3) the costs of the action. In assessing profits, the plaintiff shall be required to prove defendant's sales only; defendant must prove all elements of cost or deduction claimed. 15 U.S.C. § 1117.[1] In addition, a plaintiff may request an injunction, subject to principles of equity, to prevent violation of a registered mark. See 15 U.S. §1116.[2]

- Because actual damages are difficult to prove in trademark cases, the availability of pecuniary relief often equates with the availability of an accounting of the infringer's profits, itself a difficult, complex, and expensive undertaking (see James M. Koelemay Jr., "Monetary Relief for Trademark Infringement Under the Lanham Act," 72 TMR, 1982, p. 458).

- Recovery of monetary damages recently became easier with the 2020 Supreme Court decision in *Romag Fasteners, Inc. v. Fossil, Inc.* In that case, the court ruled that willfulness need not be an "inflexible precondition" for awarding disgorgement of an infringer's profits in a trademark case.[3]

1 The Lanham Act does not define "defendant's profits" or give guidance as to measuring recoverable profits. See Christopher P. Gerardi, Dawn R. Hall, Julie Saitz, "Calculating Infringer's Profits in 'Soft' Intellectual Property Disputes, Trademark, Copyright, and Design Patent Cases," Chapter 22, in Roman L. Weil, Daniel G. Lentz, and Elizabeth A. Evans, *Litigation Services Handbook,* 6th edition, Wiley, 2017, p. 22.2. Also, "Generally Accepted Accounting Principles (GAAP) do not define the term profit or list the costs one should subtract in order to calculate profit." Ibid. p. 22.5.

2 Of these remedies, an injunction has been the main one plaintiffs have used in trademark litigation. The injunction option became more challenging with requirements listed in the Supreme Court's 2006 decision in *eBay v. MercExchange*, a patent case, and less challenging with passage of the Trademark Modernization Act of 2020 (TMA), enacted on Dec. 27, 2020, which codified a presumption of irreparable harm in trademark cases. See *eBay Inc. v. MercExchange, L.L.C.,* 547 U.S. 388 (2006); see also Mark A. Lemley, "Did eBay Irreparably Injure Trademark Law," 92 *Notre Dame L. Rev* 1795 (2017).

3 *Romag Fasteners Inc. v. Fossil Inc. Romag* 18-1233, April 2020, is somewhat consistent with the 7th Circuit having abrogated the scienter requirement for monetary relief. See James M. Koelemay, *A Practical Guild to Monetary Relief in Trademark Infringement Cases*, 85, Trademark Reporter 263 (1995), p. 268. The *Romag* decision was 9-0 and eliminated the split between the courts as to this inflexible precondition. Now willfulness is just another factor courts may consider.

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As these examples imply, it can be a challenge to sort out monetary remedies to trademark infringement. Yet, a broader view of basic remedies provides a context that may be helpful.

Judicial remedies usually fall into one of four main categories:[4]

1. Damages remedies;
2. Restitution remedies;
3. Coercive remedies such as injunctions; or
4. Declarative remedies.

Damages remedy. A damages remedy is compensation to the plaintiff for his or her losses, generally awarded as a lump sum of dollars for past and future harm. Compensation as such can take several forms such as losses in sales, measured at market values, or consequential damages if plaintiff's loss of exclusive use of a trademark leads to subsequent changes in sales, prices, market share, or greater operating expense incurred in special efforts, such as marketing, to retain customers, factors that, alone or combined with related factors, lead to loss of plaintiff's profits.

It is well-established that a jury can award a trademark owner his or her lost sales. In an infringement action, "damages are typically measured by any direct injury which a plaintiff can prove, as well as any lost profits which the plaintiff would have earned but for the infringement." *Lindy Pen Co. v. Bic Pen Corp.*, 982 F.2d 1400, 1407 (9th Cir. 1993), *abrogated on other grounds by SunEarth, Inc. v. Sun Earth Solar Power Co.*, 839 F.3d 1179 (9th Cir. 2016). Because proof of actual damage is often difficult, however, the jury may use disgorgement of the defendant's profits as a *proxy* for lost sales in making a damages award.[5]

4 Dan B. Dobbs and Caprice L. Roberts, *Law of Remedies, Damages-Equity-Restitution*, 3rd edition, West Academic Publishing, 2018, p. 2.

5 William J. Robinson, "Legal and Equitable Profit

Restitution remedies. The term "restitution" means the restoration of something; in litigation, especially trademark litigation, it means preventing *unjust enrichment* by the defendant.[6] While a restitution award may provide compensation to the plaintiff, the restitution purpose is distinct. It is the not the plaintiff's loss but the defendant's gain that is of concern.

> As an example of restitution, assume a plaintiff spends $1,000 to design and register a trademark that the plaintiff does not use. A thief steals the mark and sells it for $2,000. Leaving aside questions about the logo value in use, the defendant's gain is $2,000, so the restitution remedy is $2,000. The damages remedy means payment for the plaintiff of $1,000. However, the damages remedy leaves the thief better off by $1,000, a net gain from wrongdoing.

A district court is empowered to order disgorgement of a defendant's profits as an equitable remedy under 15 U.S.C. § 1117(a) under an unjust enrichment theory. [7]

Other remedies. Many judges refer to the term "damages" to refer to any monetary award, but such an award based on defendant's unjust gain is a restitution remedy versus a monetary award based on a plaintiff's loss. [8] As per coercive remedies such as *injunctions,* a frequent remedy in trademark litigation, especially before *eBay* in 2006, such are beyond the scope of this article. Defendants who disobey an injunction may be fined, jailed, or sanctioned for contempt, all of which are separate from damages or restitution. Similarly, *declarative remedies* are also outside the scope of this article and make no award for damages, restitution, and injunction.

In the remainder of this article, we focus on monetary remedies, especially those dealing with damages to the owner of the trademark, the plaintiff, and to unjust enrichment of the trademark infringer, the defendant.

The subject of our 2012 article, "Proving Damages in Trademark Cases," was damages to the plaintiff.[9] We argued then and now for measurement of possible damages from plaintiff's loss of actual sales, but for added consideration of possible changes in product prices, profit margins, scale of operations (economies of scale), and extraordinary expenses that may be impacted (such as management costs and advertising costs), all of which may be linked to loss of incremental profits for the plaintiff.

Unjust enrichment. Measuring unjust enrichment from trademark infringement, with equity principles, is challenging to courts, especially so when dealing with complex issues such as defendant's overhead, apportionment of infringing and noninfringing products and expenses, use of an incremental approach to measuring defendant gains versus full absorption of operating expenses, defining the infringement period, and other related factors. We review these issues below but begin with an example.

George Roach provides a pertinent example, "the *National Brake* paradox," from a 1926 case in Wisconsin heard by District Judge Geiger.[10]

Disgorgement in a Trademark Case" June 2018, foley.com/en/insights/publications/2018/06/legal-and-equitable-profit-disgorgement-in-a-trade.

6 Ibid. p. 4, citing *Restatement (Third) Restitution and Unjust Enrichment* § 1 (2011) ("A person who is unjustly enriched at the expense of another is subject to liability of restitution.").

7 Robinson, op cit.

8 Ibid, p. 5. Courts lumping these two types of monetary loss together fail to distinguish between the equitable remedy of an accounting of the "defendant's profits" and the legal remedy of an award of the plaintiff's damages. See J. Thomas McCarthy, *McCarthy on Trademarks and Unfair Competition* § 30: 57 (4th edition, 2011).

9 Stanley Stephenson and Gauri Prakash-Canjels, "Proving Damages in Trademark Cases," *Business Valuation Update,* Vol. 18, No. 10, October 2012.

10 George P. Roach, "Counting the Beans: Unjust Enrichment and Defendant's Overhead," *Texas Intellectual Property Journal,* Spring 2008.

As illustrated in the exhibit, imagine an infringer makes two products, X and Y, that generate revenues of $2 million and $1 million, respectively. Product X requires $1.6 million of variable costs and $0.2 million of fixed costs, but infringing product Y can be produced with only $0.9 million in added variable costs and no added fixed costs. If the goal is to remove unjust enrichment by the infringer, what is an appropriate award?

- In the full absorption approach, implied in Column II in the exhibit, one allocates $200,000 in fixed costs to each product, X and Y, and, in so doing, eliminates infringer's profits for producing Y; and

- In the incremental approach, shown by comparing Columns I and III, fixed costs are disregarded and the defendant's incremental profits of $300,000 from wrongly making product Y is reduced by $200,000. However, the infringer is made better off by $100,000.

This result, while hypothetical, nonetheless reflects the split in federal circuits between the two approaches and contrasts the traditional approach to trademark monetary damages with a restitutionary goal of eliminating unjust enrichment by the infringer.

Specifically, the *Third Restatement* favors the full absorption approach in Section 42 and the incremental approach in Section 51. Denial of any advantage from infringing is stated in Section 51:

> By contrast, the defendant will not be allowed to deduct expenses (such as ordinary overhead) that would have been incurred in any event if the result would be that defendant's wrongful activities—by defraying a portion of overhead expenses—yield increased profit from defendant's operations as a whole.[11]

Trademark Infringement and Unjust Enrichment Remedies: An Example

	Col. I	Col. II	Col. III
	Product X But for Y	Product Y Incremental	Products X and Y Actual Case
Revenue	$2,000,000	$1,000,000	$3,000,000
Var. Costs	$1,600,000	$900,000	$2,500,000
Fixed Costs	$200,000		$200,000
Profit	$200,000	$100,000	$300,000

Note: Production of Product Y does not increase infringer's fixed costs of $200,000. Such costs can be reasonably allocated at $100,000 for products X and Y. The infringer's profit after such an allocation is $0 under full absorption approach or $100,000 under the incremental income approach.

Source: National Brake paradox from Judge Geiger in *Christensen v. National Brake & Elec. Co.,* 10 F 2d 856, 971 (E.D. Wis. 1926), cited in George Roach's "Counting the Beans," op cit. 2016.

Goals of monetary relief. James Koelemay observed that federal appellate courts in the 1970s began construing Section 35 (of the Lanham Act) to require monetary relief to serve one of three purposes: *compensation, prevention of unjust enrichment, or deterrence of infringement.*[12] Before this time, courts had interpreted Section 35 as a *compensation* remedy only when parties made and sold *competing goods*. When the law expanded to include noncompeting goods such that an

11 See *Restatement (Third) of Restitution & Unjust Enrichment* § 42 cmt. D (2011) (discussing damages and profits); id. § 51 cmt. E (citing uses of the "incremental change method"). As cited in George Roach, Chapter 26, "Restitution Rollout," in Fannon Dunitz, 2nd edition, *Calculating Economic Damages*, 2016, ftn. 74, p. 694.

12 James M. Koelemay Jr., "A Practical Guild to Monetary Relief in Trademark Infringement Cases," Vol. 185, TMR, 1995.

infringer's profits were but a rough indicator of plaintiff's lost sales, a new rationale was needed, so courts then began to rely on the *restitutionary goal of preventing unjust enrichment*. The 2nd Circuit in 1965 added *deterrence as a third rationale in* Monsanto.[13] In this purpose, an accounting might be ordered even if no actual injury to the plaintiff or unjust enrichment by defendant.

Categories of damages. Aside from reasonable royalties, especially if defendant's profits are small, *traditional damages* include: (1) profits on plaintiff sales diverted to the infringer—if not duplicative; (2) price cuts by plaintiff due to infringer; (3) harm to reputation of plaintiff—difficult to prove; and (4) corrective advertising.

Accounting of recovery. Section 35 of the Lanham Act requires the plaintiff only to prove infringer's sales and for the infringer to provide evidence of expenses incurred in those sales. This second requirement is the most debated. Koelemay adds a degree of clarity to the choices confronting the courts in trademark cases:

1. *The differential cost rule*. Under this rule, only deduct those expenses that the infringer would not have incurred except in the course of making and selling the infringing product. This is a pure incremental rule; fixed costs, such as overhead, are not deducted. This approach also is used to compute plaintiff's lost profits on lost sales.[14] Professor Margolis believes the key opinion in support of an incremental approach is *Taylor v. Meirick*, a copyright case in the 7th Circuit.[15] A later and often cited 7th Circuit case, *Roulo v. Russ Berrie & Co.,* also made clear fixed costs are not deducted from profit calculation.[16]

2. *Direct assistance rule*. The key case for this rule is *Sheldon v. Metro-Goldwyn Pictures,* in which the plaintiff challenged the allowance of overheads on the theory that defendants did not show that the production of the infringing picture increased overhead. In response, Judge Learned Hand wrote what became known as the "*Sheldon* rule": Overhead that does not assist in the production of the infringement should not be credited to the infringer; that which does, should be. It is a question of fact in all cases.[17]

3. *Fully allocated cost rule*. In this rule, all expenses properly allocated to the product under generally accepted accounting principles are allowed. Courts in both the direct assistance rule and the fully allocated rule often permit use of a "sales ratio" to allocated general expenses and overhead, computed as the sales ratio of the infringing product as a percentage of total sales revenue.[18]

Split of federal circuits. Federal circuits that advocate offsetting allocations of attributable fixed costs are mainly the 1st, 2nd, and 9th Circuits.[19] Federal circuits that advocate the incremental cost approach and eschew fixed cost allocations are mainly the 5th, 7th, and 11th Circuits.[20]

13 Id. Ftn. 70. *Monsanto Chemical Co. v. Perfect Fit Products Mfg. Co. Inc*., 349 F2nd 389, 392, 146 USPQ 512 (CA 2 1965), cert denied 383 US 942, 48 USPQ 772 (1966).

14 *BASF Corp. v. Old World Trading Co. Inc.,* 41 F3d 1081, 1092 (CA 7 1994).

15 Judge Richard Posner ruled to disallow credit for defendant's fixed costs. This is a breach of contract case, not a trademark case, but his ruling supports the incremental rule and is consistent with micro economic theory of the firm. 712 F. 2d 1112 (7th Cir. 1983).

16 886 F. 2d. 031, 941 (7th Cir. 1989). Margolis notes *Taylor* and *Roulo* have been cited in 10th Circuit cases as well. Op. cit. p. 1541.

17 *Sheldon I*, 106 F. 2d at 54.

18 Margolis op cit. claims the full absorption rule is justified.

19 *Sammons v. Colonial Press, Inc.* 126 F.2d 341, 348 (1st Cir. 1942); *Hamil Am. Inc. v. GFI, Inc. (Hamil II),* 193 F.3d 92, 106 (2nd Cir. 1999); *Frank Music Corp. v. Metro-Goldwyn-Mayer, Inc*. 772 F. 2d 505, 515 (9th Cir. 1985).

20 *Maltina Corp. v. Cawy Bottling Co*., 613 F 2d 582, 585

Disgorgement as restitution damages. Restitution and unjust enrichment is a distinct body of law. A restitution claim, including disgorgement of defendant's gains from a trademark infringement, is to recapture these gains to offset unjust enrichment by the defendant, not to measure the plaintiff's loss and then compensate for that loss.[21] A plaintiff whose trademark is infringed is, therefore, awarded restitution based on the gains to the infringer in the form of disgorgement of profits from the infringement.

Example. Assume defendant uses a mark that is confusingly like the plaintiff's trademark. Customers may be misled and purchase the defendant's product when they intended to buy the plaintiff's product. When the infringer is at fault to some degree, restitution of his or her profits is permitted.[22] However, the infringer may argue that the infringed mark was only partly responsible for sales of infringing products (and related products). In this instance, apportionment is needed. However, in the traditional damages approach, the burden is on the defender to present evidence of those expenses tied to infringement, whereas, in the law of unjust enrichment, the burden of allocation of production is on the party seeking disgorgement.[23]

"Generally, the unjust enrichment of a conscious wrongdoer … is the net profit attributable to the underlying wrong. The object of restitution is to eliminate profit from wrongdoing while avoiding, so far as possible, the imposition of a penalty. Restitution remedies that pursue this object are often called 'disgorgement or accounting.'"[24]

Compensatory damages and restitution. In a trademark infringement, restitution and compensatory damages may be combined but with two limits. First, if a damages claim is not permitted by itself, then restitution may be claimed by itself but not both. Second, the combination may not produce excess recovery. The issue in *damages law* is the remedy should not provide more than one full compensation. In *restitution and unjust enrichment law,* restitution should not force disgorgement of more than the unjust enrichment. Combined, full recovery should not exceed either full compensation or full disgorgement.[25]

Summary. Monetary remedies in trademark infringement cases are evolving as statutes and case law evolves. Until recently, monetary damages in Lanham Act cases generally called for evidence of likely *confusion, or willfulness, bad faith, or counterfeit.* But, in 2020, the Supreme Court in *Romag Fasteners* said willfulness need not be required for disgorgement of an infringer's profits in a trademark case. So, too, are evolving approaches to measuring monetary remedies to trademark infringement. Traditional damages *a la Lanham Act* focus on plaintiff's losses, especially as noted here by losses in plaintiff's sales, product price declines, or various measures of expenses of the plaintiff and defendant. Another financial remedy is to focus on defendant's gains from the infringement and to argue for disgorgement of any benefits of the wrongdoing. Disgorgement as a proxy for plaintiff's lost sales or from unjust enrichment theory may simplify monetary remedies in trademark infringement litigation. The accompanying sidebar presents a general model for the disgorgement of unjust enrichment.

Stanley P. Stephenson, *Ph.D., economics, has provided economic litigation services in more than 400 cases and is managing principal at*

(5th Cir. 1980); *Taylor v. Meirick*, 712 F.2d 1112, 1120 (7th Cir. 1983); *Abbott Labs. v. Unlimited Beverages Inc.*, 218 F. 3d 1238, 1242 (11th Cir. 2000).

21 Ronal L. Israel and Brian P. O'Neil, "Disgorgement as a Viable Theory of Restitution Damages," *Commercial Damages Reporter*, 2014, Also, Dan B. Dobbs and Caprice L. Roberts, Chapter 4, "Restitution," in *Law of Remedies Damages-Equity-Restitution,* 3rd edition, West Academic, 2018, pp 369-503.

22 Dobbs and Roberts, op cit. p. 444.

23 Ibid., p. 446, citing *Restatement (Third) of Restitution and Unjust Enrichment* § 51 (5)(d) (2011).

24 Ibid., p. 418.

25 Ibid., p. 457.

Litigation Economics LLC, an economic consulting and expert witness firm in Tampa, Fla., with staff expertise in economics, accounting, finance, and statistics (stan@litigationeconomics.com).

***Gauri Prakash-Canjels,** Ph.D., economics, is a managing principal at Litigation Economics LLC and has 20 years of economic consulting experience (gauri@litigationeconomics.com).*

General Model for Disgorgement of Unjust Enrichment

Disgorgement of unjust enrichment of the defendant (infringer) as a general model can be shown as follows:

Revenue but-for the infringement or in the hypothetical world where there is no infringement

(NI) = R_{NI}

And $R_{NI} = P_{NI} * Q_{NI}$, where P_{NI} is the price and Q_{NI} is the quantity sold but-for the infringement or there is no infringement

Profits but-for the infringement = Π_{NI}

$\Pi_{NI} = R_{NI} - F_{NI} - V_{NI}$, where F_{NI} is the fixed cost and V_{NI} is the variable cost (in the but-for the infringement world)

Actual revenue after the infringement is generally higher and represents unjust enrichment. It is denoted by R_A.

$R_A = P_A * Q_A$, where P_A is the actual price and Q_A is the actual quantity

Actual profits after the event = Π_A

$\Pi_A = R_A - F_A - V_A$, where F_A is the actual fixed cost and V_A is the actual variable cost. Unjust gains are thus expressed as:

$\Pi_A - \Pi_{NI} = (R_A - R_{NI}) - (F_A - F_{NI}) - (V_A - V_{NI})$

In trademark infringement cases, the fact and amount of unjust enrichment comes down to how one measures and interprets these expressions.

1. Was there unjust enrichment? That is, is $\Pi_A - \Pi_{NI} \leq 0$? If no profit by infringer, then no unjust gains.
2. If $\Pi_A - \Pi_{NI} > 0$, then what is the amount of incremental gain from sales of infringing products? Is only one defendant product involved or do only some products infringe?
3. If the court prefers an incremental approach, then gains are $\Pi_A - \Pi_{NI} = (R_A - R_{NI}) - (V_A - V_{NI})$.
4. If the court prefers a fully absorbed measure of infringer's profits, then the question becomes: How to allocate a portion of $F_A - F_{NI}$ used for production of an infringing product?