Feature

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Damage limitations

Most litigation is geared towards obtaining an injunction, but damages are often well worth pursuing. The challenge for rights holders is that the requirements for obtaining an award tend to differ in each federal circuit

In trademark infringement cases the focus is often on the granting of an injunction; however, monetary damages are another important aspect of enforcement. This article reviews ground-breaking trademark damages awards in the most active federal circuits in the United States and takes a detailed look at the positions adopted by appellate courts on the prerequisites for damages awards.

Equity, actual confusion and wilfulness

Injunctive and monetary relief for trademark infringement is guided by a multi-step process outlined in the Lanham Act. The first step forwards proving entitlement to either form of relief is a finding of infringement. As described by David S Almeling, "this is generally accomplished by satisfying a multi-factor test that determines whether there is a 'likelihood of confusion' between the plaintiff's mark and the defendant's allegedly infringing mark" ("The Infringement-Plus Equity Model: A Better Way to Award Monetary Relief in Trademark Cases", *Journal of Intellectual Property Law*, Spring 2007). Once infringement is proven, the court may award injunctive relief (15 USC §1116) and/or recovery for violation of rights in the form of monetary relief. The Lanham Act states that "the plaintiff shall be entitled, ... 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" (15 USC §1117).

The phrase 'subject to the principles of equity' is not specifically defined and has been interpreted in various ways in trademark actions. However, courts generally impose one of two requirements before the plaintiff can recover monetary relief:

- The plaintiff must prove actual confusion, meaning that people confused the plaintiff's and defendant's marks; and/or
- The plaintiff must prove wilfulness (ie, that the defendant's infringement was wilful).

The courts are not in agreement as to whether both of these requirements must be proven, as will be discussed in the following sections.

Actual confusion

Courts are divided on whether actual confusion is a requirement for an award of monetary damages. According to the Second Circuit in

George Basch Co v Blue Coral Inc (968 F2d (2d Cir NY 1992)), it was "settled that in order for a Lanham Act plaintiff to receive an award of damages the plaintiff must prove either 'actual consumer confusion or deception resulting from the violation' ... or that the defendant's actions were intentionally deceptive thus giving rise to a rebuttable presumption of consumer confusion". The Eighth Circuit in *Co-Rect Products Inc v Marvy! Advertising Photography Inc* (780 F2d (8th Cir Minn 1985)) echoed this position when it stated that "a showing of actual confusion entitles the owner of the mark to damages, while a showing of a likelihood of confusion entitles the owner to injunctive relief".

In contrast, the Third Circuit maintains that the Lanham Act itself does not require that actual confusion be proven for an award of damages. In *Choice Hotels Int'l Inc v Pennave Assocs* (43 Fed Appx (3d Cir Pa 2002)), the court noted that "use of a mark which is 'likely to cause confusion' is all that is required by 15 USC §1125(a)(1)(A)" to be proven for an award of monetary damages. The Fifth Circuit concurred with the Third Circuit in *Taco Cabana Int'l Inc v Two Pesos Inc* (932 F2d (5th Cir Tex 1991)). In this case, the court stated that it disagreed with the position that a monetary award requires evidence of actual confusion.

Wilfulness

Courts are also divided as to whether wilfulness is a requirement for awarding monetary damages in trademark infringement matters. The Second Circuit has taken a position that wilfulness is a prerequisite for an award of damages. According to the Second Circuit in *Twin Peaks Prods v Publ'ns Int'l Ltd* (996 F2d (2d Cir NY 1993)), the standard set forth for a finding of wilfulness is "simply whether the defendant had knowledge that its conduct represented infringement or perhaps recklessly disregarded the possibility". As for the damages awarded based on a finding of wilfulness, the Second Circuit held in *Blue Coral* that "a closer investigation into the law's historical development strongly supports our present conclusion that, under any theory, a finding of defendant's wilful deceptiveness is a prerequisite for awarding profits".

Both the Third Circuit in *Banjo Buddies Inc v Renosky* (399 F3d (3d Cir Pa 2005)) and the Fifth Circuit in *Quick Techs v Sage Group Plc* (313 F3d (5th Cir Tex 2002)) have adopted a factor-based approach to evaluating whether equity supports disgorging the infringer's profits. The approach involves a consideration of the totality of the circumstances, as opposed to a simple determination as to whether infringement was wilful. The

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Trends in trademark case filings

US district courts have seen a downturn of 10.4% in the number of trademark cases filed between 2003 and 2008. However, the number of trademark cases filed annually over this same period has fluctuated, with more than 3,600 cases filed in both 2005 and 2006 (Figure 1).

In reviewing trademark litigation activity by circuit, it is clear that certain circuits have more trademark litigation activity than others. Between 2003 and 2008 roughly 55% of all cases filed were filed in the Ninth, Second, and Eleventh Circuits. As Figure 2 shows, during this period the Ninth Circuit received 31% of annual filings, while the Second and Eleventh Circuits received 13% and 11% of annual filings, respectively.

A possible explanation for the concentration of trademark cases in these circuits could be the types of business conducted in these circuits and such businesses' increased likelihood of involvement in trademark infringement matters. For example, the Ninth Circuit includes both California and Washington where the film, entertainment, toy, clothing, and IT industries have a strong presence. The Second Circuit includes New York, where the toy and clothing industries are prevalent as well. Meanwhile, the Eleventh Circuit includes Florida, which is a hub for the clothing, entertainment and tourism industries (see illustration on page 23). These industries tend to generate activity in trademark infringement matters due to the critical role their marks play in generating sales.

Figure 1. **Trademark cases filed in the US district courts between 2003 and 2008**

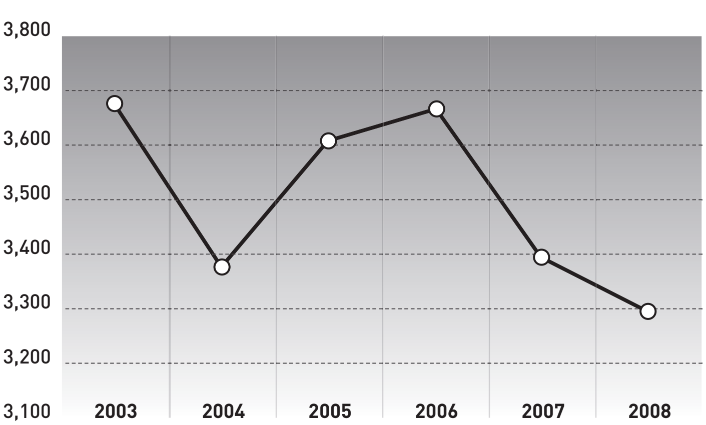
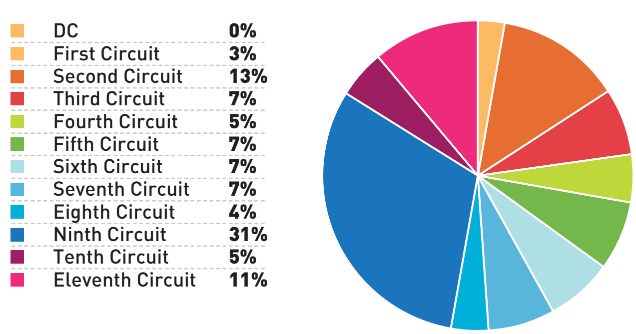
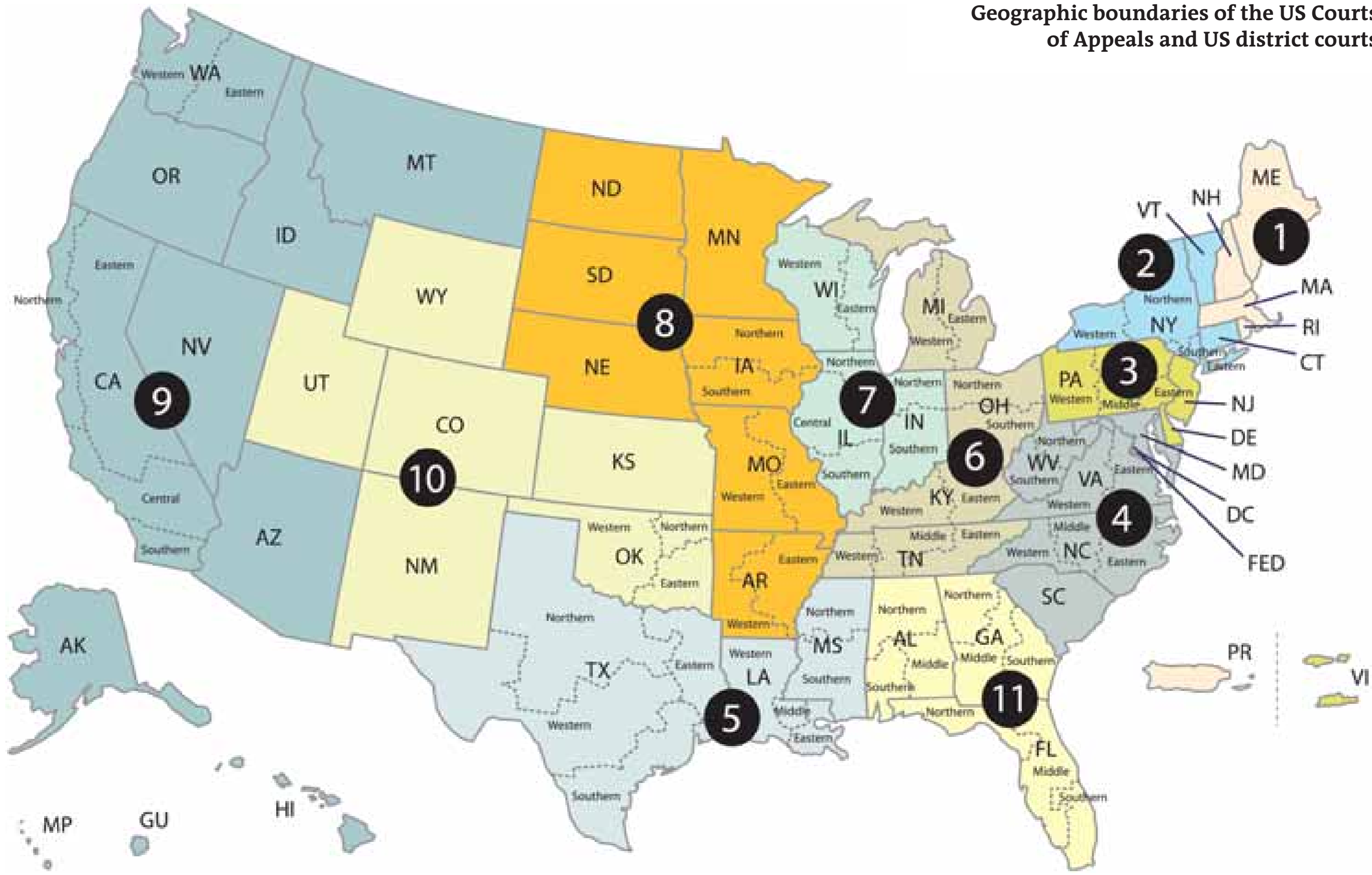


Figure 2. **Trademark cases filed in the US district courts between 2003 and 2008 (average by circuit)**



Source: **LexisNexis CourtLink Nature of Suit Strategic Profile reports for "Property Rights – Trademark"**

Geographic boundaries of the US Courts of Appeals and US district courts



Fifth Circuit in *Quick Techs* declined "to adopt a bright-line rule in which a showing of wilful infringement is a prerequisite to an accounting of profits". Furthermore, the Third Circuit in *Banjo Buddies* summarized the Fifth Circuit's opinion in *Quick Techs*, stating that the "infringer's intent was an important – but not indispensable – factor in evaluating whether equity supports disgorging the infringer's profits". These factors include, but are not limited to:

- whether the defendant had the intent to confuse or deceive;
- whether sales have been diverted;
- the adequacy of other remedies;
- any unreasonable delay by the plaintiff in asserting its rights;
- the public interest in making the misconduct unprofitable; and
- whether it is a case of palming off.

Clearly, 'wilfulness', as defined above by the Fifth Circuit as "whether the defendant had the intent to confuse or deceive", is one factor of several considered in awarding an accounting of the infringer's profits.

The requirement of wilfulness was addressed by the Tenth Circuit in *Western Diversified Servs v Hyundai Motor Am Inc* (427 F3d (10th Cir Utah 2005)). The court referenced *McCarthy on Trademarks and Unfair Competition* §30:62 (4th ed 1998) which stated: "This standard [a requirement of wilfulness] is not universally applied among the circuit courts. While most courts basically agree that an award of profits in the absence of actual damages requires some kind of 'intent' on the defendant's part, the precise articulation of the required state of mind varies from deliberate and knowing to wilful and fraudulent." It should also be noted, as Roberta Jacobs-Meadway stated in "Monetary Recovery in Trademark Cases: Recent Decisions of Interest" (ALI-ABA Audio Seminar, March 11 2009), that "wilfulness remains a significant factor in an award of profits, even if it is not any longer a prerequisite outside the Second Circuit".

Damages awards in the most active circuits

In any given year, over 50% of all trademark infringement actions are filed in the Second, Ninth or Eleventh Circuit. The following is a sampling of trademark cases involving damages in these circuits.

Ninth Circuit

Payless Shoesource Inc and adidas have had a long history of trademark disputes, beginning with a suit adidas filed in New York in 1994 which alleged that Payless wilfully infringed adidas's trademark rights by selling athletic shoes bearing imitations of adidas's three-stripe mark (as referenced in *adidas Am Inc v Payless Shoesource Inc* (546 F Supp 2d (D Or 2008)) see below). This suit was settled in 1994 with Payless agreeing not to sell athletic shoes bearing "three substantially straight parallel stripes on the side of the shoe running diagonally from the outsole forward to the lacing area, or two or four parallel double-serrated stripes of contrasting colour running diagonally from the outsole forward to the lacing area". In agreeing to this settlement, adidas dismissed the action with prejudice and released any claims that it had brought based on Payless's use of "two or four parallel double-serrated stripes" on footwear. Subsequent to the settlement, Payless stopped selling three-striped shoes, as well as shoes with two or four double-serrated stripes, but continued to sell shoes with two or four straight-edged stripes.

In November 2001 adidas filed another action against Payless, this time in Oregon (*adidas Am Inc v Payless Shoesource Inc* (as cited above)). adidas claimed that Payless infringed its trademark and trade dress rights because of its sale of footwear bearing two or four stripes. After a three-week trial, the jury determined that adidas was entitled to a three-pronged damages award, as follows:

- actual damages in the amount of $30.6 million, representing a 7.78% running royalty on Payless's sales of infringing shoes;
- disgorgement of Payless's profits in the amount of $137 million; and
- punitive damages of $137 million.

Payless had argued in its defence that the law required adidas to prove that Payless used two or four stripes on shoes as its own

In November 2001 a jury awarded adidas a three-pronged damages award made up of $30.6 million in actual damages, $137 million in disgorgement of profits and a further $137 million in punitive damages

trademark, rather than as decoration. The court disagreed with this defence, but also disagreed with the disgorgement of profits and punitive damages elements of the jury's damages award.

In considering whether to enter the jury's disgorgement of profits award, the court noted that adidas was very aggressive in calculating Payless's profits and concluded that the profits as calculated by adidas's expert were overstated. As an example, the running royalty of 7.78% of sales awarded as actual damages should have been deducted as one of Payless's direct expenses of selling the shoes. The fact that adidas did not include a royalty in its calculation of Payless's profits was an indication of the unreasonableness of the calculation. In addition, adidas's own damages expert, after testifying that Payless earned $208 million in profits, admitted that a "commonly used measure of profit" would result in a $19 million profit, which was a figure very close to that set forth by Payless's damages expert. Ultimately, the judge determined that the jury's verdict of $137 million relating to disgorgement of Payless's profits was so high that it was punitive rather than compensatory, and instead awarded $19.7 million.

Regarding the jury's award of punitive damages, the court found that a 1:1 ratio between compensatory and punitive damages was too high, mainly because there was no physical harm or disregard for a person's health or safety, there were no lost sales, and adidas suffered no economic harm that jeopardized its business in any way. The court concluded that the punitive damages award must be reduced to $15 million and denied Payless's motion for a new trial, conditioned on adidas accepting a remittitur of the punitive damages award to $15 million (*adidas Am Inc v Payless Shoesource Inc* (D Or, September 12 2008)).

The judge and jury in this matter addressed the issues of wilfulness and actual confusion in their conclusions. Regarding actual confusion, the jury did not specifically offer an opinion or finding (*adidas Am Inc v Payless Shoesource Inc*, Verdict Form dated May 5 2008). However, Judge King did state in *adidas Am Inc v Payless Shoesource Inc* (546 F Supp 2d (D Or 2008)) that "in the Ninth Circuit, neither an intent to confuse, nor actual confusion are required elements of a trademark infringement claim". Additionally, King made it clear in his September 2008 decision in this matter that "In determining whether the accused Payless shoes were likely to cause consumer confusion, the jury was charged with considering not just evidence of actual confusion – that is… likelihood of confusion surveys – but with weighing: (1) the similarity of the marks; (2) the relatedness of the parties' goods; (3) the similarity of trade or marketing channels; (4) the strength of the plaintiff's marks; (5) defendant's intent; (6) evidence of actual confusion; (7) the degree of care exercised by the average purchaser; and (8) the likelihood of expansion into other markets [*AMF v Sleekcraft Boats* (599 F2d 341, 348-49 (9th Cir 1979))]". He further stated that "sufficient evidence supports the jury's finding of likelihood of confusion".

As for wilfulness, the "jury found that Payless acted wilfully and maliciously, or in wanton and reckless disregard of adidas's trademark and trade dress rights". King further stated: "I have also given a great deal of consideration to the jury's finding of wilfulness. I firmly believe that the jury's finding of wilfulness is correct given the evidence before it." Further, the court's opinion noted : "A defendant's profits can only be disgorged to prevent unjust enrichment if the trademark infringement was wilful [*Adray v Adry Mart Inc* (76 F3d 984, 988 (9th Cir 1995))]."

Second Circuit

In *Gucci America Inc v Duty Free Apparel Ltd* (315 F Supp 2d (SDNY 2004)), the court initially determined that the defendant unlawfully sold counterfeit merchandise bearing trademarks of the plaintiff Gucci America Inc. Subsequent to this finding, the court also found that the defendant again sold counterfeit Gucci merchandise in violation of a court-imposed injunction. The court was then left to determine the proper monetary and injunctive remedies.

Gucci elected to receive statutory damages under Section 35(c) of the Lanham Act, for both the contempt and the underlying Lanham

“Circuit courts remain divided as to whether a showing of actual wilfulness and/or confusion is required to obtain an award of monetary damages”

Act violations. According to 15 USC §1117(c), “the plaintiff may elect, at any time before final judgment is rendered by the trial court, to recover, instead of actual damages and profits under Subsection (a) of this section, an award of statutory damages for any such use in connection with the sale, offering for sale, or distribution of goods or services in the amount of – (1) not less than $500 or more than $100,000 per counterfeit mark per type of goods or services sold, offered for sale, or distributed, as the court considers just; or (2) if the court finds that the use of the counterfeit mark was wilful, not more than … [$1 million] per counterfeit mark per type of goods or services sold, offered for sale, or distributed, as the court considers just”. The court then noted as follows “Congress added the statutory damages provision of the Lanham Act in 1995 because ‘counterfeiters’ records are frequently nonexistent, inadequate, or deceptively kept…, making proving actual damages in these cases extremely difficult if not impossible’ [S Rep 104-177, at 10 (1995)].”

In its discussion of the appropriate statutory damages award, the court recognized that its estimate of the defendant’s profits of $720,000 involved a number of assumptions made necessary by the defendant’s poor record-keeping. The court added that “the Second Circuit has held that a counterfeiter who keeps poor records ‘must bear the burden of uncertainty’ in determining a damages award [*Louis Vuitton SA v Spencer Handbags Corp* (765 F2d (2d Cir 1985))]”.

The determination of the statutory damages award was also influenced by the court’s finding of wilfulness. It stated “that over the two-year time period, [the defendant] was, at best, acting with wilful blindness or, at worst, exhibiting bold contempt for the law… Moreover, [the defendant] was also unreasonable in relying, as he asserted, on the absence of litigation by other designers; [the defendant] should have known that a defendant who waits to get sued to determine whether his merchandise is legitimate runs the risk (as has happened here) of losing that lawsuit. Such 'wilful ignorance' would be sufficient to trigger the heightened penalties of the actual damages provisions of the Lanham Act [*International Star Class Yacht Racing Ass'n v Tommy Hilfiger* (80 F3d (2d Cir 1996))]".

The parties had agreed in their joint pre-trial order that a wilful violation of Gucci's rights would give the court discretion to award between $2,000 and $2 million in damages. The court ultimately found that "Gucci would have been automatically entitled to treble damages had it elected actual (versus statutory) damages under Section 35(b) of the Lanham Act" and subsequently awarded the maximum in statutory damages of $2 million as well as approximately $60,000 in fees and costs, for a total award of $2.06 million.

It is interesting to compare the statutory damages awarded to Gucci to the actual damages it would have received if it had not made the election for statutory damages. Under Section 35(b) of the Lanham Act, Gucci would have been automatically entitled to treble damages had it elected for actual, rather than statutory, damages. Based on the court's estimate of $720,000 in defendant's profits discussed above, the trebled actual damages would have equalled $2.16 million, which is roughly equivalent to the statutory damages award. In addition to the monetary damages award, the court also amended its previous injunction so as to enjoin the defendants "from selling any merchandise bearing any trademarks owned by Gucci, unless defendants maintain records demonstrating that that merchandise originated from an authorized Gucci dealer" for two years from purchase.

Eleventh Circuit

In *Nike Inc v Variety Wholesalers Inc* (274 F Supp 2d (SD Ga 2003)) Nike claimed that "Variety [Wholesalers Inc] breached a settlement agreement and violated Nike's trademarks when it sold counterfeit Nike socks, t-shirts and fleece items bearing designs similar to Nike's trademarks". Similar to the *adidas Case* discussed earlier, these parties had previously squared off in trademark infringement disputes. Their first dispute was settled by an agreement dated February 19 2001, in which Variety paid Nike $80,000 and agreed to cease selling counterfeit Nike goods. Then, on November 16 2001, Nike's counsel contacted Variety and asserted that the latter had breached the settlement agreement.

The case at issue was subsequently filed on August 9 2002 and the court found "for Nike on its trademark counterfeiting, trademark infringement, false designation of origin, unfair competition, trademark dilution and breach of contract claims". The court permanently enjoined Variety from selling counterfeit Nike products and awarded Nike a total of just over $1.35 million in damages, which represented Variety's profits on the accused goods. Variety asked the court to deduct various costs and expenses (eg, corporate overhead, occupancy costs, payroll costs, advertising expenses, operating expenses) from its net profit on the accused goods. The court declined to deduct the overhead and occupancy costs "on the grounds that it appears that Variety would have incurred these costs even without selling the accused goods" and further found that "Variety has failed to meet its burden, required by §1117(a), of proving the costs that it contends should be deducted from its profits on the accused goods".

Nike had also asked the court to award it statutory damages as an alternative form of relief. The court found that Nike was entitled to $900,000 in statutory damages, which represented $100,000 in damages for each of nine uses by Variety of the Nike logo and the Swoosh design on different items of clothing. In its order, the court gave Nike 10 days to elect either statutory damages or the award of profits. If Nike did not make an election, the court would award Nike the $1.3 million in actual damages.

Regarding actual confusion, the court in *Nike* stated the following: "In determining whether there is a likelihood of confusion, the court may consider 'a variety of factors, including similarity of design, similarity of the products, identity of retail outlets and purchasers, similarity of advertising media, the defendant's intent and actual confusion.' Application of these elements to the facts of this case compels the conclusion that Variety's sale of the accused goods is likely to confuse the public into believing that such goods are associated with Nike or that Nike sponsored, licensed or consented to the sale of such goods."

The court in this Eleventh Circuit case also addressed wilfulness as it relates to monetary damages. The court stated that "in order for Nike to recover treble damages on its counterfeiting claim, it must demonstrate not only that Variety infringed a registered trademark in violation of 15 USC §1114(1)(a), but also that Variety 'intentionally used a mark, knowing such mark is a counterfeit mark'… In the Eleventh Circuit, 'wilful blindness' is sufficient to satisfy §1117(b)'s intent requirement". In referencing *Monsanto Co v Campuzano* (206 F Supp 2d (SD Fla 2002)), the court also stated that "wilful blindness occurs when [a] person suspects unlawful activity and deliberately fails to act". In reliance on this definition, the court stated: "Quite simply, Variety consciously took many steps to ensure that the Nike products that it bought were genuine. While Variety ultimately failed in this endeavour, such failure was caused by negligence, perhaps gross negligence, but not by wilful blindness." As such, Nike was denied treble damages.

The bottom line

As this analysis shows, circuit courts remain divided as to whether a showing of actual wilfulness and/or confusion is required to obtain an award of monetary damages. Based on the cases reviewed and discussed above in the most active federal circuits, it appears that the Second, Ninth and Eleventh Circuits have taken differing positions on these issues. Regarding a showing of actual confusion, it appears that the Second Circuit requires such a finding while the Ninth and Eleventh Circuits do not. As for a showing of wilfulness for an award of monetary damages, it appears the Second Circuit requires this criterion be met while the Ninth and Eleventh Circuits do not. However, it should be noted that wilfulness may be a requirement for certain types of monetary damages awards (eg, discouraging a defendant's profits to prevent unjust enrichment and treble damages) in the Ninth and Eleventh Circuits. WTR

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