

Panel Date and Time	Friday, 27 October 2017
Location	FICPI conference, Hilton Molino Stucky Hotel, Venice, Italy
Topic	Trade Marks and the Bottom Line: Valuation of trade marks and branding in the 21st century
Description	Trade marks can be incredibly valuable assets, even when sold or licensed separately from any part of a firm's business. Annual lists of top performing brands regularly value such assets in the billions of dollars. Panellists will discuss how such valuations arise and will offer practical strategies for increasing a brand's value through trade mark protection, licensing and other means, moving past a purely legal view of a trade mark professional's role to focus on the valuable contributions such professionals can make to overall business strategies.
Speaker	Robert Cumming, Appleyard Lees
Precis	Robert will focus on the intersection of brand valuation and damages during litigation from an English law perspective. This will include a walk through of the damages judgment in the case of the Hotel Cipriani, which remains the largest ever award for trade mark infringement in English history.

1. Introduction

- 1.1. The primary objective for most claimants in intellectual property disputes is to stop the infringing activity. This is understandable because if a litigant is willing to accept the risk and has the resources to invest, the best it can usually hope for is merely to be returned to the original position, minus legal costs and management time. It is small wonder then that the pursuit of damages is regarded as simply too great a task to justify the effort; forget it and move on.
- 1.2. As tempting as that approach might be, businesses should not dismiss the opportunities that court proceedings can bring. Used wisely, tactical litigation can allow a solid intellectual property portfolio to be leveraged to its full potential by opening up new markets or closing off entry to competitors. This inevitably adds value to the underlying business. To ensure maximum returns therefore, any rights in patents, designs, trade marks, copyright and databases should be complemented by a carefully thought-out litigation strategy and form part of a company's overall vision.

2. The calculation of damages for trade mark infringement under English law

- 2.1. When calculating damages for trade mark infringement in English law, the general principle is that the court will seek to determine what is fair in the circumstances. It will generally¹ seek to put the claimant back into the same position which he would have been in had the infringement not occurred²:

¹ In cases of copyright infringement, it is also possible to recover additional damages for "flagrant" copying - s.97(2) Copyright, Designs and Patents Act 1988; *Absolute Lofts South West London Limited v Artisan Home Improvements Limited and another* [2015] EWHC 2608 (IPEC)

² *Meters v Metropolitan* [1911] 28 RPC 157, per Cozens Hardy MR: "...where licences are not granted to anyone who asks for them for a fixed sum, it is a matter which is to be dealt with in the rough - doing the best one can, not attempting or professing to be minutely accurate - having regard to all the circumstances of the case and saying what upon the whole is the fair thing to be done"

*Damages should be liberally assessed but... the purpose is to compensate the claimant and not punish the defendant - General Tire v Firestone*³.

- 2.2. This approach is now complemented by Article 13 of Council Directive 2004/48/EC on the Enforcement of Intellectual Property Rights⁴ which requires that when setting the damages for IP infringement, judicial authorities across the European Union:

(a) shall take into account all appropriate aspects, such as the negative economic consequences, including lost profits, which the injured party has suffered, any unfair profits made by the infringer and, in appropriate cases, elements other than economic factors, such as the moral prejudice caused to the rightholder by the infringement; or

*(b) as an alternative to (a), they may, in appropriate cases, set the damages as a lump sum on the basis of elements such as at least the amount of **royalties or fees** which would have been due if the infringer had requested authorisation to use the intellectual property right in question.*

- 2.3. The claimant's choice of which remedy to seek will largely depend on the method likely to achieve a higher award⁵. The question is, how does a claimant know which is likely to result in the higher award?

Liability and quantum

- 2.4. Very often the claimant will not know the value of its claim at the outset of the matter nor indeed when legal proceedings are begun at court. English court procedure therefore allows for the litigation to be bifurcated. This means that the trials for liability (who did what) and quantum (how much is it worth) are dealt with in sequence rather than together. In practice, quantum trials are rare as parties usually settle once liability is established.

General principles for assessment of damages

- 2.5. The general principles to be applied in assessing damages for infringement of intellectual property rights were considered in detail in *Gerber Garment Technology v Lectra Systems*⁶. They can be summarised as follows:

- i) damages are compensatory. The general rule is that the measure of damages is to be, as far as possible, that sum of money that will put the claimant in the same position as he would have been in if he had not sustained the wrong;
- ii) the claimant can recover loss which was (i) foreseeable, (ii) caused by the wrong, and (iii) not excluded from recovery by public or social policy. It is not enough that the loss would not have occurred but for the tort. The tort must be, as a matter of common sense, a cause of the loss;
- iii) the burden of proof rests on the claimant. Damages are to be assessed liberally. But the object is to compensate the claimant and not to punish the defendant;
- iv) it is irrelevant that the defendant could have competed lawfully;
- v) where a claimant has exploited his patent by manufacture and sale he can claim

³ *General Tire and Rubber Co v Firestone Tyre and Rubber Co* [1976] RPC 197

⁴ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:157:0045:0086:en:PDF>

⁵ *Island Records Ltd v Tring International plc* [1996] 1 WLR 1256

⁶ *Gerber Garment Technology v Lectra Systems* by Jacob J at first instance at [1995] RPC 383, and by the Court of Appeal at [1997] RPC 443

(a) lost profit on sales by the defendant that he would have made otherwise; (b) lost profit on his own sales to the extent that he was forced by the infringement to reduce his own price; and (c) a reasonable royalty on sales by the defendant which he would not have made;

- vi) as to lost sales, the court should form a general view as to what proportion of the defendant's sales the claimant would have made;
- vii) the assessment of damages for lost profits should take into account the fact that the lost sales are of "extra production" and that only certain specific extra costs (marginal costs) have been incurred in making the additional sales. Nevertheless, in practice costs go up and so it may be appropriate to temper the approach somewhat in making the assessment;
- viii) the reasonable royalty is to be assessed as the royalty that a willing licensor and a willing licensee would have agreed. Where there are truly comparable licences in the relevant field these are the most useful guidance for the court as to the reasonable royalty. Another approach is the "profits available" approach. This involves an assessment of the profits that would be available to the licensee, absent a licence, and apportioning them between the licensor and the licensee; and
- ix) where damages are difficult to assess with precision, the court should make the best estimate it can, having regard to all the circumstances of the case and dealing with the matter broadly, with common sense and fairness.

Damages based on account of profits

- 2.6. The English courts developed the remedy based on account of profits in *Potton v Yorkclose*⁷ and *Hoeschst Celanese International Corp. v BP Chemicals Ltd*⁸.
- 2.7. They found that it is intended to deprive the defendants of the profits which they have improperly made by the wrongful acts committed in breach of the claimants' rights and to transfer those profits to the claimants. The defendant is to be treated as having conducted business on behalf of the claimant and therefore the maximum recoverable amount is the total profit made through the infringing activity.
- 2.8. Following general accounting principles, the court should seek to identify the specific profit attributable to the infringing acts. It also established that:
 - i) an account is confined to profits actually made;
 - ii) account is addressed to identifying profits caused by the infringement;
 - iii) the fact that the profits could have been made in a non-infringing fashion is irrelevant;
 - iv) the claimant must take the defendant as he finds him; and
 - v) overheads, including tax, should be dealt with so as to arrive as closely as possible at the true profit.

⁷ *Potton v Yorkclose* [1990] FSR 11

⁸ *Hoeschst Celanese International Corp. v BP Chemicals Ltd* [1999] R.P.C. 203

Damages based on the loss suffered

- 2.9. Attempting to identify the loss which has been suffered is inherently problematic. The courts have therefore adopted an approach which assumes that the claimant granted a licence to the defendant at the market rate for the duration of the infringement (known as the "user principle" - see *Wrotham Park v Parkside*⁹, *General Tire v Firestone*¹⁰, *Ludlow v Williams*¹¹, *Irvine v Talksport*¹² and *National Guild v Silveria*¹³).
- 2.10. In the absence of direct comparisons, the court will look to comparable licences and data to determine what is the market rate and decide in all the circumstances what is fair. It may in particular consider the following factors:
- i) the terms of any agreement between the parties - *National Guild v Jones*¹⁴;
 - ii) the value and contribution of the mark to the defendant's business - *National Guild v Jones*;
 - iii) the nature and extent of the infringing use (e.g. greater magnitude of infringement on the internet than through hard copy publications) - *National Guild v Jones*; and
 - iv) whether the infringing party was a "direct competitor" - *USP plc v London General Holdings Ltd*¹⁵.
- 2.11. However, some judges may take the view that the user principle does not apply automatically, especially where a trade mark is not "available for hire" - *Reed v Reed*¹⁶.
- 2.12. The European Commission's analysis on the application of Directive 2004/48/EC, which reviewed the application by courts across the EU, observed that:

*where a licence royalty is already fixed and used in the relevant sector, this amount will be used; if there is not an agreed royalty rate or where it is difficult to determine precise rates, often an estimated average royalty related to the specific type of business involved is used*¹⁷.

3. Damages for trade mark infringement in Hotel Cipriani

- 3.1. In *Hotel Cipriani SRL & Others v Cipriani (Grosvenor Street) Ltd*¹⁸, the English courts considered an allegation of trade mark infringement and passing off brought by the owners of the luxurious Hotel Cipriani in Venice.
- 3.2. The proceedings were brought against three defendants who ran a restaurant in London called Cipriani London. The first defendant operated the day-to-day running of the restaurant. The second was an individual who was the sole director of the first defendant. The third

⁹ *Wrotham Park Estate Co Ltd v Parkside Homes* [1974] 1 W.L.R. 798

¹⁰ *General Tire v Firestone*

¹¹ *Ludlow Music Inc v Williams (No 2)* [2002] EMLR 29: "The basis of the assessment is a transaction as between willing licensor and willing licensee... to be decided on all the evidence... other similar transactions and... the approach which is taken to the negotiation of such agreements... precision is not attainable and that if one is to err, one should err on the side of generosity to the Claimant"

¹² *Irvine & Ors v Talksport Ltd* [2003] EWCA Civ 423

¹³ *National Guild of Removers & Storers Limited v Christopher Silveria and others* [2010] EWPC 15

¹⁴ *National Guild of Removers & Storers Limited v Jones*

¹⁵ *USP plc v London General Holdings Ltd* [2005] EWCA Civ 931

¹⁶ as per Jacob LJ (obiter) in *Reed v Reed* [2004] RPC 40

¹⁷ <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010SC1589&from=EN> at para 2.7.4

¹⁸ *Hotel Cipriani SRL & Others v Cipriani (Grosvenor Street) Ltd* [2008] EWHC 3032 (Ch), [2010] EWCA Civ 110, [2010] EWHC 628 (Ch)

defendant was a Luxembourg corporation which licensed the use of the name Cipriani to the first defendant.

- 3.3. The claimants succeeded in establishing infringement and that the mark was well known. The defendants' arguments were rejected and the decision was upheld on appeal. Having established liability and with no settlement being reached, the case moved to a quantum trial. The claimants sought an account of profits.
- 3.4. In his judgment on quantum, detailed management accounts were filed in evidence and each party relied on forensic accountants as expert witnesses. The judge sought to identify precisely what profits each of the defendants had earned from their infringing activities since the restaurant opened.

The licensor's liability

- 3.5. The liability of the third defendant, the licensor based in Luxembourg, was considered first as it was the most straightforward. The licence agreement to the first defendant allowed it to use several trade marks in exchange for 11.5% of gross sales. The court found that all of the marks contained in the licence agreement infringed those of the claimants. The court therefore held that all of the entitlement due under the licence was attributable to infringing activity. This meant that 11.5% of the gross sales of the restaurant during the infringing period would be payable in damages to the claimants. The gross sales were £34,640,000. The entitlement under the licence was therefore £5,304,000.

The restaurant operator's liability

- 3.6. The first defendant's liability was a little more complex. The claimants never claimed that all of the profits were attributable to the infringement. Some profits, after all, could be attributed to other, non-infringing, factors. The difficulty was in separating out these other bits from the profits relating to the misuse of the Cipriani brand.
- 3.7. Both expert witnesses in the case favoured a "distribution of costs" approach, which broadly speaking means the profits of a business are allocated in an approximate manner to different business units based on the proportion of the costs and expenses borne by each unit. However, this can over-simplify the calculation as it means that each cost is assumed to be equally profitable. The judge accordingly recognised that some weighting must be applied.

Calculate the functional profit and the intangible profit

- 3.8. The judge therefore tried to identify what is the functional profit level, that is, what is the ordinary margin at which a restaurant would expect to operate based on service alone. His view was that any profit made beyond this threshold would be attributable to other intangibles which give a special value, such as branding and marketing. He said:

a free market will only permit a marginal profit to be made from the provision of any service per se. Therefore, profits made over and above that level are likely to be as a result of something other than the service. By definition, the extra profit is caused by whatever intangibles are giving the service provider an edge over others in the same market.

- 3.9. The claimant submitted 7.5% was a typical profit margin for a restaurant, though the judge favoured the defendants' submission that 5% was more appropriate. The judge then calculated 5% of the turnover of the defendant to give a functional profit figure of £1,732,000. This could be deducted from the profit to leave a value which is attributable to profit from intangibles of £2,094,000.

Calculate the proportion of profits attributable to the infringement

- 3.10. However, this figure was inappropriate because some intangibles did not infringe, for instance the logo aspects of the branding. How could those be separated out?
- 3.11. The judge, following the guidance of the expert witnesses, decided that the best guide was the ratio payable between (a) the royalty under the licence agreement for the use of the name and logo (11.5% of turnover), and (b) the management fee for running the business affairs (3% of turnover). This equated to 79% of the profits being allocated to intangibles.

The calculation

- 3.12. Using the first defendant's turnover and the licence and management agreements with the third defendant, the court was therefore able to calculate the damages from the date when the restaurant opened to the date of the injunction as almost £6,965,000 excluding interest and costs.

4. Practical steps for increasing value – trade marks, licensing and business strategy

- 4.1. Integrate litigation into the overall business strategy using SWOT analysis¹⁹. It is often only used as a reactive measure to threats but should also be regarded as an opportunity to maximise the potential of the investment in the intellectual property portfolio.
- 4.2. Acting early can give the upper hand in litigation by, for example, seisin of jurisdiction and EUIPO torpedoes.
- 4.3. If you're likely to lose a quantum trial then pay any tax you owe quickly! Profits are only calculated net of tax if there is evidence they have been paid. Otherwise a losing defendant could be liable to the taxman without receiving the benefit of a set off against gross profits in the damages assessment.
- 4.4. Compile strong evidence of typical margins in your market. As claimant these should be as high as you possibly can prove.
- 4.5. Be prepared with evidence of expenses to reduce the gross profits.

¹⁹ https://en.wikipedia.org/wiki/SWOT_analysis

Annex 1

Damages calculation in Hotel Cipriani SRL & Others v Cipriani (Grosvenor Street) Ltd & Others

Item	Description	Value	Explanation
A	Gross sales	£34,640,000	Disclosed in evidence.
B	Total profit earned	£3,826,000	Disclosed in evidence.
C	Functional profit 5% of gross sales, £34,640,000 (A)	£1,732,000	This identifies profit which would be expected to accrue through a typical business.
D	Intangible profit Total profit (B) less functional profit (C) £3,826,000 - £1,732,000 =	£2,094,000	This identifies profit which is above the functional profit level and therefore which is attributable to other special value items, such as branding and marketing.
E	Proportion of which royalty payments form part of all payments to D3 to run the business. Royalty rate = 11.5% Management rate = 3.5% Ratio = $11.5 / (11.5 + 3.5) = 0.793$	79%	This identifies the proportion of the intangible profit (D) which relates to the infringing activity.
F	Infringing profit Intangible profit (D) x Proportion of profit attributable to infringing activity (E) 79% of £2,094,000 =	£1,661,000	This identifies the profit which has accrued through the infringing activity.
G	Damages payable by first defendant	£1,661,000	
H	Damages payable by third defendant	£5,304,000	
I	Total damages (before interest and costs)	£6,965,000	