Question MPT-2 – February 2023 – Selected Answer 1

B&B Inc. v. Happy Frocks Inc.

...

III. Legal Argument

Generally, there are three rationales justifying an award of profits in Trademark Infringement cases: (1) deterring the wrongdoer from doing so again, (2) preventing the defendant's unjust enrichment, and (3) compensating the plaintiff for harms caused by the infringement. *Spindrift Automotive Acc. v. Holt Ent., Ltd.* (Fr. Dist. Ct. 2021). A court must balance many factors in determining whether such an award is appropriate, and has discretion in assessing the relative importance of each factor in light of the particular situation to determine whether the equities weigh in favor of awarding profits. *Id.* The court in *Spindrift* outlined five factors for this consideration: (1) the infringer's mental state, (2) the connection between the infringer's profits and the infringement, (3) the adequacy of other remedies, (4) equitable defenses, and (5) the public interest. Each of these factors weighs in favor of denying an award of profits to Plaintiff B&B Inc.

(1) <u>Happy Frocks should not be held liable for profits, as the infringement was made innocently and its conduct at most amounted to mere negligence.</u>

Prior to the Supreme Court's decision in *Romag Fasteners v. Fossil Group,* 140 S. Ct. 1493 (2020)*,* courts had held that under the Lanham Act a plaintiff could only obtain an award for profits upon a showing that the defendant willfully infringed upon its trademark. The Court in *Romag* held that while a trademark defendant's mental state is highly important in determining whether awarding profits is appropriate, it is not an inflexible precondition to recovery.

In *Spindrift*, the District Court held that "particularly culpable defendants should be more likley to be subjected to an award of profits*,"* while on the other hand, "mere negligence, or an innocent nature to the infringement, would argue against an award of profits." In that case, the defendants knowingly and deliberately sold automotive parts not made by Spindrift but containing Spindrift's trademark, and it continued to do so after Spindrift notified it of the infringement.

In this case, however, Happy Frocks was not purposefully or knowingly infringing on B&B's trademark; rather an overseas contract manufacturer had begun producing infringing buttons without Happy Frocks knowledge and in express violation of its contract with Happy Frocks. Unlike *Spindrift*, Happy Frocks immediately investigated the infringement upon being made aware of it, terminated its contract with Quality Clothing, and removed infringing clothing out of its inventory at great cost to its business.

B&B will likely argue that Happy Frocks did not notify them of its efforts and also that it should have discovered the infringement upon inspection of the four shipments from Quality Clothing that were accepted over the course of the year. However, Happy Frocks has testified that they did not skimp on inspections, and had done due diligence in checking the quality of clothing received during the time period. Even if its quality control had been lacking, this would have amounted to mere negligence, and not recklessness or intent with regard to the infringing buttons on Happy Frocks' clothing. Additionally, while Happy Frocks did not notify B&B of its efforts to end the infringement, it took every reasonable effort to remedy the infringement and comply with its commitment to B&B.

Therefore, Happy Frocks' innocent infringement weighs against an award of profits.

(2) <u>The connection between Happy Frocks' profits and the infringement are negligible, as the buttons are only one small part of the clothing sold and consumers are unlikely to be swayed by the button brand.</u>

In determining the proximity of the connection between the infringement and the defendant's profits, a court may consider several questions: whether the trademark owner was harmed by lost or diverted sales beyond the infringement itself, whether the infringer's profits directly flow from or were caused by the infringement, whether consumers were confused by the infringement, and the certainty of whether the infringer benefited from the infringement. The essence of these questions is whether the infringer benefitted economically from the infringement. *Spindrift*. In *Spindrift*, the infringer, Holt, sold infringing parts that cost it 25% of the cost it would have paid for genuine parts, then sold them for the full amount that the genuine part would have cost. This was an obvious and direct economic benefit for Holt.

In this case, however, there is no direct profit to Happy Frocks from the button infringement. In fact, Happy Frocks made no additional income from the faulty buttons, as it still reimbursed Quality Clothing under its contract for the full price of the B&B buttons, meaning that Quality Clothing was the only party to make a profit from the infringement. To the contrary, Happy Frocks lost substantial profit from the infringement, as it had to terminate its contract with Quality Clothing at remove inventory at a loss during a time when clothing sales were highest, as their clothing had been "flying off the shelves."

Additionally, there is no evidence that B&B was harmed beyond the lost profits from Quality Clothing's infringement, as its profits increased during the period of the infringement. B&B will likely argue that customers will be able to recognize the difference between their high-quality buttons and cheap plastic buttons, and the release of so many fake buttons will harm their brand and confuse consumers, and that Happy Frocks should have recalled all of the clothing with inferior buttons as it had previously recalled pajamas with defective fabric. However, no other clothing manufacturers stopped using B&B buttons based on the infringement, and expert consumer surveys have shown that button quality is a very small factor in consumers' decisions to purchase clothing; only 3% of respondents say they would have noticed the logo as an added desireable feature of Happy Frocks clothing, 6% even noticed whether there was a brand name printed on the buttons, and less than 1% stated that the appearance of the brand name on a button was their only reason for purchasing a particular clothing item, showing B&B's button trademark only contributes a very small percentage to any increased profits for Happy Frocks, and that share would likely not amount to the profits lost by Happy Frocks in remedying the infringement.

Additionally, conducting a recall from over 900 retailers would be a drastic measure for the relative harm to B&B from the infringement, which was negligible based on the percentages. A court that was to award profits would have to determine to the best of its ability what portion of profits are attributable to non-infringing aspects of the product. *Spindrift*. Here, Happy Frocks' main product was not the buttons as it was in *Spindrift*, but rather was clothing of its own line, of which the buttons constituted a very small percentage. The harm attributable to the B&B infringement would be very small for the huge cost of recalling all those clothing items, and the inferior buttons do not present a risk or quality issue in the same way that defective fabric would have affected the integrity of the entire clothing piece in the previous recall done by Happy Frocks.

Therefore, B&B has not shown that Happy Frocks economically benefitted from the infringement, or that Happy Frocks' profits are tied to the infringement.

(3) <u>Other remedies are adequate to make B&B whole, making an award of profits inequitable.</u>

If other relief, such as actual damages and injunctions, are sufficient to make a trademark owner whole, then there is no basis for an award of profits. *Spindrift*. In *Spindrift*, the court held that there was nothing in the factual record to support Spindrift's claim that consumers would lose confidence in Spindrift's genuine parts based on consumers purchasing the infringing parts, leading this factor to weight against Spindrift's claim.

Here, as in Spindrift, B&B claims that consumers who received clothing items with the inferior buttons will lose confidence in B&B's quality. However, as described above, there is no evidence in the record supporting this assertion. B&B's profits have increased, it has kept all of its contracts with other manufacturers, and consumer surveys show that the consumers are unlikely to notice or be swayed by B&B's markings on the buttons.

Additionally, B&B has acknowledged that it does not have evidence of any lost profits aside from the lost sales from Quality Clothing's contract, and actual damages will provide an adequate remedy for that lost profit, while injunctive relief will meet B&B's desire to prevent future infringement, although Happy Frocks had terminated the infringement of its own accord months before this action was brought.

Therefore, this factor also weighs against a grant of profits to B&B.

(4) <u>Happy Frocks has a claim of equitable defenses based on B&B's delay in bringing its action until immediately before Happy Frocks' peak sales day and season.</u>

Where a defendant has a claim of laches (unreasonable delay) or failure to timely act on the part of the plaintiff or unclean hands, these would argue against an award of profits. *Spindrift.* In *Spindrift*, as Spindrift took action to stop sale of infringing parts immediately upon learning of the infringement, including filing a lawsuit and seeking a preliminary injunction, so there was no claim of equitable defenses.

In this case, on the other hand, while B&B did notify Happy Frocks immediately upon learning of the infringement, it then delayed an additional nine months to bring its case despite the fact that Happy Frocks took immediate action to investigate and terminate the infringement, and had already done so by the time B&B requested the injunction, which constituted an unreasonable delay on B&B's part. B&B may argue that Happy Frocks did not notify B&B of its measures taken, but neither did B&B look into whether remedial action was taken for nine months after its initial request to Happy Frocks. Additionally, Happy Frocks has a defense of unclean hands in this case, as the timing of B&B's claim, just before Black Friday which is a peak sales day and the start of peak holiday shopping, after nine months of delay, indicates a lack of good faith in bringing the action as it puts additional pressure on Happy Frocks when poor publicity and legal filings would be most harmful to its business.

Therefore here equitable defenses weigh in favor of Happy Frocks and against a reward of profits to B&B.

(5) <u>There is no public interest in making Happy Frocks disgorge profits, as there is no threat to public safety, and no indication that Happy Frocks would willingly participate in other infringements.</u>

If there is a public interest in preserving safety or deterring other infringements, this could weigh in favor of an award of profits. The court in *Spindrift* noted, for example, that a medicine containing a harmful ingredient would raise significant public safety concerns for the public interest, but where infringing parts did not cause a danger to the public and an injunction would prevent future infringement, there was no public interest in awarding profits.

Here, as in *Spindrift*, there is no public safety concern related to the infringing buttons. B&B has testified that there was no increased likelihood of choking, poisoning, or coming loose that would endanger children. Additionally, even before this case was brought, Happy Frocks had willingly terminated its innocent infringement and ended its contract with the infringing manufacturer, and an injunction against future infringement would protect B&B's and the public's interest in preventing trademark infringement.

Therefore, this factor also weighs against a grant of profits to B&B, as there is no public interest in making the award.

<u>Conclusion</u>

Every factor outlined by under Franklin precedent weighs against a granting of profits to B&B, as Happy Frocks was an innocent infringer that did not act willfully and did not profit from the infringement. Other remedies will be adequate to compensate B&B for its losses from the infringement, and its bad faith in delaying the timing of its claims and lack of public interest in further penalizing Happy Frocks beyond all of its lost profits already incurred weigh against any award of profits to B&B in this case.

Question MPT-2 – February 2023 – Selected Answer 2

POST-TRIAL BRIEF

INTRODUCTION

This post-trial brief concerns whether Happy Frocks (HF) is liable to B&B for an award of profits from the sale of infringing goods arising from the instant trademark infringement lawsuit. For the reasons set out below, this Court should hold that HF is not liable to B&B for profits.

CAPTION

[Omitted per instructions]

STATEMENT OF FACTS

[Omitted per instructions]

LEGAL ARGUMENT

HF first sets out the law applicable to liability for profits in trademark infringement actions. HF then applies those laws to the facts of this case in showing that B&B is not entitled to lost profits.

<u>A: Applicable law</u>

The Lanham Act specifically authorizes the award of lost profits in trademark infringement lawsuits. (Romag case). The infringing defendant's mental state is a relevant consideration when it comes to awards of lost profits in the trademark infringement context. (Id. (opinion of Gorsuch, J.)). However, willfulness is not a prerequisite to awards of lost profits under the Lanham Act. (Id., opinion of Alito, J.)). Although this statement by Justice Alito was set out in a concurrence and not the majority opinion, the majority implicitly endorsed this conclusion in declining to interpret the Lanham Act to specifically require a showing of willfulness for lost profits. (Id. (opinion of Gorsuch, J.)). And Justice Alito confirmed this reading of the split opinions by explaining that, although willfulness is highly important of the propriety of lost profits in trademark infringement actions, it is by no means dispositive. (Id., opinion of Alito, J.)).

The District of Franklin has read *Romag* as much and confirmed that willfulness need not be found to justify lost profits awards. (Spindrift case). Applying this principle, the District of Franklin set out several factors to be considered in identifying whether awards of lost profits are justified in trademark infringement contexts: (1) the infringer's mental state--whether the defendant acted willfully, with callous disregard for the plaintiff's rights, or with a specific intent to deceive--mere negligence and innocent conduct do not lend themselves to a cuplable mental state; (2) the connection between the trademark infringement and the infringer's profits, i.e., is there a causal nexus between the infringement and the profits at issue; (3) whether other remedies--such as actual damages and injunctive relief--are sufficient to make the defendant whole; (4) the availability of equitable defenses like laches (unreasonable delay), failure timely to act by the plaintiff, acquiescence in the infringement by the plaintiff; or unclean hands; and (5) whether awards of lost profits would serve the public interest by preserving public safety or deterring other infringement. (Id.).

B: Application of law to fact

HF analyzes the foregoing five elements in the context of this case in the ensuing paragraphs.

B.1: HF does not have a culpable mental state because it acted innocently, and not with willfulness, callus disregard, or with a specific intent to deceive.

The record establishes that HF acted innocently in this case.

Importantly, Samuel Harris, the CEO of HF, testified on direct examination that Quality Clothes (QC), the supplier using the allegedly infringed B&B buttons, was supposed to purchase the buttons directly from B&B and then bill HF for the cost of the buttons. (Harris transcript). Although QC was "using cheaper buttons, [it] was still billing [HF] and [HF] was still paying [QC] for the cost of buttons from B&B." (Id.). And B&B confirmed Harris's explanation of what had happened with the fake buttons through the direct examination of B&B Chief Executive Officer Vera Garcia. (Garcia transcript).

This information from Harris and Garcia establishes that HF was entirely innocent when it came to the infringement of B&B's trademark. (Harris transcript; Garcia transcript). Instead, QC was the responsible party for this trademark infringement because QC itself affirmatively went out and acquired buttons not made by B&B but that bore the B&B trademark. (Harris transcript). And, when HF found out that QC was using B&B-marked buttons that did not come from B&B, HF contacted QC immediately and told them to stop. HF also terminated its contract with QC and ceased selling its inventory of clothing that QC manufactured using fake B&B buttons. (Id.).

HF acknowledges that Harris testified that HF was negligent when it came to the inspection of QC-made clothing containing buttons from B&B such that HF should have noticed the trademark infringement earlier. (Id.). That does not matter with regard to lost profits. The District of Franklin has specified that mere negligence is insufficient to tip the mental state factor for awards of lost profits in favor of the plaintiff. (Spindrift case)). And the fact that HF accelerated its processing of the shipments received from QC pursuant to generalized instructions to all employees is insufficient to raise HF's mental state from negligence to something more sinister. (Id.; see Spindrift case)).

These facts establish that the first element of the test for the propriety of lost profits favors HF. (Cf. Spindrift case (holding that the first element favored the plaintiff when the defendant acted knowingly and deliberately)).

<u>B.2: There is no connection between the alleged infringement by HF and profits earned by HF at B&B's expense.</u>

The record demonstrates that there is no connection between the alleged infringement by HF and profits earned at B&B's expense, so the second lost profits factor favors HF.

As explained by the District of Franklin, the requisite causal connection for lost profits cannot be shown by pointing to sales lost by the infringement itself, which is accounted for in actual damages. (Id.). Indeed, all B&B can complain of here is lost sales. Harris testified that QC was supposed to buy real buttons from B&B but instead bought fake B&B buttons from someone else. (Harris transcript). Garcia confirmed this account of the infringement on behalf of B&B. (Garcia transcript). This factual context epitomizes actual damages that should not be remedied through lost profits. (Spindrift case).

In addition, HF does not have profits flowing directly from the infringement because it is uncertain whether HF even benefited from the infringement. (Id.). As explained by Harris, HF immediately stopped selling clothing products made by QC when it learned about the infringement. (Harris transcript). Harris also explained to the court that HF lost the entire value of its on-hand inventory of QC clothing due to the infringement. (Id.). It is unclear whether HF can recover this money lost from QC. (Id.). This important fact cancels out the competing facts that QC clothing stocked by HF was selling like hotcakes, and that HF did not recall the allegedly infringing clothes. (Id.). Nor would a recall have been possible given the volume of retailers (900) to whom HF shipped QC clothing containing fake B&B buttons. (Id.).

Nor were consumers confused by the alleged infringement by HF. (Id.). As HF's retained expert witness Tiffany Chen explained, HF conducted a scientific consumer survey in response to the use of fake B&B buttons on HF clothing made by QC. (Chen transcript). In this survey, HF quizzed 839 consumers of HF clothes made by

QC. The survey revealed that use of B&B's logo on the buttons played a minimal role in the clothing purchase. (Id.). Indeed, only "3% of [survey] respondents said that they noticed the logo and thought it added to the desirability of the clothes." (Id.). HF also conducted a separate survey of 997 general consumers of children's clothing during the pendency of this lawsuit. (Id.). This survey showed that only 6% of consumers base clothing purchases on whether a brand name is printed on the button. (Id.). And less than 1% of consumers in this second survey said the appearance of a brand name on a button was their only reason for purchasing clothing. (Id.). To this point, Garcia confirmed that customers "know the difference between [B&B's] high quality buttons and the inferior-quality ones that were used" by QC in manufacturing clothes for HF. (See Garcia transcript).

Based on these facts, it is clear that the second element of the test for propriety of lost profits favors HF. (Cf. Spindrift case). Given the presence of only lost sales to QC, the lack of profits flowing from infringement (as shown by HF's unrecoverable total loss of the value of its QC inventory), and the lack of confusion on the part of customers, the facts simply do not favor B&B. The facts instead favor a ruling that B&B is not entitled to lost profits.

<u>B.3: Alternative remedies like actual damages and injunctive relief are sufficient to make B&B whole in this case.</u>

The record establishes that alternative remedies like actual damages and injunctive relief are sufficient in this action such that B&B is not entitled to recover lost profits from HF.

Importantly, Harris explained in his testimony that the harm inflicted on B&B was lost sales of its buttons to QC as a result of QC's decision to use fake B&B buttons in clothing manufactured for HF. (Harris transcript). And Garcia confirmed this account of what had happened with the fake buttons on cross-examination. She complained to the jury that B&B "lost the revenue from the sales of [its] buttons to [QC] for the time that they used the infringing buttons until they stopped." (Garcia transcript). This harm epitomizes the harm that must be remedied through actual damages and not lost profits.

Furthermore, injunctive relief would be sufficient to remedy the harm suffered by B&B from the fake buttons by preventing HF and QC from using fake buttons in the future. As explained by Garcia on cross-examination, one of B&B's concerns with regard to the trademark infringement in this case was that HF and QC stop using fake buttons. (Garcia transcript). An injunction will accomplish this goal far more effectively than lost profits. (See id.).

For these reasons, the third factor in the five-factor test for B&B's entitlement to lost profits favors HF. (See Spindrift case).

<u>B.4: HF benefits from equitable defenses of laches, unclean hands, and failure timely to act by B&B in response to the alleged infringement.</u>

Evidence in the record shows that the fourth factor of equitable defenses favors HF such that B&B is not entitled to lost profits.

At the outset, this factor superficially favors B&B because Garcia testified that, when B&B found out that fake buttons were on HF clothing, B&B sent HF a cease-and-desist letter. (Garcia transcript). Garcia further testified that a HF manager told B&B that HF would look into the issue but B&B heard nothing from HF and so sued HF for trademark infringement. (Id.).

Despite B&B's urge to argue otherwise, these facts do not tip the forth factor in favor of B&B. Garcia admitted on cross-examination that B&B did not file the complaint in this action, seeking an immediate injunction, until nine months after the alleged infringement was discovered. (Id.). To make things worse, B&B complicated resolution of the infringement matter by suing HF only one week before the popular American "Black Friday" sales starting in November. (Id.). As admitted by Garcia, Black Friday is the day with the largest sales of most retail goods like clothing. (Id.).

The above critical facts admitted by Garcia--that B&B waited nine months to sue HF, and filed suit immediately before the busiest sales day on the calendar, demonstrate that the fourth factor of the lost profits test favor HF. By unduly delaying B&B subjected itself to the equitable defenses of laches and failure timely to act. B&B also subjected itself to the unclean hands defense because any harm to B&B was accelerated by HF's inability to address the trademark infringement complained of before Black Friday. (See Spindrift case (setting out the countervailing factual scenario where the plaintiff immediately took action to stop the alleged trademark infringement)).

<u>B.5: A lost profits award would not serve the public interest by preserving public safety or preventing future harm.</u>

The factual record in this case is such that the fifth and final factor of the test for lost profits in trademark favors HF. There is no evidence that the fake buttons used by QC in making HF clothing are dangerous. Nor is there any evidence that lost profits will prevent future harm that could not be remedied through equitable injunctive relief.

Importantly, Garcia conceded on cross-examination that the infringing buttons sold on HF clothing were not dangerous--they were not poisonous or anything like that. They were simply made of cheap plastic. (Garcia transcript). And Garcia further conceded that a child was not more likely to swallow a fake B&B button than a real B&B button. (Id.).

Furthermore, as explained above, injunctive relief is satisfactory in this case because such equitable relief will stop HF and QC from using fake B&B buttons. And no other clothing manufacturers besides QC have stopped using B&B buttons because HF sold the clothes using fake B&B buttons. (Garcia transcript). Therefore, lost profits will not stop future infringement of B&B's trademarked buttons by third parties. (See id.).

In this context, the fifth and final factor for B&B's entitlement to lost profits in trademark favors HF such that the court should not grant lost profits to B&B in this action. (See Spindrift case (denying lost profits because injunctive relief was sufficient and no public health and safety-type harm could possibly result from not awarding lost profits to the plaintiff in that trademark infringement action)).

CONCLUSION

For the foregoing reasons, this Court should find that B&B is not entitled to recover lost profits from HF in this trademark infringement action. All five factors of the test for a trademark infringement plaintiff's entitlement to lost profits favor HF such that an award of lost profits to B&B is indefensible. Such an award to B&B would surely be reversed on appellate review.