

Key Damages Questions To Ask In Copyright Mediation

By **Bruce Isaacs** (June 18, 2019, 5:15 PM EDT)

In 2016, the jury ruled in favor of the defendant Led Zeppelin in the “Stairway to Heaven” case (*Skidmore v. Led Zeppelin*). In the fall of 2018, the U.S. Court of Appeals for the Ninth Circuit, in a controversial opinion, ordered a new trial. However, on June 10, 2019, the Ninth Circuit issued an order granting a rehearing of the case, en banc, and further ordered that the prior Ninth Circuit opinion may no longer be cited.

Although it is not clear how the Ninth Circuit will ultimately rule on the issues raised in the case, or what its rationale will be, this recent development focuses attention on the issue of damages if a new trial is required. If the Ninth Circuit permits a new trial, *Skidmore* will present the issues of actual damages plus a disgorgement of profits to the jury and, should *Skidmore* prevail, the issue of attorney fees to the trial judge. These same issues, among others, typically arise at a mediation of a copyright infringement action, and they are discussed below.



Bruce Isaacs

Section 412

Section 504 of the Copyright Act sets forth the monetary relief to which a prevailing plaintiff is entitled in a copyright infringement action: (1) actual damages plus a disgorgement of profits “attributable” to the infringement (and only profits not taken into account in the calculation of actual damages, i.e., no double dipping) plus attorney fees; or (2) statutory damages (or enhanced statutory damages if the conduct is “willful”) plus attorney fees. Given that these elements of damages are clearly set forth in the statute, why start a mediation asking questions about Section 412? Because often the issue of attorney fees, and ability to recover them or not, is the tail that wags the dog.

Section 412 provides that if the copyright infringement took place before the copyright at issue was registered (and assuming the three-month safe harbor provision does not apply), then the copyright plaintiff has lost his or her right to recovery attorney fees and statutory damages. This is important because often a copyright plaintiff learns that his or her copyrighted work has been infringed and that the infringement took place before he or she ever registered it. The plaintiff immediately runs to the Copyright Office and obtains his or her copyright registration, a prerequisite before the copyright plaintiff can file suit (as the U.S. Supreme Court recently made clear in *Fourth Estate Public Benefit Corporation v. Wall-Street.com LLC*).

However, if the infringement took place before the date of the registration, the plaintiff has lost the right to recover attorney fees, and the plaintiff has lost significant leverage at the mediation. And to further shift the equilibrium in the case, the defendant may even create further leverage for itself by way of a Rule 68 offer, which may shift the attorney fees and costs to the plaintiff even if the copyright plaintiff does prevail to some extent at the time of trial.

In short, at the copyright infringement mediation, a fundamental question will arise early: Are attorney fees off the table, or not?

Actual Damages

The most common scenario for actual damages is a lost license fee or a lost royalty stream. In order to determine actual damages, the key question is: What is the fair market value for the lost transaction that should have taken place (and, at a mediation, is there a “vig” for “taking without asking”)? Or what would a willing licensee pay for a license to use the copyrighted work? The past licensing history of both parties is highly probative and persuasive evidence as to the issue of actual damages.

Even if there is no documentation for past licenses, and the defendant makes a showing that the plaintiff would not have entered into the license in the first place, the courts still permit a “hypothetical negotiation” of fair market value to determine a nonspeculative amount for actual damages.[1]

Disgorgement of Profits — Direct Profits and Indirect Profits

In addition to actual damages, a copyright plaintiff is entitled to recover a disgorgement of direct profits as well as indirect profits “attributable” to the infringing activity. As expressly set forth in Section 504(b), it is plaintiff’s burden to determine the amount of the gross receipts derived from the alleged infringing work and then, in response, it is the defendant’s burden to establish (1) legitimate deductible expenses and (2) the percentage of the profit “attributable” to the infringement. If the profits are attributable to “other factors,” then those profits are not recoverable. Whether or not profits are attributable to “other factors” can be demonstrated by the testimony of the defendants themselves, explaining how their profits are made and what factors do and do not contribute to those profits, as well as by the testimony of experts.

The distinction between direct profits and indirect profits is important because of the issue of causation and burden shifting. This distinction is demonstrated by the leading case of *Frank Music Corp. v. Metro-Goldwyn-Mayer Inc.*, which establishes many of the rules for the recovery of direct and indirect profits.

In *Frank Music*, the Hallelujah Hollywood revue at the MGM casino performed several songs from the musical “Kismet” without a license. The music publisher sued for actual damages and disgorgement of direct profits, the profits derived from the musical revue itself that were attributable to the infringed songs. But the music publisher argued that the patrons who came to see the musical show contributed significantly to the other profit centers of the hotel, especially the gaming tables where patrons gambled and, therefore, the music publisher should be entitled to a percentage share of those indirect profits as well.

Thus, direct profits are the profits that derive from the exploitation of the copyrighted materials themselves, in this case the profits from the musical revue which performed the songs from “Kismet,” while indirect profits are the profits which derive from the use of the copyrighted work to sell or promote a separate and distinct product, in this case gambling and other services offered at the

hotel.[2] In *Frank Music* (decided under the 1909 Act), in a case of first impression, the Ninth Circuit ruled that a copyright plaintiff is entitled to recover indirect profits if they are “ascertainable.”

The Element of Causation for Indirect Profits and How the Burden Shifts to the Copyright Plaintiff

Section 504(b) establishes it is the defendant’s burden to make the showing of deductible expenses (including an overhead calculation which is allowed as *Frank Music* so holds) and to make the showing as to whether or not the profits are attributable to the infringement as opposed to other factors. Although these burdens fall on the defendant according to the statute, that is not really true insofar as indirect profits are concerned according to the case law. The courts have consistently held that when considering the issue of indirect profits, the copyright plaintiff must first satisfy the additional element of causation, before the two burdens of deductible expenses and apportionment shift to the defendant.

In *Mackie*, an artist filed a copyright infringement suit when the Seattle Orchestra used a picture of his sculpture, an unauthorized derivative work, in its brochure promoting ticket sales. Mackie sought not only actual damages (in the form of a hypothetical negotiation for a license fee or a royalty payment), he also sought indirect profits claiming that some of the profits earned by the Seattle Symphony Orchestra concerts were attributable to the use of his sculpture in the brochure.

The Seattle Symphony moved for partial summary judgment on the issue of indirect profits, and the trial court granted that motion, then the Ninth Circuit affirmed. The Ninth Circuit reasoned that Mackie had to show a causal link between the infringement and the profits and he had to do so with nonspeculative evidence before the issue of apportionment (defendant’s burden) even arises. The Ninth Circuit concluded that Mackie could not establish this element of causation with any nonspeculative evidence and thus the sculptor had no right to recover indirect profits.

In *Polar Bear Productions Inc. v. Timex Corp.*, the Ninth Circuit articulated a two-step framework with respect to indirect profits: (1) the copyright plaintiff must first show the causal link between the infringement and the profits; and (2) once the element of causation is satisfied, then the alleged infringer bears the burden of showing deductible expenses and which profits are attributable to the infringement as opposed to other factors.

In *Polar Bear*, the plaintiff made a kayaking film, which Timex used for commercial purposes after its license had expired, thus constituting copyright infringement. Polar Bear contended that Timex used the film at trade shows, in a Mountain Dew commercial and to enhance its brand generally. Polar Bear sought indirect profits in connection with all three of these uses. The Ninth Circuit found Polar Bear’s expert testimony and other circumstantial evidence convincing as to the trade show use and as to the Mountain Dew commercial use, but not with respect to the brand-enhancement theory. The Ninth Circuit concluded that the Polar Bear had met its initial burden to establish the element of causation in order to recover indirect profits as to two of the three categories of use.[3]

Statutory Damages

Assuming the copyright plaintiff does not have a Section 412 problem, and assuming that actual damages and a disgorgement of profits would yield less recovery, a copyright plaintiff may elect to seek statutory damages, which range in the amount of \$750 to \$30,000, an amount which can be enhanced to \$150,000 if the conduct is found to be willful.

Typically, the fight is over how many awards of statutory damages apply. Is it per photograph? Per

video? Per use? Per violation? Section 504(b) is crystal clear that the award of statutory damages is “per work infringed.” Thus, if the facts present a situation where only one work is infringed, and assuming nonwillful conduct, the damages are limited to a single recovery in the \$750 to \$30,000 range. But often times, it is still not clear, and vigorously debated, how many “works” are at issue.

For example, in *VHT Inc. v. Zillow Group Inc.*, VHT, a real estate photography company, provided thousands of photographs to Zillow. VHT contended that Zillow exceeded the scope of a license agreement by using the photographs on unauthorized platforms. As part of its claim, VHT sought statutory damages because, as it contended, thousands of works were at issue. If the photographs were deemed to be separate works, the amount of statutory damages would be substantial.

If, on the other hand, the group of photographs were deemed to be a “compilation,” then the statutory damages award would be quite modest, a one-time, per work amount. The Ninth Circuit emphasized that Section 101 includes a definition of compilation and ultimately ruled that it could not decide the issues of how many works were in dispute and whether or not the photographs constituted a compilation and it remanded those issues back to the district court for determination.

In addition to a dispute over the number of works infringed, there is almost always a dispute over willfulness. Typically, the copyright plaintiff will demand enhanced statutory damages because it had previously sent a cease-and-desist letter to the defendant and the defendant had nevertheless continued to make use of the infringing work after this demand letter.

A clear case of willfulness? Perhaps so, but not so fast according to the case law. As the Ninth Circuit has made clear, a finding of willfulness is appropriate if: (1) the alleged infringing party is aware of the infringing activity; or (2) the alleged infringing party acts with reckless disregard or with “willful blindness.”[4] Reckless disregard can be demonstrated when the alleged infringing party refuses to investigate the alleged violation. Willful blindness requires that the alleged infringing party holds a subjective belief that infringing conduct is taking place on its platform, network, etc., but deliberately takes no action to avoid learning about the infringement.[5]

However, according to the Ninth Circuit, ignoring a cease-and-desist letter and continuing to use the infringing work is not necessarily fatal to the issue of willfulness. As the Ninth Circuit has held: “[c]ontinued use of a work even after one has been notified of his or her alleged infringement does not constitute willfulness so long as one believes reasonably, and in good faith, that he or she is not infringing.[6]

Attorney Fees

Again, assuming no Section 412 problem, the prevailing party, whether plaintiff or defendant, shall be entitled to recover attorney fees under Section 505 in an amount in the discretion of the trial judge.[7] In *Kirtsaeng v. John Wiley & Sons* (2016), the U.S. Supreme Court further ruled that substantial weight should be given to the “objective reasonableness” factor, but that the other factors articulated in *Fogerty v. Fantasy, Inc.* need to be considered as well in order to promote the purposes of the Copyright Act and to strike the correct balance between encouraging and rewarding works of authorship while also enabling creators to build on works that came before them.

Conclusion

In order to make meaningful progress at a mediation of a copyright infringement case, the parties

should be ready to defend or attack the damages models and demonstrate: (1) how actual damages are calculated; (2) the amount of direct profits; (3) the amount of indirect profits — provided the element of causation has been satisfied (and, if so, how); (4) the amount of gross receipts; (5) the amount of deductible expenses; (6) whether the profits are “attributable” to the infringement as opposed to “other factors”; (7) whether statutory damages are in order and, if so, the number of works at issue and whether the infringement was willful; and (8) whether there is, or is not, a Section 412 problem that permits or prevents the recovery of statutory damages and attorney fees.

Bruce Isaacs is a mediator and arbitrator at Signature Resolution.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] See *Polar Bear Productions, Inc. v. Timex Corporation* (9th Cir. 2004); *Gaylord v. United States* (Fed. Cir. 2015); *Oracle Corporation v. SAP, AG* (9th Cir. 2014).

[2] See also *Mackie v. Seattle Symphony Orchestra Public Benefit Corporation* (9th Cir. 2002).

[3] Compare *Bouchat v. Baltimore Ravens Football Club, Incorporated* (4th Cir. 2003); *Fahmy v. Jay-Z* (D.C. Cal 2011); *Griffo v. Oculus VR, Inc.* (C.D. Cal 2018).

[4] *Unicolors, Inc. v. Urban Outfitters, Inc.* (9th Cir. 2017).

[5] *Luvdarts, LLC v. AT&T Mobility, LLC* (9th Cir. 2013).

[6] *Evergreen Safety Council v. RSA Network Inc.* (9th Cir. 2012); *Danjaq LLC v. Sony Corp.* (9th Cir. 2001).

[7] *Fogerty v. Fantasy, Inc.* (1994).