

Milano Pizzeria Case Study: Hard Lessons Learned by Canadian Licensor

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Every now and then a case comes before the courts and serves as a stark reminder that good licensing practices and IP portfolio management are critical to any business. *Milano Pizza Ltd. v. 6034799 Canada Inc.*¹ (“*Milano Pizza*”) is certainly such a case, highlighting the need to develop rigorous practices when it comes to documenting the creation, acquisition and licensing of IP assets.

Milano Pizza is the saga of a family business, operating since the early nineties, which initiated IP infringement proceedings against a disgruntled former licensee. To its utter dismay, it discovered that it could neither claim ownership of the copyright in the company logo it had been using for decades, nor establish that it ever had an enforceable licence in place with any of its 32 operating pizzerias that used the logo, let alone the defendant company. As a result, its copyright claims were dismissed entirely, and its registered trademark faces serious risk of being expunged.

This case is a wake-up call to licensors of IP assets who conduct their business affairs on nothing more than a smile and a handshake, perhaps with the imprudent thought that doing so will allow for a savings on legal spend and reduction in administrative burden. Of course, the reality is that such an approach to business is very likely to give rise to unnecessary disputes and expensive litigation, and may lead to the potential loss of exclusive rights to use key IP assets, including the core brand.

1. When the Facts Hit Your Eye Like A Big Pizza Pie

Milano Pizza Ltd. (the “Plaintiff”) owned a business, self-described as “a group of independently owned and operated pizzerias”, each operating under the trademark “MILANO PIZZERIA”.

At the outset, there were six pizzerias operated directly by members of a single family, but by the mid 1990’s pizzerias were being sold to others to own and operate. In 1996 one of these, the “Baxter Location”, was sold to an individual and subsequently to that individual’s numbered company. In 2002 the Baxter Location was sold to the Defendant. That same year, the Plaintiff obtained a registration for the following composite trademark (the “Logo”) in association with “take out restaurant services, with delivery”, claiming a date of first use of March 1994:



In or around 2013, the relationship between the Plaintiff and the Defendant began to deteriorate, and had completely broken down by 2016. The Plaintiff contended that the Defendant’s use of the Logo was subject to a written licence agreement, which Plaintiff purported to terminate on June 29, 2016. Subsequently, the Plaintiff commenced an action in the Federal Court of Canada

¹ 2018 FC 1112.

concerning the Defendant's unlicensed use of the Logo at the Baxter Location, including allegations that this act constituted (i) infringement of, and depreciation of goodwill attaching to, the trademark registration for the Logo, contrary to sections 19 and 22 of the *Trade-marks Act*; (ii) passing off contrary to the statutory codification of the tort in subsection 7(b) of the *Trade-marks Act*, and; (iii) infringement of its copyright in the Logo contrary to s. 27 of the Copyright Act. In response, the Defendant sought to invalidate the trademark registration for the Logo, and sought damages and injunctive relief in regards to the Plaintiff's own alleged passing off.

The context of the Court's decision in *Milano Pizza* was a motion for summary judgment by the Defendants to have the Plaintiff's claims dismissed, and a cross motion by the Plaintiff for summary judgment on all of its claims with the exception of the copyright infringement. In Canada, the Federal Court will grant summary judgment when there is no genuine issue for trial with respect to a claim or defence. That is, where there is no legal basis for a claim or defence, or where the Court has all of the evidence required to make a fair and just determination, the matter can be decided without the need for a trial. Summary judgment is often considered inappropriate where there is conflicting evidence and issues of credibility remain.

2. Licensor + Licensee or Loosely Organized Buying Cooperative ?

One of the central issues in dispute concerned the nature of the relationship between Plaintiff and Defendant, which the parties characterized very differently. The Plaintiff asserted that it and the independent operators of the Milano Pizzerias (including the Defendant's Baxter Location) were parties to licence agreements through which Plaintiff granted the pizzerias rights to use the Logo and related trademarks. However, the Defendant maintained that the Plaintiff and the independent pizzerias merely collaborated in a loosely organized family business and buying cooperative and that Plaintiff, rather than being a licensor granting rights in the trademark, merely acted as a purchasing agent and coordinator.

While the Plaintiff maintained that there was a written licence agreement to which the Defendant was subject, unfortunately it could not produce the written agreement, its only copy believed to have been destroyed in a flood. Under Canadian trademark law, while a written licence agreement is always the best evidence of the existence of the licence, it does not need to be in writing to be valid and enforceable. The critical issue is whether the trademark owner has authorized the other person to use the trademark and that the owner has, directly or indirectly, control over the character or quality of the goods or services that the other person is providing in association with the trademark. The following factors were raised by the Plaintiff to substantiate its claim that it had sufficient control over the pizzerias such that a licence was in place:

- **Purchasing Commitment and Quality Control:** The Plaintiff alleged that in exchange for use of the trademarks, the pizzerias were obliged to purchase most of their supplies through a specific supplier designated by the Plaintiff. The Plaintiff asserted that this was sufficient to demonstrate that it held a level of control over the taste and quality of the food being sold at each location.
- **Investment in the Brand:** The Plaintiff argued that by using a single supplier, it received rebates, which allowed it to allocate more resources towards marketing and promotion of the pizzerias.

- **Territorial Restrictions on Operators:** The Plaintiff contended that because the pizzerias were precluded from advertising or accepting food orders outside of specified territorial areas, such geographic restrictions further underscored the Plaintiff's control over the pizzerias.

Conversely, the Defendant alleged that no such licence was in place and that the Baxter Location had at all times independently exercised complete control over advertising and marketing of the pizzeria. The Defendant advanced the following arguments intended to show that the Plaintiff did not exercise the requisite control required of a licensor:

- **Independent Control over Goods, Advertising, and Accounting:** The Defendant claimed it made its own choices with respect to menu items, recipes, and ingredients as well as advertising and marketing materials such as pizza box stamps and uniforms. It also pointed to its accounting practices, which differed from those of the Plaintiff.
- **Centralized Purchasing was Purely Voluntary:** The Defendant claimed the reason the pizzerias opted to use a single supplier was to obtain the financial discounts and rebates that could be applied to a common marketing and advertising budget. The Defendant stressed that opting-in was at all times "purely voluntary". To illustrate this, the Defendant provided receipts showing the Baxter Location had on several occasions sourced its products from third parties.
- **Asset Purchase Agreement – absence of trickle down obligations:** The Defendant also relied upon the asset purchase agreement it executed when purchasing the Baxter Location. The Defendant pointed to the absence of any terms governing or restricting the use of the Logo, the name "Milano pizzeria", "Milano pizza", or any other intellectual property.
- **15 Years of Pizzeria Autonomy:** Lastly, the Defendant pointed to the fact that while the Plaintiff had approached the Defendant on numerous occasions to sign a licence agreement governing the use of the Mark, the Defendant had always refused to sign it on the basis that the Defendant believed the Plaintiff did not own the Mark and the fact that the Baxter Location had been running autonomously for the prior 15 years.

In the end, the Court noted that the affidavit evidence of the parties was irreconcilable, bringing the credibility of the witnesses into question. As a result, the court concluded there was a genuine issue for trial as to whether a trademark licence agreement ever existed, and if so, what the terms of such a licence may have been.

3. Intellectual Property in the Logo: the copyright and trademark claims

Against the backdrop that the Court was unwilling to reach a conclusion as to the nature of the relationship between the parties, the Court turned to the claims of copyright infringement and the trademark claims of passing off and the depreciation of the value of goodwill. The Court first sought to make a determination as to: (i) whether the Plaintiff could show it had title over the copyright in the Logo (as an artistic work); and (ii) whether the trademark registration for the Logo was still valid and enforceable. As put forward by the Defendant, if the Plaintiff neither

owned the copyright in the Logo nor owned a valid and enforceable trademark in the Logo, the Plaintiff's causes of action collapsed.

(i) **Copyright Claim**

The Plaintiff alleged that the Defendant, by reproducing the Mark, was infringing the Plaintiff's exclusive rights in its artistic work. In response, the Defendant asserted the Plaintiff had no right to raise a copyright claim given that the Plaintiff had no proof that it had valid title to the copyright in the Logo.

Again, the Court was faced with a fundamental conflict in evidence, this time in respect of the author of the Logo. The Plaintiff's evidence was that one of its shareholder/directors created the concept or idea for the design in the early 1990's and created a rough sketch which resembles the present Logo. In contrast, Defendant claimed the Plaintiff's shareholder/director merely had but an abstract idea for the Mark² that did not attract copyright protection. The Defendant's evidence was that the independent Milano pizzeria operators all contributed to the cost of hiring a graphic designer to develop a logo to give a more uniform appearance among the independent operators and to use in group marketing efforts. The graphic designer prepared various logos which were put to a vote by the operators, who selected what ultimately became the design of the Logo. The Plaintiff's position was that it had hired the graphic designer, but only to create a polished version of the shareholder/director's design concept, and that it owned the Logo. The Defendants, however, insisted that there was never any discussion about ownership or licensing of the logo, or about any limitations concerning the operators' ability to reproduce and use the Logo as they saw fit.

So, as with the issue of whether the licence agreement existed, there was an incongruity of evidence on this point as well. However, unlike the issue of the licence agreement in which the Court considered it appropriate to have a trial on the issue, the Court dismissed the Plaintiff's copyright claim in its entirety.

Why? Because even if the Plaintiff's version of events was correct, that still did not give it standing to make a copyright infringement claim. The Plaintiff had failed to lead any evidence that the shareholder/director had assigned the copyright in the Logo to the Plaintiff and, moreover, did not allege that any such assignment had ever taken place. Thus the Plaintiff had no right to make a claim for copyright infringement as there was no evidence whatever that it owned any copyright in the Logo.

Why Written Assignments and Licenses of Copyright Matter: This scenario highlights the importance of licensors obtaining written assignments from the authors of the copyright-protected works which are licensed to others, particularly in light of the default copyright ownership regime in Canada. Under Canadian law, the author/creator of a work is generally the first owner of the copyright therein.³ The primary exception to that rule is where the work was made by the author in the course of her employment, in which case s.13(3) of the *Copyright Act* provides that the employer is the first owner of the copyright, subject to any agreement to the

² Ideas are not protected by copyright in Canada, rather it is the fixation of the idea in a work that gives rise to copyright protection.

³ S.13(1), *Copyright Act* (R.S.C., 1985, c. C-42) ("*Copyright Act*")

contrary between the author and employer.⁴ However, where the author is not an employee of the purported licensor but an independent contractor, ownership of the copyright will remain with the author unless and until the author assigns the copyright to the licensor in writing.⁵ The *Copyright Act* permits copyright to be assigned and that any interest in the right may be granted by licence, but provides that no such assignment or grant is valid unless it is in writing and signed by the owner of the right in which the assignment or grant is made.¹ Without such a written assignment, a non-employee author/creator retains the copyright in the work, including the exclusive right to produce and reproduce the work, together with the other bundle of rights which constitute copyright under Canadian law. A person who has procured the creation of a work from a non-employee contractor for good and valuable consideration but who fails to provide for a written assignment of the copyright may discover that she merely has an implied licence to use the work for the purpose for which it was intended, but not have any right to exclude others from producing or reproducing the work

Why Written Waivers of Moral Rights Matter: Good IP management in relation to works of authorship does not stop at the written assignment of copyright. Equally important is obtaining a written waiver of moral rights from the author. As soon as an author creates the work that is subject to copyright protection, the author automatically gains moral rights in that work. Under Canadian law, this means the author has: (1) the right to be associated with her work by name or pseudonym, where reasonable in the circumstances; (2) the right to remain anonymous; and (3) the right to the integrity of the work, which right is infringed if, to the prejudice of the honour or reputation of the author, the work is (i) distorted, mutilated or otherwise modified; or (ii) used in association with a product, service, cause or institution. An owner of copyright therefore needs to obtain the written waiver of moral rights from the author to ensure that the work can be used without any restrictions.

In summary, it is critical that a person owns the copyright in a work of authorship and who wishes to licence others to reproduce the work (the “Licensor”) ensure that all person(s) who created such works assign their copyright to the Licensor and waive their moral rights (in favour of the Licensor), in writing. Obviously, a Licensor’s ability to allow for uninhibited use and to enforce exclusivity is a major point of concern for Licensees, and a Licensor’s inability to do so will tend to significantly decrease the value of the relationship, particularly in a franchising arrangement.

(ii) *Trademark claim*

Turning to the trademark claims, the Plaintiff relied on its registered trademark for the Logo to pursue its claims for trademark infringement and depreciation of the value of goodwill in the registered trademark, and relied on its common law rights in the Logo in respect of its passing off claim. In response, the Defendant alleged that the Plaintiff’s registered trademark was invalid as it contravened the following provisions of the *Trademarks Act*:

⁴ Even though the *Copyright Act* provides that the employer is the first owner of the copyright in an employee’s work of authorship, as a matter of practice it is wise to paper the transfer with a confirmatory assignment (and waiver of moral rights) to preclude any argument that the s.13(3) was not operative in the circumstances, and to ensure that there is a documentary record for the purposes of introducing the transfer of the ownership into evidence.

⁵ S.13(4), *Copyright Act*.

- The Mark should never have been registered because it violated the s. 12(1)(a) prohibition on the registration of marks that are primarily a name or surname of an individual;
- The Mark should never have been registered because it violated the s. 12(1)(b) prohibition on the registration of marks that are clearly descriptive or deceptively misdescriptive of a place of origin of the services in association with which the mark is used; and
- The Mark should be invalidated pursuant to s. 18(1)(b) as the Mark lacked distinctiveness at the time of the counterclaim because it was no longer an indicator of a single source.

The Defendant further argued that the Logo was not distinctive and that the passing off claim could not succeed.

(1) Registrability of the Logo

The trademark application for the Logo was filed in 1997, and was finally registered in November 2002 “after some initial reluctance on the part of the Trade-mark Office to register the mark.” The Defendant alleged that because the word “Milano” is both primarily a name or surname and is also a the name of a city in Italy, it was not registerable as it triggered the two aforementioned s.12 prohibitions. Ultimately, the Court sided with the Plaintiff and did not consider the mark to have been unregistrable at the date of registration. The Court thus found in favour of the Plaintiff on this issue, and did not invalidate the trademark on the basis that it was unregistrable at the time of registration.⁶

(2) Distinctiveness of the Logo

The Defendant’s second line of attack was that the registration for the Logo was invalid because it was not distinctive of a single source. The Plaintiff maintained that a written licence agreement had indeed been executed and, although a flood had destroyed its only copy of that agreement, the existence of the licence was nevertheless established by the conduct of the parties. The Plaintiff argued that the distinctiveness of the Logo had been maintained by virtue of that licence agreement, as all of the Defendant’s pre-termination use of the Logo inured to the benefit of the Plaintiff. When the Plaintiff purported to terminate the Defendant’s licence in 2016, all subsequent use of the trademarks by Defendants was alleged to be an infringement of Plaintiff’s exclusive rights. In response, the Defendants claimed that there was never any licence, written or otherwise, and that there had been substantial long-term unlicensed use of the Logo (as well as the formative trademarks and trade names) by each of the independent Milano pizzeria operators, including the Defendant.

As a result of the Plaintiff’s inability to prove that the Defendant’s use of the Logo was under licence, the Plaintiff could not establish that the Logo had remained distinctive of a single source. The Plaintiff’s inability to proffer documentary evidence at its motion for summary judgment on the trademark infringement claim meant that it could not clearly show that the Defendants’ use of the trademark had ever been subject to a licence agreement pursuant to which

the Plaintiff had control over the character or quality of the Defendants' goods and services. Thus, there remained a live question as to whether the Plaintiff (by itself and through its licensees) was the only person using the trademark, both at the time the application for registration was filed and at the time the issue of distinctiveness was called into question by the Defendants. To the extent that there were in fact multiple users of the trademark not under licence from a single licensor, Plaintiff could not succeed in establishing that it was the person entitled to register the trademark in the first place. Thus, the Court held that the Plaintiff's claims of trademark infringement, depreciation of goodwill of the registered trademark and passing off were not suitable for summary judgment.

The lack of a written trademark licence agreement means that the question of the distinctiveness of the Plaintiff's trademark will now have to be resolved at a trial. A trial judge will have to hear live witnesses give evidence about whether a licence ever existed, and if so, if it included terms providing that the Plaintiff had control over the character and quality of the goods/services provided in association with the Logo by Defendant.

Why Quality And Control Provisions in a Trademark Licence Matter: In Canada, if a trademark is used by an entity other than the owner, the trademark's distinctiveness is impaired unless proper licensing provisions are in place which provide that the trademark owner has, directly or indirectly, control over the character or quality of the goods and services that are provided in association with the trademark. If a mark does not distinguish the goods and services of the owner from the goods and services of others, it cannot be afforded trademark protection under the law. An application for registration may be opposed on the ground that it is not distinctive, and a registered trademark may be invalidated if it loses its distinctiveness. Beginning June 17, 2019, the Registrar will be permitted to refuse registration on the basis that a trademark is not distinctive.

In *Milano Pizza*, because a live question remained as to whether the Plaintiff (by itself and through its licensees) was the only person using the Mark when the application for registration was filed and at the time the issue of distinctiveness was questioned by the Defendants, or whether there were in fact multiple users not operating under licence from a single licensor, the Plaintiff could not succeed in establishing that it was the person entitled to register the trademark in the first place. Thus, the validity of the trademark registration and, consequently, the issues of trademark infringement and depreciation of goodwill of the registered trademark that flow from the registration, were not suitable for summary judgment.

In short, the lack of a written trademark licence agreement containing terms that the Plaintiff has direct or indirect control over the character and quality of the goods and services sold by the independent operators' pizzerias left the Plaintiff vulnerable to the expungement of a Mark it had been using for decades.

4. Lessons learned: Pitfalls and Best Practices when Licensing

The facts of the case illustrate several pitfalls into which licensors can inadvertently stumble if not careful, including:

- failing to properly document the creation of, and the transfer of rights in, key works (logo designs, software, advertising materials, menus website content) for use by the licensees, leading to uncertainty concerning the ownership of (and therefore the ability to enforce) the copyright therein;
- selecting trademarks for use that may not be registrable under the requirements of the *Trademarks Act*; and
- letting others use trademarks without a written licence agreement. Under Canadian law, a trademark must identify a single source of origin of goods/services or the seat of control over the character or quality of those goods/services. If a trademark fails in that regard, it is not distinctive and cannot be afforded exclusivity. A mark that fails to distinguish its owner's goods/services from those of others is not protectable as a trademark under the common law and cannot be registered as a trademark. Moreover, a registered trademark that becomes non-distinctive may be invalidated, and may be struck from the register by the Federal Court.

Best practices to avoid the hazards highlighted by the *Milano Pizza* case include:

- ensure your licence agreements are in writing, contain quality control provisions if trademarks are at issue, and refer to the all trademarks (including common law marks) and copyright-protected works that may be used by licensee;
- take advantage of the *Trademarks Act* s. 50(2) public notice provisions, which create evidentiary presumptions that the mark is being used under a licence with sufficient character and quality control provisions if the mark is accompanied by language such as “Mark is owned by [insert name of trademark owner] and used under licence by [insert name of licensee]”;
- if your trademark is a design mark, register the copyright in the design mark as an artistic work with the Copyright Office;
- when selecting trademarks, particularly cornerstone marks that are intended to be used as core brands by franchisees or other licensees, obtain legal advice concerning the likelihood that you can obtain a registration before you start using the trademark. The value of a franchise system may depend on it.

¹ S.13(4), Copyright Act