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25-Year Battle Over Hard Rock Turns on Value of IP Assets

For years I have advised about how careful "buddies" need to be when they start on a business venture after meeting over a beer and writing down an agreement on a cocktail napkin!! This real live court story below affirms my warning.

***Okun v. Morton*, 2012 Cal. App. Unpub. LEXIS 201 (Jan. 11, 2012)**

Ten years after Peter Morton created the first Hard Rock Cafe in London in 1971, he made plans to expand into the United States, beginning with a restaurant in Los Angeles. Music industry maven Milt Okun expressed interest in backing the venture, and together, the two men executed a four-page agreement in 1982, creating a company that gave Morton an 80% ownership interest and Okun 20%.
Of particular note, one paragraph of the parties' agreement provided that Okun would have a right to participate in "all business opportunities" that came about in connection with the Hard Rock Cafe; if he declined the opportunity, then Morton would be free to exploit it in "any manner."

Three rounds of litigation. Okun first sued Morton in the 1980s for breach of their agreement. In resolving those claims, the federal district court (California) found that the parties intended to participate in any future investment schemes commensurate with their 80-20 ownership interests, conditioned on Okun's right of first refusal and his contribution of a proportionate share of expenses. In a second lawsuit, the court rejected Okun's claims for a share of Hard Rock management fees.
Soon after, Morton began raising funds to open a Hard Rock Hotel and Casino in Las Vegas. He offered Okun an option to invest at $1.96 million (his 20% share of expenses), but Okun declined and for a variety of reasons, this first attempt failed. Three years later, Morton partnered with a new casino operator (Harvey's). Okun asked to participate, but Morton refused, claiming Okun's prior decision not to invest in Las Vegas foreclosed his involvement now.
Okun sued Morton for a third time, but the court dismissed his claims as frivolous. "Morton owes no duty to Okun with regard to the Hard Rock Hotel and Casino" in Las Vegas, the court held. However, any future effort by Morton to "sell, convey, or license" the Hard Rock name would invoke Okun's right of first refusal and participation along the original 80-20 split.
In 1996, Morton sold all of the Hard Rock Cafe business assets, including its intellectual property, for $380 million, but retained the trademarks associated with the Hard Rock hotel and casino in the United States and other countries. Pursuant to the parties' 1982 agreement, Morton cut a check to Okun for nearly $48 million, or 20% of the deal (minus

expenses).With that, Morton said he was cashing Okun out of any further interest in Hard Rock trademarks.
In 2007, Morton decided to sell all of his remaining Hard Rock assets, including the Las Vegas hotel and casino and its land and all the trademark rights retained from the 1996 transaction. In an auction, the top bidder paid $770 million for the three bundled assets, succeeding to all licensing rights and becoming the sole shareholder in the Hard Rock Hotel and Casino in Las Vegas.

Okun sues for a fourth time. In 2007, Okun sued Morton once again for breach of the 1982 agreement, saying that he was entitled to 20% of the $69 million paid for the IP assets, which he claimed related to all trademark and branding rights outside of Las Vegas. Morton said that the "lion's share" of the $69 million was paid for the Las Vegas IP, however, to which Okun had no rights.
At trial before a special referee, Morton called two valuation experts. The first testified that the non-Las Vegas IP was worth anywhere from $0 to $13.2 million. The second believed that the "value of the rights outside of Las Vegas were so speculative and remote in nature that it was not possible to reliably conclude a fair market value," although he "hazarded" an estimate of $11.8 million.
The referee concluded that court documents supplied a "reliable quantification" of the $770 million purchase price, the referee found. In particular, the form 10-K specifically affirmed that the $69 million "was for *both* Las Vegas and non-Las Vegas IP," the referee said, and was particularly powerful proof, because the buyer had no stake in the current dispute. Based on this evidence, the referee rejected Okun's claim that he was entitled to a 20% share of the $69 million.
Instead, the issue became what portion of that amount was attributed to non-Las Vegas IP. Believing that Morton was "in the best position to evaluate the worth of the empire he built," the referee decided that $27.5 million—or the midpoint of the range that Morton gave in deposition—was the best indication of value and awarded 20% to Okun ($5.5 million), minus his share of the costs. Still not satisfied, Okun appealed the referee's decision.

Fruits of an 'ancient and relatively' trivial investment. As a preliminary matter, the appellate court confirmed that Okun was not entitled to any share of the Las Vegas IP. In Round 3 of the parties' litigation, the court determined that Las Vegas was "one opportunity that Okun elected to pass up" and that as a result, Morton was under no obligation to include him in any Las Vegas investment.
As a second matter, the court affirmed the referee's reliance on Morton's deposition testimony to value the non-Las Vegas IP assets. If anything, the referee gave Okun "the benefit of the doubt" by settling on the midpoint of Morton's valuation range instead of deferring to the lower amounts posited by his two valuation expert, and in an attempt to close the book on the parties' long dispute, the court rejected Okun's claims for prejudgment interest and ordered him to pay Morton's attorneys' fees.

This article originally appeared in the Business Valuation Update™ (BVU) newsletter. For information, please visit: www.BVResources.com

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