Unfair Competition In Advertising: Developments and Trends in Lanham Act Litigation

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THE PAST YEAR HAS SEEN A NUMBER of significant developments in false advertising litigation under the Lanham Act. Courts continue to limit claims based on standing. The Supreme Court's *Dastar* decision continues to raise issues concerning the application of the Lanham Act to advertising claims involving intellectual property rights. In addition, late 2007 brought a significant decision regarding court deference to National Advertising Division decisions.

This article summarizes major developments in this fast changing area, first, by discussing major trends, and second, by discussing two major cases from last year—DirecTV's battle with Time Warner over advertising for its high-definition satellite service, and the ongoing battle over the claim that McNeil Nutritional's SPLENDA product is "Made from sugar, so it tastes like sugar."

Standing

Over the past several years, an increasing number of courts have applied prudential standing limitations to bar false advertising actions under the Lanham Act. The most significant case last year was the Eleventh Circuit's decision in *Phoenix of Broward, Inc. v. McDonald's Corp.*[1] Phoenix of Broward, a Burger King franchisee, brought a purported class action against McDonald's seeking damages based on McDonald's advertising for its promotional games. These games were advertised as being "fair and equal." Due to fraud committed by the company McDonald's engaged to operate the games, there was no "fair and equal chance" to win high-value prizes, which were redirected to people affiliated with the contractor. The district court granted McDonald's motion to dismiss for lack of prudential standing.

On appeal, the Eleventh Circuit joined the Third and Fifth Circuits in holding that prudential standing limitations apply to Lanham Act false advertising claims. The court adopted the Third Circuit's *Comte Brothers* test for prudential standing and concluded that while Phoenix of Broward had alleged an injury stemming from the McDonald's advertisements and, as a competing franchisee, was likely to be injured by the advertisements, "the causal chain linking McDonald's alleged misrepresentations about one aspect of its promotional games to a decrease in Burger King's sales is tenuous, to say the least." The court also held that the damages were both remote and speculative and that apportioning damages between McDonald's many and various competitors would be excessively complex. Accordingly, Phoenix of Broward was found to lack standing.

In the Second Circuit, *ITC Ltd. v. Punchgini, Inc.*,[2] also reflects the continuing trend to limit standing. Plaintiff ITC operates a "Bukhara" restaurant in India, previously operated "Bukhara" restaurants in the United States, and sells "Dal Bukhara" packaged foods in the United States. The defendants operate their own "Bukhara Grill" restaurant in the United States. The plaintiff claimed that the defendants implied that their restaurant was affiliated with the plaintiff's products, and this constituted false advertising. The lower court dismissed these claims for lack of standing, and the Second Circuit affirmed.

First, the court stated that the plaintiff's mere plans to open "Bukhara" restaurants in the United States did not establish a protectable interest sufficient to support standing. Second, the court held that because the defendants were not comparing their restaurant to the plaintiff's packaged food products, the plaintiff's use of the "Dal Bukhara" name on such products did not provide it with standing to challenge the defendants' advertising. Finally, the court rejected the claim that the plaintiff's interests based on the operation of "Bukhara" restaurants overseas supported standing, as such activities were too remote to justify a U.S. court's intervention.

At the district court level, in *Alexander Mill Services, LLC v. Bearing Distributors, Inc.*,[3] the court rejected a Section 43(a) claim for lack of standing. Plaintiff AMS entered into a contract for BDI to supply AMS a centrifuge that met certain standards. After AMS began to use the centrifuge, AMS found that it did not meet those standards. Litigation ensued, with AMS claiming that BDI's representations about the centrifuge constituted false advertising under the Lanham Act. BDI moved to dismiss AMS's Lanham Act claim for lack of

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standing, and the district court granted the motion, finding that AMS lacked prudential standing under *Comte Brothers*. The court held that while AMS hoped to develop a business that competed with BDI, its injury resulted from its status as a consumer of BDI, rather than a competitor.

Similarly, in *Mugworld, Inc. v. G.G. Marck & Associates*,[4] the district court again recognized the need to show competition between the parties in order to support standing for a Lanham Act false advertising claim. Marck markets and sells mugs to a variety of customers, including Mugworld. Marck asserted a counterclaim alleging that certain Mugworld mugs were falsely labeled and packaged in violation of the Lanham Act. Unsurprisingly, the court rejected Marck's counterclaim for lack of standing, noting that "there is no competent . . . evidence that Marck and Mugworld are, or have ever been competitors."

These cases all indicate that courts are continuing to express skepticism about expansive standing under the Lanham Act, especially where customers or suppliers, rather than competitors, attempt to bring false advertising actions under Section 43(a).

The Fallout of *Dastar*

Another significant trend has been the continuing effort by courts to determine the extent to which *Dastar Corp. v. Twentieth Century Fox Film Corp.*[5] bars false advertising claims based on representations about intellectual property rights in a product. In *Baden Sports, Inc. v. Molten*,[6] the court refused to set aside a jury's finding that Molten's advertisement of a "Dual Cushion" basketball, which includes a sponge cushion layer between the skin of the basketball and the basketball's bladder, as "innovative" was false. Although some witnesses had taken the position that the "innovative" claim was false because Molten was claiming inventorship of the "dual cushion" technology, the court concluded that the essence of the advertisement was a claim that the basketball was "new," and, thus, the claim was not barred by *Dastar*.

Notably, however, in an earlier decision in the same case,[7] the court rejected Baden's claim based on Molten's advertising its product as "exclusive" or "proprietary." The court held that such representations did "not relate to the 'nature' or 'qualities' of Molten's products, but to the fact that Molten invented and owns the basketball technology." This pair of decisions illustrates that choice of words matters a great deal in determining actionability. While falsely advertising a product as "new" likely remains actionable, making representations that relate to exclusive rights in such a product may not be.

Similarly, in *Thomas Publishing Co., LLC v. Technology Evaluation Centers, Inc.*,[8] Thomas contended that TEC had "misrepresent[ed] that it is the developer, creator or owner of" a directory of software suppliers in various promotional materials. The court held that *Dastar* barred the action because the representations at issue concerned the authorship of the work, not its inherent characteristics, and the claim was little more than an effort to duplicate the copyright claim as a Lanham Act claim.

Finally, in *Pernod Ricard USA, LLC v. Bacardi U.S.A., Inc.*,[9] the court held that *Dastar* barred false advertising claims stemming from allegedly false representations about trademark ownership. Relying on *Dastar*, the court dismissed Pernod's claim that Bacardi's statements concerning ownership of the HAVANA CLUB mark in the United States constituted false advertising, finding that while representations about trademark ownership "may signal to a consumer that a product is of a certain quality or consistency, this is distinguishable from conferring actual information about the characteristics or qualities of the product as contemplated by § 43(a)."

In sum, courts are continuing to use *Dastar* to limit false advertising claims when those claims are based on a statement concerning ownership of or rights in intellectual property or a statement of inventorship.

Deference to the National Advertising Division

One of the more significant decisions in 2007 was *Russian Standard Vodka (USA), Inc. v. Allied Domecq Spirits & Wine USA, Inc.*[10] Russian Standard made claims in its advertising that it was the only true Russian vodka and that Allied Domecq's Stolichnaya vodka was not Russian. Allied Domecq challenged these claims at the National Advertising Division of the Council of Better Business Bureaus (NAD), an industry self-regulatory forum.[11] After the NAD challenge was fully briefed, Russian Standard sought a declaratory judgment in the Southern District of New York that would allow it to continue making the claims. It also sought damages and injunctive relief based on Allied Domecq's claims that Stolichnaya is "Russian." Under the NAD rules, cases that are the subject of litigation are outside of its jurisdiction, and the NAD suspended its proceeding after Russian Standard filed suit.

In response, Allied Domecq sought a stay of the federal suit to allow the NAD to complete its "inquiry." The court found that a stay was appropriate because

> allowing the NAD, a highly reputable institution, to provide its expert view on Stoli's authenticity as a Russian vodka would be extremely useful in resolving remaining claims in the complaint. The decision would promote judicial economy and be informative to the court in its own decision regarding the remaining claims. Furthermore, the NAD decision would promote settlement between the parties.

This holding makes it harder for an advertiser to avoid a NAD proceeding by filing an action for declaratory judgment. It also enhances the reputation of the NAD in federal court proceedings, as the court suggested it would likely follow the NAD's decision.[12]

What Constitutes Advertising

The question of whether something constitutes "commercial advertising or promotion" sufficient to give rise to a false advertising claim is often litigated. In *Midwest Canvas Corp. v. Commonwealth Canvas, Inc.*,[13] defendant sold plaintiff a concrete curing blanket. The invoice delivered with the blanket described it as being 25 mm thick, but the blanket was actually thinner, and plaintiff sued. The court rejected the Lanham Act claim, noting that the invoice was not actionable because "the goods accompanying a shipment have already been ordered by the consumer who needs no further inducement to buy them."

Similarly, in *Chamilia, LLC v. Pandora Jewelry, LLC*,[14] a case involving competitors "in the cutthroat world of charm bracelet design and manufacture," the court granted summary judgment to Pandora after concluding that its statements that Chamila was a "knock-off company" that produced "cheap imitations" of Pandora's products and that Pandora had patent rights in its products were made orally at trade shows and in letters sent to its authorized resellers, who were barred from selling competing products, and therefore did not constitute advertising. As the court put it, "If communications between two parties with an exclusive sales agreement inherently constituted commercial advertising and promotion under the Lanham Act, the parties to the agreement could never communicate to each other their opinions on when a breach had occurred without fearing liability under the Act."[15] In addition, the court found that the oral statements at trade shows were not actionable, as plaintiff only identified six statements, which was deemed to be de minimis.

Other Noteworthy Cases

While the cases discussed above illustrate trends, there were a number of other decisions of note. In *L & J.G. Stickley, Inc. v. Cosser*,[16] the Second Circuit remanded an injunction to the district court with orders to clarify that it barred only false or misleading references to the plaintiff's products, rather than all references to such products. This demonstrates that successful parties should carefully tailor the language of injunctions in order to limit the possibilities for appeal.

The opposite peril is demonstrated by the Third Circuit's decision in *Al C. Rinaldi, Inc. v. Bach to Rock Music School, Inc.*[17] In a 2001 settlement agreement, Bach to Rock agreed to cease making certain representations in "any television or radio advertisement, newspaper or magazine advertisements, promotion, circular or other document." When Bach to Rock continued to make the statements on the Internet, Rinaldi sought relief. The court concluded that since the agreement did not specifically address the Internet, it was not violated.

IDT Telecom, Inc. v. CVT Prepaid Solutions, Inc.,[18] demonstrates the risk in attempting to rely solely on the presumption of irreparable harm to support an injunction when the defendant is making false statements about its own products. The plaintiffs asserted that the defendants overstated the number of minutes available on their prepaid calling cards, and sought an injunction. The district court denied the motion for a preliminary injunction because money damages would adequately compensate for the loss. The Third Circuit summarily affirmed, making clear that plaintiffs must point to something beyond potential loss of market share to support injunctive relief.

Muzikowski v. Paramount Pictures Corp.,[19] demonstrates the difficulty of proving deception with anecdotal evidence. The plaintiff claimed that Paramount falsely advertised that its film *Hardball* was based on his life because of the use of an "inspired by a true story" tagline. In support of his claim, the plaintiff submitted eighteen affidavits from individuals who knew him and had seen the film asserting that they believed the film was based on his life. The district court found this fell "far short" of meeting the burden of showing likely deception, and granted Paramount's summary judgment motion. The court noted that although the film's character "Conor O'Neill" and Muzikowski had certain similarities, the differences in their names and character traits were so substantial as to undermine any claim. Also undermining Muzikowski's claim was that, at various times, he identified three different characters in the film as being based on him.

Procter & Gamble Co. v. Ultreo[20] demonstrates the perils of attempting to shield studies or surveys with a privilege claim. Procter and Gamble sought disclosure of five studies conducted by Ultreo concerning the efficacy of its power toothbrush. Ultreo asserted that the studies were privileged because they were commenced at counsel's direction due to the possibility of litigation. The court rejected this claim, finding that these studies were part of a continuing effort "to obtain clinical proof of the effectiveness of the ultrasound component of its toothbrush" that predated the litigation rather than having been conducted due to the possibility of litigation. In addition, the court noted that Ultreo had treated these studies no differently than those which had been conducted in the normal course of its business. Accordingly, the court held that "Ultreo has not met its burden to show that the studies would not have been prepared in substantially similar form but for the prospect of that litigation," and ordered them produced.

Thus, parties seeking to shield studies with privilege claims must ensure that it is clear to a court that the studies were prepared solely due to litigation and specifically at the request of counsel, rather than as part of the regular course of business. To assist in maintaining the privilege, such studies should be handled and held separately from any non-privileged studies performed by the company.

In *Doctor's Associates, Inc. v. QIP Holders, LLC*,[21] the operator of the Subway sandwich chain sued the operator of the Quiznos sandwich chain. Quiznos sponsored a contest inviting contestants to submit videos comparing Quiznos sandwiches to Subway sandwiches. Subway contended that the contest entries contained false advertising, and sued Quiznos. Quiznos moved to dismiss based on the Communications Decency Act's provision that "no provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content provider."[22] The court denied the motion, finding that whether the defense applied was a disputed question of fact, as the complaint alleged that Quiznos altered or provided material used in the videos. The case continues, with dispositive motions due in July 2008, and will likely generate a significant precedent on the scope to which companies can be held liable for false or misleading representations in user-generated content.

DirecTV—Keeping Litigation in the Picture

The battle between Time Warner Cable and DirecTV over DirecTV's advertising for its high definition satellite services heated up in 2007. Early in 2007, Judge Swain of the Southern District of New York issued a preliminary injunction against two television commercials and a series of Internet advertisements as literally false.[23] In the first commercial, Jessica Simpson proclaimed that "You're just not gonna get the best picture out of some fancy big screen TV without DirecTV. It's in 1080i." In the second television ad, William Shatner, as *Star Trek*'s Captain Kirk, declared that "With what Starfleet just ponied up for this big screen TV, settling for cable would be illogical." Both TV commercials ended with a narrator stating "For an HD picture that can't be beat, get DirecTV." The Internet ad in question was divided into two parts. One, "OTHER TV," was "so highly pixilated that it is impossible to discern what is being depicted." The other, "DIRECTV" presented a very sharp image. The ad invited viewers to click to "FIND OUT WHY DIRECTV'S picture beats cable."

On review of the injunction,[24] the Second Circuit quickly determined that the Simpson commercial was literally false, because programming in 1080i was available through cable providers as well as DirecTV. The Shatner commercial proved more complex for the court, because it made no express statement as to picture quality. The court, after considering Second Circuit precedent, found that the clashing precedent "compel[s] us to now formally adopt what is known in other circuits as the 'false by necessary implication' doctrine." The court concluded that it was not clearly erroneous for the district court to hold that the Shatner commercial's statement that "settling for cable would be illogical" "unambiguously implied the false claim that cable's HD picture quality is inferior to that of DIRECTV." Therefore, the court found that Time Warner was likely to succeed on the merits of its claims that the television ads were false.

The court came to a different conclusion about the Internet ads. Although DirecTV conceded that the depiction of "OTHER TV" in the ads did not accurately depict cable's quality, DirecTV asserted that the depiction constituted puffery. While the district court rejected the puffery defense, the Second Circuit disagreed, noting: "It is difficult to imagine that any consumer, whatever the level of sophistication, would actually be fooled by the Internet Advertisements into thinking that cable's picture quality is so poor that the image is 'nearly entirely obscure[d].'" Accordingly, the Second Circuit reversed the injunction against the Internet advertisements.

Finally, the court briefly addressed arguments on irreparable harm. The court first rejected DirecTV's contention that Time Warner could not rely on a presumption of irreparable harm since the ads did not reference it by name, noting that because Time Warner is the sole cable franchisee in many markets, the reference to "cable" would be understood as one to Time Warner. In addition, the court concluded that even though the Simpson commercial did not expressly refer to "cable," because "90% of households have either cable or satellite service. . . it would be obvious to consumers" that the claims were targeted at cable. Accordingly, the Second Circuit affirmed the grant of the preliminary injunction against the television commercials.

Sugar Wars

Among the most closely watched and hard-fought advertising cases in recent years is litigation stemming from the dispute between Merisant and McNeil over the use of the tagline "Made From Sugar, So It Tastes Like Sugar" on McNeil's SPLENDA artificial sweetener. The case was fully tried to a jury in Philadelphia in May 2007, but the parties settled shortly before the jury's verdict was read. Allegedly, settlement talks heated up after the jurors requested a calculator to assist their deliberations, indicating that they had found in favor of Merisant and were attempting to calculate damages.[25] While the settlement is confidential, both the timing of the settlement and media reports indicate that it was substantial.

Although the parties settled prior to the jury verdict, there were a number of significant decisions in the matter before trial. On March 2, the court denied the parties' cross-motions for summary judgment.[26] First, the court rejected McNeil's laches defense. McNeil launched Splenda in 2000, but Merisant did not sue until 2004. During that time, Merisant attempted to informally contact McNeil with its concerns, which were heightened when McNeil removed the additional tagline of "but it's not sugar" from its advertising. Because of the changing advertisements and other factual questions about McNeil's intent, the court rejected the laches argument.

Second, McNeil moved for summary judgment on the grounds that Merisant lacked evidence of consumer deception. McNeil contended that its tagline could not be perceived as false, and the only surveys Merisant presented related to McNeil's packaging, requiring summary judgment with respect to other uses of the tagline. The court found the surveys and their various potential interpretations raised a substantial question of fact about deceptiveness and denied the motion. Although the surveys only addressed the packaging, since the same "made from sugar . . ." tagline was present throughout McNeil's advertising campaign, the court found that the survey was probative with respect to all types of advertising.

Finally, the court rejected McNeil's motion for summary judgment on Merisant's claim for disgorgement of profits, finding that there were still substantial disputes of fact about McNeil's intention in using the challenged tagline and whether actual diversion of sales had occurred.

On the other hand, the court granted Merisant's motion for summary judgment rejecting McNeil's unclean hands defense. McNeil claimed that because Merisant attempted to promote its products as being "natural," it could not complain about McNeil's advertising. The court found that this defense did not apply, because "the defense of 'unclean hands' is not a mere 'they did it too' defense, but instead serves as a shield against a plaintiff's claims where the plaintiff has engaged in 'egregious misconduct.'" The court also rejected McNeil's attempt to base an unclean hands defense on Merisant's alleged advertising outside the United States, finding such material irrelevant. Furthermore, the court concluded that Merisant's advertising relating to its products' "natural" origins did not have a sufficient nexus to McNeil's claims to support the defense. Accordingly, the unclean hands defense was rejected as a matter of law.

Finally, the court dealt with a pair of *Daubert* motions concerning experts on "standards and customs in the marketing industry" and how the human body determines taste. In both instances, the court allowed the testimony, as the witnesses were qualified, and the testimony would likely be helpful to a jury.

In a pair of later opinions, the court dealt with various motions in limine filed by the parties. In the first,[27] the court declined to issue an order excluding all third-party statements evidencing confusion, but noted such evidence would not prove actual confusion. For instance, the court allowed evidence relating to *Today Show* anchor Ann Curry's on-air question whether Splenda was "more natural" than other products, but noted that this could not establish that Curry was actually confused about Splenda's origins.

In the second opinion,[28] the court ruled on various motions to preclude survey evidence. Although the court expressed doubts about the relevance of the first survey, which dealt with the reasons people switched from Merisant's product to McNeil's, it nonetheless denied the motion, noting that the survey's purpose was to rebut another survey that had not been challenged. On the second survey, relating to McNeil's evidence that the claims were not misleading, while the court expressly found it "far from perfect," it nonetheless allowed the survey. This illustrates courts' willingness to admit surveys even where there may be methodological flaws on the assumption that cross-examination can deal with the weaknesses in the survey.

Conclusion

The past year represented an interesting period in Lanham Act false advertising litigation. While prospective plaintiffs now face additional limitations on their claims through limitations on standing and through courts' willingness to bar claims under *Dastar*, plaintiffs also experienced significant victories in the DirecTV and SPLENDA cases. In addition, the *Russian Standard* decision both increases the profile of the NAD and makes it harder for parties to avoid NAD inquiries by filing suit. Neither plaintiffs nor defendants scored a knock-out blow, and both sides will continue to spar over future developments. ■

1 489 F.3d 1156 (11th Cir. 2007).

2 482 F.3d 135 (2d Cir. 2007).

3 2007 WL 2907174 (W.D. Pa. Sept. 28, 2007).

4 2007 WL 2446539 (E.D. Tex. Aug. 23, 2007) (dismissing Lanham Act causes of action).

5 539 U.S. 23 (2003) (finding that selling copies of material on which copyright had lapsed without attribution to creator of materials was not actionable as false advertising under Lanham Act § 43(a)).

6 2008 WL 238593 (W.D. Wash. Jan. 28, 2008).

7 2007 WL 2058673 (W.D. Wash. July 16, 2007).

8 2007 WL 2193964 (S.D.N.Y. July 27, 2007).

9 505 F. Supp. 2d 245 (D. Del. 2007).

10 523 F. Supp. 2d 376 (S.D.N.Y. 2007).

11 The NAD is an industry forum that allows both the Council of Better Business Bureaus and competitors to bring informal advertising challenges. While the NAD cannot order injunctive relief, voluntary compliance with NAD recommendations is common and the NAD regularly refers parties who decline to participate in challenges or who refuse to comply with NAD recommendations to the FTC.

12 *See also* BellSouth Telecommc'ns, Inc. v. Hawk Commc'ns, LLC, 2004 WL 1085324 (N.D. Ga. Apr. 12, 2004) (noting prior NAD finding as significant in granting preliminary injunction); Mead Johnson & Co. v. Abbott Labs., 41 F. Supp. 2d 879 (S.D. Ind. 1999), *rev'd*, 201 F.3d 858 (NAD decisions are persuasive authority on importance of consumer surveys); Abbott Labs. v. Gerber Prods. Co., 979 F. Supp. 569 (W.D. Mich. 1997) (citing NAD decisions in support of requirement that survey subjects be potential users of the product in question); Coca-Cola Co. v. Procter & Gamble Co., 642 F. Supp. 936 (S.D. Ohio 1986), *rev'd on other grounds*, 822 F.2d 28 (6th Cir. 1987) (NAD finding that ads not misleading weighed in favor of finding that ads are not misleading), AMF, Inc. v. Brunswick Corp., 621 F. Supp. 456 (S.D.N.Y. 1985) (enforcing settlement agreement requiring parties to submit disputes to NAD). *But see* Millennium Import Co. v. Sidney Frank Importing Co., 2004 WL 1447915 (D. Minn. June 11, 2004) (declining to enjoin advertising previously found to be misleading by NAD due in part to newly offered consumer surveys).

13 2008 WL 162757 (N.D. Ill. Jan. 16, 2008).

14 2007 WL 2781246 (S.D.N.Y. Sept. 24, 2007).

15 *Id.* at *9.

16 2007 WL 4171651 (2d Cir. Nov. 27, 2007).

17 235 Fed. Appx. 866 (3d Cir. 2007).

18 2007 WL 2980181 (3d Cir. Oct. 9, 2007).

19 477 F.3d 899 (7th Cir. 2007).

20 2008 WL 110245 (S.D.N.Y. Jan. 8, 2008).

21 2007 WL 1186026 (D. Conn. Apr. 19, 2007).

22 47 U.S.C. § 230(c)(1).

23 475 F. Supp. 2d 299 (S.D.N.Y. 2007).

24 497 F.3d 144 (2d Cir. 2007).

25 http://www.msnbc.msn.com/id/18618557/.

26 515 F. Supp. 2d 509 (E.D. Pa. 2007).

27 242 F.R.D. 303 (E.D. Pa. 2007).

28 242 F.R.D. 315 (E.D. Pa. 2007).