

I N S I D E T H E M I N D S

Recent Developments in Advertising Law

*Leading Lawyers on Applying Traditional
Laws and Policy Guidance to Emerging
Technologies and Advertising Media*



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Efficiently Stopping False or Unsubstantiated Competitive Advertising

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Introduction

Comparative advertising has evolved dramatically over the years. When we were young, ads would feature comparisons to “Brand X.” Those generic comparisons have morphed into ads showing comparisons to specific plastic storage bags that leak, brand name shavers that do not work properly, and household name batteries that die while your daughter is playing with her favorite toy. Advertising can also omit reference to any product, but still be deemed competitive with claims such as “the most effective,” “the fastest,” or the “best price.”

Just as competitive advertising has continued to evolve, so too have the legal tools advertisers can utilize to challenge claims that may be false, deceptive, or unsubstantiated. Deciding which avenue to pursue depends on a number of factors, including budgets, goals, and timeframes, which we will explore below.

False Claims by Competitors

What are your legal options if you believe that a competitor’s advertising is false, unsubstantiated, or unfairly denigrating to your company?

One option is to send a cease and desist letter, which is an informal way to proceed. The letter can be sent by an attorney or by the company itself advising the competitor as to its issues of concern. One benefit of the cease and desist letter is that it provides notice to the competitor which could come into play if there is ultimately litigation and the competitor’s conduct is found to be unlawful. A cease and desist letter may demand a time for a response or remedial action and may also demand certain things such as the payment of damages. The primary benefits of this option are that it is relatively inexpensive and quick, puts the advertiser on notice of the violation, and that it can be used with other options, discussed below. The primary drawback of the cease and desist letter is that there is no enforcement mechanism and it requires voluntary compliance by the competitor or further action by the advertiser.

Another option is to refer the competitor to the appropriate government agency for enforcement, such as the Federal Trade Commission (FTC). This is an inexpensive method and may well have its desired effect of

changing the competitor's conduct. This method can be used in connection with other options such as a cease and desist letter or commencing a lawsuit, but there are also a number of drawbacks to this approach. Most importantly, it cedes control to the regulatory agency and the challenger loses control of the ability to seek or force enforcement. In addition, any enforcement may be industry-wide, which could result in unintended consequences, such as broad changes to a particular industry. In addition, there is no set timeline for enforcement once a matter is referred to a regulatory agency, there may never be any action by the regulator, and given privacy issues, you may never know if the government acted at all.

The two primary remedies available to an advertiser that wants to challenge the claims of its competitor, however, are to bring an action in federal court or a challenge before the National Advertising Division of the Council of Better Business Bureaus (NAD). In determining which of these forums is most appropriate for a given challenge, there are various considerations that should be taken into account including the advertising claims at issue; the availability of damages; costs; the time involved before a decision is rendered; confidentiality and press coverage; the need for discovery; risk of counterclaims (particularly in light of the advertiser's own business practices); and the remedies sought.

Federal Court

The Lanham Act governs false advertising cases along with trademark and trade dress claims.¹ Specifically, Section 43a of the Lanham Act is what governs false advertising cases. In relevant part, § 1125(a) provides that:

“Any person who, on or in connection with any goods or services, or any container for goods, uses in commerce any word, term, name, symbol, or device, or any combination thereof, or any false designation of origin, false or misleading description of fact, or false or misleading representation of fact, which—”

...

¹ 15 U.S.C. §§ 1051 *et seq.* (2002).

(b) *in commercial advertising or promotion, misrepresents the nature, characteristics, qualities, or geographic origin of his or her or another person's goods, services, or commercial activities, shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act.*" (emphasis supplied.)

As you can see, the Lanham Act's focus is a false or misleading description of fact or a false or misleading misrepresentation of fact in an advertisement that misrepresents the nature or the characteristics or qualities of either the advertiser's product or another's product. The most important thing to consider here is that to succeed on a Lanham Act claim you must demonstrate that the advertising is actually false, or that the claim, while true, nonetheless misleads or is likely to confuse consumers.

The five elements you have to prove to succeed on a Lanham Act case for false advertising are:

- A false or misleading statement of fact in a commercial advertisement about a product;
- That the statement deceived or had the capacity to deceive a substantial segment of potential consumers;
- That the deception is material and likely to influence a consumer's purchasing decision;
- The product is in interstate commerce; and
- The plaintiff has been or is likely to be injured as a result of the statement.²

NAD

A potential alternative forum to Federal Court, and one that is increasingly utilized by challengers, is the NAD. The NAD is an influential forum for resolving advertising disputes. Participation by both the advertiser and the challenger is voluntary. However, as we will discuss below, there is a very high compliance rate with NAD decisions because

² See, e.g., *Skydive Arizona, Inc. v. Quattrocchi*, 673 F.3d 1105 (9th Cir. 2012) (upholding District Court's granting of summary judgment as to false advertising claim where subject claims were found to be false, misleading and where a consumer declaration demonstrated that consumer was misled.).

there is a serious risk of referral to the appropriate government agency for non-participation or for failure to comply with a NAD decision.

Any person or entity, including the NAD itself as part of its own ongoing monitoring, can issue a complaint regarding national advertising. There are no formal pleadings, but rather, a challenge typically consists of a letter to the NAD that sets forth the basis of the challenge, relevant NAD or FTC precedent, and any expert opinion or consumer survey evidence that it believes supports the basis for the challenge. If the NAD decides that it has jurisdiction to hear the dispute, it will accept the challenge and forward it to the advertiser for its opposition. The advertiser's response is due within fifteen business days after receipt. In its response the advertiser must set forth its substantiations for the challenged claims and provide all relevant advertising that is related to the campaign. Upon receipt of the advertiser's opposition, the challenger can choose to waive a reply or, more commonly, to submit a reply within ten business days of the advertiser's response. In that case, the advertiser is permitted the equivalent of a sur-reply within ten business days. While extensions of the various briefing deadlines are commonly agreed to, lengthy extensions are not and, as discussed below, the entire NAD process from commencement of the challenge to decision is usually complete within six months.

Once all letter briefs are submitted, each side attends a meeting with the NAD. Typically, the NAD staff attorney that is responsible for the matter and either the head of NAD or a senior supervising attorney will attend on behalf of NAD. Anyone can attend on behalf of a party including business people, attorneys, and experts. The meetings are *ex parte* and, while not formal hearings, they are serious and important with the primary purpose of explaining your position and to answer any questions that the NAD may have. Typically, the challenger meets with the NAD first and the advertiser meets with the NAD last, and after both meetings are complete, the NAD issues its decision, which it strives to do within a few weeks of the final meeting. The NAD's decision will include discussions of the parties' positions, prior NAD decisions that are applicable, and a recommendation at the conclusion. The recommendation may be to discontinue all of the challenged claims, some of the claims, or none of the claims. If the NAD determines that at least some of the claims should be discontinued, the advertiser is required to submit a statement of no more than one page and

must indicate whether the advertiser agrees to modify or discontinue the challenged claims, whether or not it intends to appeal the decision, or whether it will abide by the NAD's recommendations. NAD matters are confidential until the NAD has issued its decision publicly (each party must sign a confidentiality agreement with the NAD). After the NAD receives the advertiser's statement, it will make the decision available to the public through press announcements and through its own published case reports.

Federal Court vs. NAD: Factors to Consider

Decision Maker

While federal judges are generally hard working and highly capable, the judge in any particular case may have very limited experience in handling false advertising cases and limited bandwidth to devote to any one particular case, since many federal judges are extremely busy and are burdened by a backlog of cases of all different types. Another factor to consider is that the judge is not going to be the fact finder for all issues, many of which are likely to be tried by a jury.

The NAD, on the other hand, is staffed by attorneys who specialize in hearing advertising disputes, including attorneys who have years, and in some cases decades, of experience handling substantiation and false advertising claims. One practical consideration to bear in mind is that since the NAD is a body with specialized expertise, it often uses its own experience in evaluating advertising. In particular, the NAD often steps into the shoes of the consumer to determine what it believes are the express and implied messages that are conveyed in an advertisement.

Burden of Proof

In a false advertising case under the Lanham Act, the burden is squarely on the plaintiff to prove each of the five elements of its claim by a preponderance of the evidence. A related but important consideration in federal court is that the focus is on false and misleading advertising. There is no claim for merely unsubstantiated claims. By contrast, in an NAD proceeding, the burden of proof is on the advertiser to substantiate all

reasonable interpretations of the claims made in its advertisement. This includes not just the claims the advertiser intends to convey but any claim or message that can be considered reasonably conveyed to a consumer. In an NAD proceeding, the initial burden is on the advertiser to show that it had a reasonable basis to make the claims in the first place. To the extent that the advertiser shows that it had a reasonable basis, the burden will then shift to the challenger to show that the advertiser's evidence is somehow fatally flawed or that the challenger processes better or more persuasive evidence.

Discovery

In federal court, both parties will have access to the full gambit of discovery and may serve document requests, interrogatories, and requests for admission, and may also take deposition testimony. Discovery will also be available from third parties via subpoena. The availability of discovery may be helpful if you are a plaintiff in a false advertising case but the scope of discovery and the usual discovery disputes that are common in litigation may greatly add to the costs involved.

There is no discovery process in an NAD proceeding. As a result, the process is much quicker and less costly. Of course, a plaintiff will not be able to find information supporting its case in discovery and will generally be limited to using publicly available information such as the advertisements themselves, and possibly, a consumer perception survey or expert report to put together a persuasive challenge.

Speed of Resolution

A federal court litigation from complaint through a final trial on the merits can easily take a year or two. As discussed above, a party can generally expect an NAD decision within approximately six months from commencement of the challenge.

Counterclaims

Counterclaims are permitted in federal court, and a party that brings a false advertising claim should anticipate and expect them. NAD Rule 2.5 expressly

provides that the advertiser may not include a counter challenge in its response. One practical consideration here is that even though the rules preclude an advertiser from interposing counterclaims, there is often a tendency on the part of an advertiser to raise issues with the challenger's own advertisements in the form of its defense. In our experience, however, the NAD does not view this as a persuasive defense. The NAD's sole focus is on the challenged claims and whether the advertiser can substantiate them. To the extent that an advertiser does have problems with the challenger's own advertisements, it is free to commence its own NAD challenge, and the NAD will review those claims in connection with that proceeding.

Costs

Litigation in federal court can be very expensive, particularly as it relates to discovery. In the digital age, the volume of possibly relevant emails and other electronic documents is often substantial and requires a party to spend a great deal of time (and, therefore, attorneys' fees) to collect and review them. In addition, there are many steps in federal court prior to trial including motions to dismiss and motions for summary judgment that greatly contribute to the costs of litigating in court. The costs associated with an NAD proceeding are comparatively modest.

Potential Remedies

There are a variety of remedies available in a false advertising case in federal court. First, there is the possibility of obtaining a temporary restraining order or preliminary injunction where the plaintiff can demonstrate, among other things, that it is likely to suffer irrevocable injury if the relief is denied and there is a substantial likelihood of success on the merits. These are extraordinary remedies, however, that are rarely granted except in the most egregious cases.³ In the false advertising context, examples of remedies that can be sought by preliminary injunction include secession of the challenged advertising, product recall, and corrective advertising. Other federal court remedies are monetary damages in the form of plaintiff's damages or, if the

³ See, e.g., *Euro-Pro Operating LLC v. TTI Floor Care N. Am.*, CIV. A. 12-10569-DJC, 2012 WL 2865793 (D. Mass. July 11, 2012) (preliminary injunction denied).

conduct was willful, the defendant's profits.⁴ If the defendant's conduct is found to be willful, a plaintiff may, in an exceptional case, obtain treble damages and attorney's fees. However, these are difficult to obtain.⁵ Also, with a federal court decision, the plaintiff will have a binding, published, enforceable decision that is backed up by the power of contempt and serious sanctions if the competitor does not comply.

In an NAD challenge, the challenger's remedy is limited to a finding that the advertiser needs to either discontinue its claims or modify them.⁶ Other remedies, such as monetary damages and injunctive relief, will not be available.

While the NAD process is voluntary, it nonetheless has an extremely high compliance rate largely because the NAD will refer the matter to the appropriate regulatory agency for failure to participate in the process or to comply with the decision. Many regulatory agencies, such as the Federal Trade Commission, will give referrals from the NAD the highest investigatory priority, meaning that an NAD case will be immediately assigned to an attorney and will be looked at very closely. A number of companies, including high-profile companies, have lived to regret failing to comply with NAD recommendations. For example, Reebok, with respect to its Shape Up shoes, failed to comply with NAD recommendations regarding its advertising. This failure resulted in a referral to the FTC. The FTC investigation culminated in a high-profile consent order and a \$25 million payment. Similarly, the popular dietary supplement Airborne failed to comply with the NAD's recommendations. A referral to the FTC resulted in a high-profile settlement and a \$30 million payment. There are a number of other high-profile and lesser known examples. The bottom line is that failing to comply with the NAD's recommendations will often be significantly more painful than not.

⁴ *Munchkin, Inc. v. Playtex Prods., LLC*, 40 Trials Digest 15th 4, 2012 WL 471066 (C.D. Cal.) (\$13.5 million dollar verdict for false advertising found to be knowingly and willfully false).

⁵ *See, e.g., Fishman Transducers, Inc. v. Paul*, 684 F. 3d 187 (1st Cir. 2012) (no damages despite finding that advertising was false).

⁶ *See, e.g., Bank of America Corporation (1-2-3 Cash Rewards Advertising Campaign)*, Report No. 5465, *NAD Case Reports* (May 2012) (NAD recommended that "Bank of America modify its 1-2-3 Cash Rewards Credit Card advertisements to disclose, in a clear and conspicuous manner, in the four corners of the advertising where the main claim appears, that the 2% and 3% bonus rewards have a combined spending limit of \$1500 per quarter.")

Conclusion

As marketers continue to push the envelope on advertising claims, a dissatisfied competitor has a number of options available to it. Federal courts can provide a powerful approach to address false advertising and obtain discovery and potential monetary damages. The NAD, however, can provide the ability to stop false advertising relatively quickly and cost effectively. Professional, experienced guidance can help a challenger select the proper course and implement a cost-effective, results-oriented challenge. While a lawsuit in federal court remains a viable option for some false advertising disputes, competitors are increasingly taking advantage of the cost-effective and specialized forum of NAD for such disputes.

Key Takeaways

- Assist the client in challenging advertising claims that may be false, deceptive, or unsubstantiated.
- Decide which avenue to pursue and consider a number of factors, including budgets, goals, timeframes, and requested remedies.
- Consider sending the client's competitor a cease and desist letter as to its issues of concern. Sending this letter provides notice to the competitor that could come into play if there is ultimately litigation and the competitor's conduct is found to be unlawful.
- Consider referring the competitor's actions to the appropriate government agency for enforcement, such as the Federal Trade Commission (FTC). This is an inexpensive method and may help change the competitor's conduct. But remember that this approach cedes control to the regulatory body and could result in industrywide enforcement.
- Keep in mind that federal courts can provide a powerful approach to address false advertising and obtain discovery and potential monetary damages. The NAD, however, can provide the ability to stop false advertising relatively quickly and cost effectively. Help your client select the proper course of action and implement a cost-effective, results-oriented challenge.

Andrew B. Lustigman is the chair of Olshan's Advertising, Marketing and Promotions Practice Group. He has a respected national practice and has been consistently recognized by Chambers and Partners USA as a "Notable Practitioner" in the area of advertising law. He has nearly two decades of experience handling false advertising disputes, including in federal and state court. He has an extensive practice before the National Advertising Division of the Better Business Bureau involving a wide-variety of consumer and business goods and services. He has handled innumerable investigations and litigation by regulators and consumers alleging claims of false advertising including advertising-related investigations and litigation brought by federal and state regulatory agencies, including the Federal Trade Commission, the Food and Drug Administration, the Federal Communications Commission, the United States Postal Service, the United States Senate, state attorneys general and other governmental organizations. Chambers and Partners USA reported that with respect to Olshan's practice - "Clients draw attention to the group's fantastic track record in defending ... false advertising challenges from competing businesses."

Howard J. Smith is a Partner in the firm's Litigation Department and the Advertising, Marketing and Promotions Practice Group. As a member of Olshan's Advertising, Marketing and Promotions Practice Group, Howard has represented a number of major corporate entities in connection with challenges before the National Advertising Division. He has also represented a consumer product good company involving claims of false advertising and an entertainment company involving privacy issues before the Children's Advertising Review Unit.

In addition, Howard is an experienced commercial litigator and has handled a number of Lanham Act false advertising and intellectual property matters in federal court including obtaining dismissal of all claims against his client in a "bet the company" trademark dispute. Recently, he successfully prosecuted breach of contract and copyright and trademark infringement claims for a major entertainment company.



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