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LITIGATION & DISPUTE RESOLUTION

False advertising challenges in the US: a potential alternative to courtroom litigation

ANDREW LUSTIGMAN

OLSHAN FROME WOLOSKY LLP

Advertisers want a level playing field on which they can compete. Businesses that advertise in the United States are frequently troubled by the advertising practices of their competitors. These responsible businesses know that their competitors have crossed the line in making claims that are either contrary to regulatory standards or their competitors likely lack substantiation for their claims. In some instances, the businesses feel that they are being unfairly denigrated in competitor advertising.

The traditional concept of addressing unfair business practices by filing suit – while powerful in its potential remedies and opportunities for discovery of the facts behind an opponent's practices – has significant drawbacks. These include the time and cost of litigation, exposure to counterclaims, and overcrowded court dockets with judges and juries that may fail to appreciate the nuances behind advertising practices. An alternative exists that has garnered increasing acceptance by US advertisers that want an intelligent, cost-effective, quicker and powerful remedy – initiating challenges before the self-regulatory bodies under the Advertising Self-Regulatory Council.

OLSHAN

Andrew Lustigman is a partner at Olshan Frome Wolosky LLP. He can be contacted on +1 (212) 451 2258 or by email: alustigman@olshanlaw.com.

False claims by competitors

It is an unfortunate reality that advertising which unfairly pushes the envelope exists in virtually every industry – ranging from health and beauty products, cleaning aids, cellular services, automobile performance, to financial services. As an example, of a number of recent cases, enrollment and use of reward credit cards remains a fiercely competitive marketplace. Assume the business is a financial services company that markets its US consumer and small business reward credit cards consistent with standards promulgated by the Office of Comptroller of the Currency and the Federal Trade Commission. In this hypothetical example, a financial services company's competitor makes unsupportable claims that its financial services aimed at that same target audience offer the most rewards or more rewards than its competitors, although it does not specifically name the business' product. The business wants the competitor to stop its false and unfair practices.

First, the unhappy competitor decides to send a cease and desist letter to the competitor. The letter outlines the business' concerns and demands cessation of the offending advertising and potentially other requests for relief. One benefit of a cease and desist letter is that it is relatively inexpensive and provides the opportunity for a dialogue on the advertising issues with the competitor. The letter also puts the competitor on notice which could be helpful in showing intentional misconduct should the practice continue and litigation is initiated. While a cease and desist letter is not an exclusive remedy, there is no enforcement mechanism associated with the letter itself and any potential change promised by the advertiser.

The business considers referring the competitor to the appropriate government agency for enforcement, such as the Office of the Comptroller of the Currency or the Federal Trade Commission. This is an inexpensive method and may well have its desired effect of changing the competitor's advertising. Like a cease and desist letter, referring the offending conduct to a regulator need not be exclusive. However, governmental involvement is difficult to garner. Moreover, it may result in the adoption of unfavourable industry standards.

Having decided against referring the matter to governmental authorities, the business considers a more formal mechanism. One option is to file suit in federal court under the Section 43(a) of the Lanham Act and perhaps a state law equivalent. The business also considers the alternative of filing an advertising challenge before one of the self-regulatory divisions under the Advertising Self-Regulatory Council (ASRC), such as the National Advertising Division (NAD). There are a number of important considerations to evaluate to determine the most appropriate forum.

Federal Court

The business evaluates filing a lawsuit in federal court. Section 43(a) of the Lanham Act provides competitors with a civil remedy for false advertising practices by others. This section of 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. To succeed on a Lanham Act claim the plaintiff must prove by a preponderance of the evidence that the advertising is actually false, or that the claim, while true, nonetheless misleads or is likely to confuse consumers.

There are five elements a plaintiff

must prove to succeed on a Lanham Act case for false advertising: (i) a false or misleading statement of fact in a commercial advertisement about a product; (ii) that the statement deceived or had the capacity to deceive a substantial segment of potential consumers; (iii) that the deception is material and likely to influence a consumer's purchasing decision; (iv) the product is in interstate commerce; and (v) the plaintiff has been or is likely to be injured as a result of the statement.

Importantly, there is no claim for merely unsubstantiated claims.

To prove or defend its claims, 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. Discovery has its benefits and its drawbacks, including the high cost of electronic discovery and the distraction it creates with both sides' business operations.

A competitor that brings a false advertising claim should anticipate that it will likely be served with a counterclaim by the challenged advertiser, taking issue with the plaintiff's own advertising. This will undoubtedly result in further expense and complication of the issues.

Plus, a plaintiff should consider who is going to decide the issues. While federal judges are highly capable, the judge in any particular case may have very limited experience in handling false advertising cases. 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 decided by a jury comprised of lay persons who may not understand technical issues.

NAD – an alternative approach

The challenger considers a potential alternative forum, such as NAD, one of four self-regulatory forums under the ASRC umbrella. The ASRC operates under the Council of the Better Business Bureaus. The other bodies are the Children's Advertising Review Unit (CARU), which by its name focuses on advertising and business practices directed at children; the Electronic Retailing Self-Regulatory Program (ERSP), which is focused on direct marketing practices such as infomercials and internet advertising; and the National Advertising Review Board (NARB), an appellate division for these divisions.

NAD challenges are evaluated by experienced attorneys who specialise in hearing advertising disputes. Since NAD is a body with specialised expertise in evaluating advertising, it often steps into the shoes of the reasonable consumer to determine what it believes are the express and implied messages conveyed in a challenged advertisement.

Any person or business can commence a challenge with NAD regarding a national advertiser's claims or practices. Typically a challenge is initiated by sending a letter to NAD that sets forth the basis of the challenge, relevant precedent, any expert opinion or consumer survey evidence that supports the challenge, and paying a filing fee (the amount of which varies depending on the gross revenue of the challenger and is in the range of $15,000-$25,000). The challenger must agree to keep the process confidential and not publicise the decision for its pecuniary benefit. If NAD decides that it has jurisdiction to hear the dispute, it will accept the challenge and forward the letter to the advertiser for its opposition.

The advertiser's response is due within 15 business days after receipt. In its response the advertiser must set forth an explanation as to the validity of its claims, including the support or substantiation for the challenged

claims. In an NAD proceeding, the burden of proof is on the advertiser to prove that it had, at the time the advertising was made, a reasonable basis for the express and implied claims in the challenged advertising. 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.

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.

A challenger can choose to waive a reply or, more commonly, to submit a reply within 10 business days of the advertiser's response. In that case, the advertiser is permitted the equivalent of a sur-reply within 10 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.

There is no discovery process in an NAD proceeding. As a result, an NAD proceeding is much quicker and less costly than a traditional lawsuit. However, a challenger must develop its own factual record, such as initiating a consumer perception survey or working with a qualified expert to prove its case and not rely on what it may find in the files of its competitor.

Counterclaims are not permitted at NAD. If an advertiser believes that the company that initiated the action's advertising is problematic, its remedy is to file its own separate challenge.

Once all letter briefs are submitted, each side attends a meeting with 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. 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 the side's position and to answer any questions that NAD may have. Usually a few weeks after both meetings are complete, NAD issues its decision. The decision presents an evaluation of both sides' positions and recommendations for future advertising on the challenged claims. NAD's recommendation may be that the advertiser has supported its claims or that some or all of the challenged claims must be discontinued.

If NAD determines that at least some of the claims should be discontinued or modified, the advertiser is required to submit a statement that it will or will not abide by NAD's decision. After NAD receives the advertiser's statement, it makes the decision available to the public through press announcements and through its own published case reports on its website.

If a party is dissatisfied with NAD's decision, it can appeal to the NARB, which similarly operates under the ASRC. An advertiser can appeal as a matter of right while a challenger must seek permission. Notably, the NARB rarely, if ever, disagrees with NAD's findings.

The bottom line comparison

A business that initiates a federal Lanham Act action must be prepared for a long and expensive battle to litigate the matter through discovery and trial, as well as counterclaims. NAD's costs (including the filing fee) are relatively modest because the process is limited to essentially two letter briefs and a meeting per side. There is no discovery and counterclaims are not permitted.

An important distinction between the two forums is the remedy. Both

forums offer the prevailing plaintiff/challenger essentially an injunction barring future false advertising. In the case of the federal forum, this would be in the form of a court-ordered injunction backed by the power of contempt. NAD relies on the parties' voluntary compliance. However, if a non-prevailing advertiser does not comply, NAD (typically at the request of the challenger), will refer the matter to the appropriate government agency. A number of these agencies, most notably the FTC, have agreed to give NAD referrals high investigatory priority. Thus, although participation at NAD by both the advertiser and the challenger is voluntary, there has historically been a 95 percent or more compliance rate.

While NAD offers a powerful *de facto* injunction it does not offer a prevailing challenger monetary damages or attorney's fees. On the other hand, in a Lanham Act action, a federal court can award a plaintiff's lost damages or, if the conduct was willful, the defendant's profits. In exceptional cases where an advertiser's conduct is found to be willful, a plaintiff may be awarded treble damages and attorney's fees. However, all monetary damages under the Lanham Act are difficult to obtain.

Conclusion

A business whose competition is engaging in false or unsubstantiated advertising has a number of options in the United States. While filing suit may on its face be the most powerful, that may not be the case when all elements are considered. Indeed, advertisers have increasingly found that the self-regulatory forums under the ASRC offer competitors the chance to obtain a level playing field at a modest cost and exposure. ■