Daily Journal

Federal Circuit Rewrites Fraud Standard

The Court of Appeals for the Federal Circuit has finally considered and rejected the "knew or should have known" standard that the Trademark Trial and Appeal Board has used for the past six years in inter partes cases where fraud has been asserted against a trademark registrant. As a result of the Federal Circuit's order in *In re Bose*, the party asserting fraud will need to show that the party accused of fraud acted with the subjective intent to deceive the Trademark Office.

The tough new standard is an abrupt change from the standard that has been used by the Trademark Trial and Appeal Board for the past six years since the its's decision in *Medinol Ltd. v. Neuro Vasx, Inc.* The *Medinol* decision was significant not merely because it clearly set a lower standard to prove fraud, it was significant also because it changed the way inter partes disputes are litigated in the Trademark Office, with fraud counterclaims suddenly being raised defensively in countless opposition proceedings, just as the fraud issue had been raised in *Medinol*.

The *Medinol* case started as a typical opposition, with the registrant relying on a prior registration to oppose a later-filed application. Rather than merely argue that there was no likelihood of confusion between their marks, the applicant went on the offensive and filed a counterclaim seeking to cancel the registration on the basis of fraud. The applicant contended that the registration was invalid because the registrant had committed fraud by filing a statement of use attesting to the fact that the mark had been used on *all* items included in the underlying application, when, in fact, it had been used on only one of the two items included in that application. Much to the surprise of many in the trademark community, the Trademark Trial and Appeal Board agreed with the applicant and held that the filing of the incorrect statement of use constituted fraud and that the registration was void in its entirety, and ordered the registration cancelled.

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The fraud standard used by the Trademark Trial and Appeal Board in the *Medinol* case departed significantly from the common law tort of fraud.

The Trademark Trial and Appeal Board held that a challenger was not required to prove a subjective intent to defraud the Trademark Office. Instead, recognizing that subjective intent is difficult to prove, the Trademark Trial and Appeal Board held that fraud would lie wherever a challenger could show that a registrant made a statement that it "knew or should have known" was false. Since then, fraud claims have been raised defensively in numerous opposition and cancellation proceedings, and nearly all have been successful. Virtually no defense raised by a trademark registrant has been sufficient to overcome an allegation of fraud concerning a false use allegation, including claims of inadvertence, lack of knowledge, inability to understand English, lack of representation by legal counsel, and ill health.

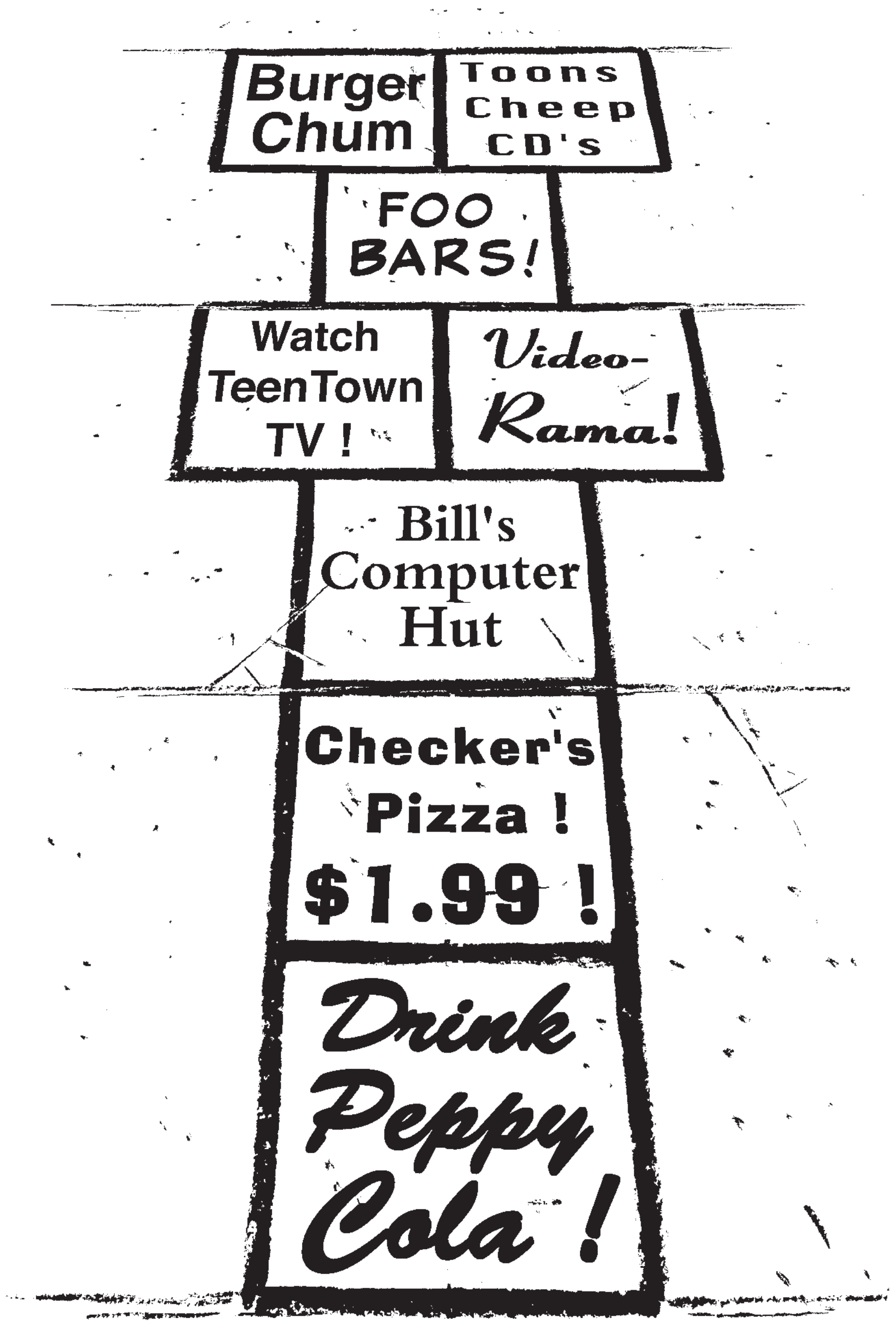
Although the Trademark Trial and Appeal Board lowered the standard to prove fraud in trademark cancellation actions, its standard was not adopted by any circuit court. In the 9th Circuit, for example, a challenger is required to prove that the registrant acted with scienter in order to cancel a registration. While similar standards have been applied in other circuit courts, until last month's decision in *In re Bose*, it was not known what standard the Federal Circuit, which hears all appeals from Trademark Trial and Appeal Board proceedings, would use when fraud is raised in trademark cases. The court's Aug. 31, 2009 order, however, could not have been clearer. The Federal Circuit firmly rejected the Trademark Trial and Appeal Board's "knew or should have known" *Medinol* standard as too low, and, in its place, held that fraud can only be found if an applicant or registrant knowingly makes a false, material representation with the intent to deceive the Trademark Office. In light of the decision in *Bose*, it is now clear that the Federal Circuit will hold parties challenging registrations on the basis of fraud to the same high standard that the other circuit courts have applied-a subjective intent to deceive.

The *Bose* case started out as a fairly typical trademark dispute in the same fashion as *Medinol*. Bose opposed Hexawave's application to register HEXAWAVE as a trademark on the basis that it was likely to be confused with Bose's WAVE mark, for which Bose claimed prior common law rights as well as a prior federal registration. Hexawave counterclaimed, seeking to cancel Bose's WAVE registration because Bose had allegedly defrauded the Trademark Office when it filed its renewal affidavit claiming continued use of the WAVE mark on audio tape recorders and players when it was no longer selling such goods. Bose had stopped manufacturing and selling audio tape recorders and players before the renewal affidavit was filed, but it contended that it continued to use the WAVE mark "in commerce" on such goods because it continued to repair them and to ship the repaired goods, bearing the WAVE trademark, back to their owners. Its general counsel testified that he had signed the renewal affidavit on the basis of such use.

The Trademark Trial and Appeal Board focused its decision on the fraud issue because the question of whether shipments of repaired goods constituted use in commerce on those goods was not even close-they did not. Applying the *Medinol* standard, the Trademark Trial and Appeal Board concluded that Bose "knew or should have known" that repair of products did not constitute use of a trademark "in commerce," held that Bose's submission of the false renewal affidavit constituted fraud, and ordered the WAVE registration cancelled in its entirety. Bose appealed, arguing both that the Trademark Trial and Appeal Board erred in its conclusion that the shipment of repaired goods did not constitute use of the trademark in commerce, and, alternatively, that Bose's belief that it did was reasonable and did not constitute fraud.

While the Federal Circuit agreed with the Trademark Trial and Appeal Board that repair of goods was not sufficient to claim continuing use in commerce, it found in Bose's favor on the fraud issue. The Federal Circuit held that the "knew or should have known" standard adopted in *Medinol* had "erroneously lowered the fraud standard to a simple negligence standard," and that this was inappropriate for "an indispensable element in the [fraud] analysis." In its place, the Federal Circuit held that fraud requires that an "applicant or registrant knowingly [make] a false, material representation with *the intent to deceive the PTO*." Applying this standard in the *Bose* case, the Federal Circuit held that Bose did not commit fraud and that the Trademark Trial and Appeal Board erred in cancelling the WAVE registration in its entirety.

In re Bose has now brought clarity to trademark law. As an initial matter, until the *Bose* decision, no reasonable registrant dared come forward voluntarily to correct a registration because even reasonable mistakes were likely to be considered fraud under the Trademark Trial and Appeal Board's strict liability standard. The *Bose* decision will allow registrants to begin to come forward and correct their registrations without serious risk, which should lead to a cleaner registry. Moreover, the demise of the *Medinol* standard will allow parties to focus on the merits of inter partes proceedings, rather than on tactical claims of fraud, and likely will lead to fewer oppositions being sidetracked with weak claims of fraud.



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California Consumer ZIP Codes Are Free Game

Many states have consumer privacy laws that protect customers' personal contact information such as addresses and phone numbers. These laws prohibit retailers from obtaining and recording such information at the point of sale during credit card transactions. They are designed to protect consumers from intrusions that range from individual advertisements to stalking. Most retailers understand this, and no longer ask for such information. Many retailers, however, continue to ask customers for their ZIP codes to aid with demographic marketing efforts. Some retailers use ZIP code information to target a marketing campaign in a particular area, while others use it to determine potential locations for new stores. Recently, scores of companies in California have been hit with consumer class actions over this ZIP code issue. There is now a published Court of Appeal opinion holding that the collection of customer ZIP codes is *not* a violation of law.

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The Song-Beverly Credit Card Act of 1971 prohibits merchants from requesting or requiring a credit cardholder's "personal identification information," such as an address or a telephone number, as a condition to accepting a customer's credit card. A merchant is liable for up to $1,000 in penalties for each violation. One need only imagine a retailer with 100 stores and 100,000 credit card transactions per store per year to understand the enormous potential liability. Thus, most California retailers no longer ask for addresses or phone numbers. Many, however, continue to ask for ZIP codes.

Retailers have had no reason to believe that ZIP codes were protected "personal identification information" under the Act, and there was no legal precedent holding that they were. Over the last few years, however, many California retailers have been hit with class action lawsuits claiming that the request for a ZIP code at the point of sale violates the Act. The threat of these lawsuits has left retailers little choice but to settle due to the costs of litigation and the possible prospect of exorbitant damages.

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A recent decision from the 4th District Court of Appeal now finally provides retailers and consumers with a definitive answer on this ZIP code issue. In *Party City v. Superior Court*, the Court of Appeal determined that a ZIP code is not "personal identification information" protected by the Act. The California Supreme Court recently denied the plaintiff's petition for review.

In *Party City v. Superior Court*, the plaintiff alleged that Party City, a national party supply retailer, requested her ZIP code when she purchased items with a credit card in violation of the Act. Like many retailers, Party City had its cashiers request customer ZIP codes at the point of sale. Cashiers asked for a ZIP code regardless of the type of transaction (i.e., cash, check, debit or credit card), and prior to knowing the type of payment. Disclosure of a ZIP code was completely voluntary, and the ZIP code information was then used for general demographic marketing purposes only. Party City made no effort whatsoever to contact the plaintiff. Consequently, Party City filed a motion for summary judgment on the grounds that a ZIP code was not protected "personal identification information" under the Act. The trial court, however, denied Party City's motion, and determined that ZIP codes were "personal identification information" as a matter of law.

Due to the procedural posture of the case, appeal was not available as a matter of right, and Party City petitioned the appellate court for a writ of mandate to consider the case. The appellate court granted the writ, reversed the judgment of the trial court, and ordered that summary judgment for defendant Party City be granted. The Court of Appeal reasoned that even though a ZIP code provided some identification, it was primarily "group identification" because tens of thousands of people reside in the same ZIP code. It evaluated the language of the Act and its legislative history to determine that "a ZIP code by itself does not qualify as 'personal identification information' because it is not 'personal' - i.e., it is not information about a particular cardholder." The Court of Appeal reasoned, that "personal identification information" allows one to find a needle in a haystack, and a ZIP code is merely the haystack itself. Importantly, there was no competent evidence before the trial court to demonstrate that a person can be located using a ZIP code and a name or credit card number. (Another appellate decision is soon expected on this issue from the same appellate district in a similar case, *Pineda v. Williams-Sonoma*, Court of Appeal Fourth District, Division One.)

The *Party City* decision is a victory for retailers and for common sense. There are many legitimate uses for ZIP code information that *do not* involve locating a particular person. With this decision, retailers can remove the ZIP code trap from the list of legal perils they confront if doing business in California.