Consumer Products Marketing Bulletin

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ARNOLD & PORTER

Court decisions, new and pending laws, and regulations arise every day affecting companies that produce and market consumer products. Because key executives in these companies are busy, the lawyers at Arnold & Porter who specialize in those issues — consumer protection, Food and Drug, Lanham Act, trademark, privacy, and consumer product safety — thought it would be useful to summarize notable policy and regulatory developments, as well as court decisions, for our clients. A&P's Consumer Products Marketing Bulletin aims at keeping you informed of these issues with a concise overview of selected developments. Attorneys in all practice areas listed are available to expand upon and answer any questions you may have in regard to any of these issues. If there is anything we are not covering in this newsletter you feel would be useful for you to know, please feel free to contact Randal_Shaheen@aporter.com.

CONSUMER PROTECTION[1]

Policy:
FTC Heads Outline Focus of Agency Efforts

Federal Trade Commission (FTC) Chairman Muris outlined, in testimony before Congress, several areas deserving of heightened consumer protection enforcement. These included "high-tech" frauds, Internet promotion of products and services as cures or treatments for serious diseases, and privacy protection.

In an earlier speech, Muris listed a number of privacy initiatives including a national do-not-call list and stepping up enforcement of deceptive SPAM, the Fair Credit Reporting Act, Children's Online Privacy, and the Telemarketing Sales Rule. Muris rejected for now the need for additional legislation.

Howard Beales, Director of the Consumer Protection Bureau, reiterated Chairman Muris' focus on privacy in a recent interview, noting that communicating privacy rights to consumers requires more effective measures than having a committee of lawyers drafting language few comprehend. He also indicated a special interest in testimonial claims, particularly where the results are more likely to vary substantially from the testimonial claim.

Enforcement:
Proud To Be American

The FTC continues vigorous enforcement of its "Made in USA" standard. The Commission requires that any product so advertised or labeled must be "all or virtually all" made in the United States. In our experience, in most cases this means that 90% or better of the total manufacturing costs must be incurred domestically. Latest FTC actions include complaints against five analgesic manufacturers who represented their products as "Made in USA" but imported the bulk aspirin, acetaminophen, or ibuprofen used in their products.

1 Arnold & Porter's Antitrust Trade Regulation Group has extensive experience in consumer protection matters before the Federal Trade Commission (FTC), State Attorneys General, and the National Advertising Division (NAD). Members of our group include Bob Pitofsky, former FTC Chairman and Director of the Bureau of Consumer Protection; Mike Sohn, former FTC General Counsel; Bill Baer, former FTC Bureau Director; Debbie Feinstein, former Assistant to the FTC Bureau Director and Attorney Advisor; and Randy Shaheen, who has practiced in this area for nearly 15 years.

FTC Supports NAD

We often tell our clients considering using the Better Business Bureau's self regulatory process, the National Advertising Division (NAD), that while the process seemingly lacks teeth, advertisers who flout the self-regulatory system risk the wrath of a FTC that is anxious to shore up the NAD. Lisa Frank, operator of a web site targeting girls, learned that lesson the hard way. The company ignored the NAD's Child Advertising Review Unit's (CARU) advice on how to modify its web site to comply with FTC child privacy regulations. CARU referred the matter to the FTC. The agency ultimately entered into a consent order with the company which broadly regulates its activities with respect to consumer privacy as well as requiring the payment of a civil penalty.

Regulatory Developments: NAD Proposes Revised Procedures

The NAD unveiled for comment a revised set of procedures. The comment period recently expired, and after further review by its Board, NAD expects the procedures to be implemented in the next few months. Among the significant proposed changes are:

1. a filing fee for competitor complaints of $1,000 for members and $2,000 for non-members;
2. an eight-page limit (excluding exhibits) for complaints, along with a requirement that they be submitted in hard and electronic versions;
3. a provision giving challengers the right to waive their reply or to request expedited review;
4. a clarification that the challenger's identity must be disclosed;
5. the ability to "administratively close" a matter if, after a challenge, the advertiser states that it is permanently discontinuing the advertising; and
6. a reduction in the time to submit an advertiser's statement and a referral to government agency if no statement is submitted.

FOOD AND DRUG[2]

Enforcement: Virtual Labeling?

The Food and Drug Administration (FDA) recently discussed its position concerning material posted on web sites about FDA-regulated products in its response to a citizen petition filed by the Washington Legal Foundation. The petition had requested that the FDA declare that material on a web site relating to any FDA-regulated product does not constitute "labeling," but may constitute advertising; in the alternative, the petition had requested the more limited relief that material on the web sites of only food companies not be considered "labeling." In its response, the FDA determined that some types of material disseminated over the Internet by or on behalf of a regulated company could be considered "labeling" regulated by the agency, that other types of material would be regulated as advertising, and that food companies should not be treated differently from other FDA-regulated industries. Finally, the FDA stated that it would "continue to use a case-by-case approach" to regulating information on the Internet, rather than issue a more general policy or guidance.

Regulatory Developments: Regs for Export of Certain Unapproved Products

The FDA published, in the *Federal Register* on December 19, 2001, its regulations implementing the notification and recordkeeping requirements for exporting unapproved drug, medical device, and biological products under the FDA Export Reform and Enhancement Act of 1996. The regulation addresses the types of information that must be contained in a "simple notification" to the FDA of the export of unapproved products that have been approved in certain specified foreign countries. It also specifies the types of information that must be maintained by the company as records of the export of such products. In the *Federal Register* notice, the FDA also responded to comments

2 Arnold & Porter's Food, Drug and Medical Devices Group has represented a variety of companies in responding to inquiries from FDA and other agencies about advertising claims and other marketing activity, as well as worked on complaints to FDA and others regarding apparently violative conduct by competitors. Members of the group in our DC office include Bill Vodra, Arthur Levine, and Don Beers, each of whom were previously prominent lawyers at FDA; Helene Madonick; Rob Conley; and David Korn.

about specific issues raised by the legislation. In particular, the FDA stated that a product that is identical to a product approved in the United States, but that has labeling in a foreign language that the FDA has not separately approved, is considered to be an unapproved product.

LANHAM ACT[3]

Court Decisions: A Refund by Any Other Name . . .

A misleading claim is not action able under the Lanham Act unless the deception is "material" to consumers, but a recent case underscores the dangers in incorrectly assuming what matters to your customers. H&R Block wanted to call a loan a "refund" so that it could advertise the fastest refund in the industry. Of course, the two are not the same, but H&R Block assumed that consumers believed the only material difference between the two was that loans usually require payment of interest. H&R Block "cured" this problem by making its loan interest free. The trouble is a competitor was able to use survey evidence to show that consumers associate loans with a bundle of unfavorable conditions and obligations, many of which have nothing to do with the payment of interest. The result: a finding that H&R Block willfully violated the Lanham Act prohibition against false advertising. [*JTH Tax, Inc.* v. *H&R Block Eastern Tax Services, Inc.*, 2002 WL 27257 (4th Cir. Jan. 10, 2002).]

Wrong Motivation Can Lead to Fees

A recent Eleventh Circuit decision provides a warning for plaintiffs. In *Tire Kingdom, Inc.* v. *Morgan Tire & Auto*, *Inc*., 253 F.3d 1332 (11th Cir. 2001), the court made it clear that if a plaintiff initiates a weak Lanham Act suit and the court thinks the plaintiff was motivated principally by a desire to harm or harass its competitor, the plaintiff will be forced to pay attorneys' fees. Under the statute, either a defendant or plaintiff as the prevailing party can obtain attorneys' fees and costs by establishing that the action is an "exceptional case." The decision suggests that a losing plaintiff's motive is relevant in determining whether the case is exceptional.

Court Toasts Extraterritorial Limits

After a number of cases had suggested that the Lanham Act could be invoked by foreign competitors with plans to enter the U.S. market, the Third Circuit has made clear that such plans must be concrete and imminent. The Third Circuit found that Russian vodka producers did not have standing to sue the American makers of Smirnoff vodka [*Joint Stock Society* v. *UDV N. Am.*, 266 F.3d 164 (3d Cir. 2001)]. The plaintiffs, the descendants of P.A. Smirnov and alleged true heirs to the Smirnov vodka legacy, sued the American vodka producer alleging that it was falsely promoting its products as the "vodka of the czars." The court found that the plaintiffs could not have been injured because they had "not adduced any evidence establishing that they are prepared at this time to sell any vodka in this country."

TRADEMARK[4]

Enforcement: TTAB Mows Over Toro

On December 12, 2001, the Trademark Trial and Appeal Board (TTAB) issued its first substantive decision applying the 1996 Federal Trademark Dilution Act (FTDA). [See *Toro Co.* v. *ToroHead Inc.*, TTAB, No. 114,061, 12/12/01.]

In *Toro,* ToroHead Inc. applied to register "TOROMR" for magnetic reading and writing heads sold to manufacturers of high performance computer disk drives. The Toro Company, manufacturer of lawn equipment, opposed ToroHead's application by

3 Arnold & Porter attorneys have significant experience with the Lanham Act, deceptive advertising counseling and representing both plaintiffs and defendants in deceptive advertising litigation. The firm has represented companies and advertising agencies in diverse product areas (including some seminal cases in the pharmaceutical sector). Attorneys in the firm with Lanham Act experience include Joel Freed, Chuck Ossola, and Helene Madonick.

4 Arnold & Porter has extensive experience in all areas of trademark and domain name law, including emerging issues, such as Internet domain name protection from "cybersquatting." Some members of the group include, in our DC offices Jim Walsh (former Administrator for Trademark Policy and Procedure at the PTO), Joel Freed, Roberta Horton, Chuck Ossola, and Mike Songer, and in our LA offices, Suzy Wilson, and Ron Johnston.

claiming, among other things, that the "TOROMR" mark diluted its TORO marks. In finding against Toro, the TTAB noted that protection under the FTDA for dilution claims should only be given in exceptional circumstances. In addition, unlike its practice in likelihood of confusion cases, the TTAB stated that it would not resolve doubts in favor of a party claiming dilution.

Further, the TTAB found that a trademark owner could not establish the "fame" of its mark for FTDA purposes simply by presenting general advertising and sales figures, evidence of duration of use or unsupported assertions of fame. A trademark owner attempting to prove fame would be required to prove that the English language had changed such that the common use of the term had been replaced by a "primary association with the trademark owner." Evidence of such a transformation could include extensive media attention, or more importantly, market surveys. In addition, the TTAB found Toro's evidence of fame in the lawn care market insufficient and further noted the absence of evidence of fame among ToroHead's potential customers. The opinion thus suggests a daunting challenge for parties asserting dilution in the PTO, particularly when the goods of the parties are yards apart.

Court Decisions: Protecting Your True Colors

Remember those crayons you used to play with? Well, you're not alone. The 1996 Federal Trademark Dilution Act, 15 U.S.C. Section 1125(c) (FTDA), was intended to provide a higher level of protection to famous trademarks, even where no likelihood of confusion was present. Nonetheless, the courts have been generally reluctant to afford the FTDA's broad protection, particularly to marks consisting of colors used in trade dress. However, in *Binney & Smith et al.* v. *Rose Art Industries*, 60 U.S.P.Q.2d 2000 (E.D. Pa. 2001), at least one court has demonstrated that with the right set of facts, a trademark owner can prevail.

In *B&S*, Plaintiff Binney & Smith (B&S) alleged that Rose Art sought to capitalize on the fame and recognition of the green and yellow design used on "Crayola" crayons and markers (the "Crayola trade dress") by introducing a line of children's markers in packaging incorporating a similar green and yellow design. In finding that Rose Art's use of a similar green and yellow packaging diluted B&S' Crayola trade dress, the court first noted that the Crayola trade dress was exactly the type of "famous" mark that the FTDA was designed to protect. The court relied upon surveys showing that the Crayola trade dress had acquired national and international recognition with consumers of children's products, as well as other evidence, such as the inclusion of the Crayola packaging in the Smithsonian Institution's permanent collection and its recent use on a U.S. commemorative stamp.

PRIVACY[5]

Enforcement: Handle With Care

In a case with broad implications for financial institutions and other businesses that regularly handle customers' personal information, the FTC announced its settlement of a complaint against the pharmaceutical manufacturer Eli Lilly and Co., alleging that Lilly engaged in deceptive practices through the unauthorized disclosure of personal information collected from consumers through the company's Prozac drug web site, "Prozac.com." According to the complaint, a Lilly employee unintentionally disclosed the e-mail addresses of all 669 subscribers to each individual subscriber. In announcing the settlement, the FTC said that: "Even the unintentional release of sensitive medical information is a serious breach of consumers' trust."

Lilly must implement a four-part information security program based on the information security provisions of the Gramm-Leach-Bliley Act (GLBA). According to the FTC Bureau Director Beales, the

5 Arnold & Porter's privacy team provides legal and strategic counsel to help clients meet their privacy obligations in a demanding, evolving, and competitive marketplace. Our attorneys have held significant senior government positions, including John Bentivoglio, former Chief Privacy Officer of the DOJ; Jeff Smith, former General Counsel for the CIA; Bob Pitofsky, former Chairman of the FTC, and Ron Lee, former General Counsel of the National Security Agency. Others with extensive experience in this area include Nancy Perkins in our DC office and Sarah Kirk in our London office.

settlement also has implications for companies whose "functional regulator" under the GLBA is a federal or state agency other than the FTC. Specifically, Beales said that compliance with the GLBA's security provisions would not automatically exempt banks, securities firms, and others from the FTC action under the new standard set forth in the settlement agreement. This is a very significant signal for financial institutions (including insurance companies, whose GLBA functional regulators are state insurance commissioners). It raises the prospect of FTC complaints against a wide range of entities, relating to both on-line and off-line information, regardless of whether a release of that information was intentional.

Regulatory Developments: Quieter Evenings at Home

In another important move, the FTC recently proposed the establishment of a national "Do Not Call" registry that would enable consumers to block calls from telemarketers. Under the proposed system, it would be illegal for telemarketers to call consumers who place their phone number on the national registry. In addition, the agency is proposing to prohibit telemarketers from trafficking in consumers' credit card and other account numbers and barring telemarketers from blocking or otherwise subverting caller ID systems. The FTC is seeking comments on the proposed telemarketing rules for a period of 60 days (due March 29, 2002).

FTC Ahead of the Technology Curve

The FTC's Children's On-line Privacy Protection Rule provides for a sliding scale approach for obtaining parental consent before collecting personal information from children, which depends on the reason for collecting the personal information. The use of an e-mail from the parent is permitted when the web site operator seeks information only for internal use. If the web site site is going to disclose the personal information to the public or third parties, the Rule requires that the web site operator use more reliable methods to obtain the parent's consent. Currently, the sliding scale is set to expire on April 21, 2002, because the FTC believed that more reliable methods of obtaining consent would become widely available and affordable. Turns out this hasn't happened yet, and the FTC has proposed extending the life of the sliding scale until April 21, 2004.

CONSUMER PRODUCT SAFETY[6]

Enforcement: Court Ruling – Speak Now or Pay Later

The Consumer Products Safety Act (CPSA) requires manufacturers, importers, distributors, and retailers of a consumer product to report to the Consumer Products Safety Commission (CPSC) if the company has information that "reasonably supports the conclusion" that the product contains a defect that could present a substantial product hazard or creates an unreasonable risk of serious injury or death.

In what we believe to be the first time that a CPSA reporting case was decided on the merits, a court recently granted summary judgment against a company selling juice extractors, finding it liable for failing to timely notify the CPSC of potential dangers posed by the company's juicers. [*United States* v. *Mirama Enterprises, Inc.*, No. 00-CV-2269-K (LAB) (S.D. Cal. Jan. 24, 2002).] The decision supports the view long held by the CPSC staff that little information (here, three unconfirmed consumer complaints) is required to trigger the duty to notify the CPSC of potential dangers.

This decision is especially significant given the considerable upward trend in the dollar value of civil penalties imposed by the CPSC in the last two years for the failure to report alleged product hazards to the CPSC. Companies that fail to report are subject to civil penalties up to a maximum of $1.65 million for a "related series of violations."

6 Arnold & Porter has several attorneys with broad experience on matters involving the U.S. Consumer Product Safety Commission (CPSC), including two former General Counsels of the agency – Eric Rubel and Jeff Bromme – and Blake Biles, formerly with the Environmental Protection Agency. We take a proactive approach to product safety issues, assisting clients to establish and audit internal controls. We represent clients in CPSC enforcement actions, as well as in private litigation that can result from CPSC matters.

After years of penalties in the low to mid six-figure range for alleged failures to report, the CPSC imposed civil penalties between $750,000 and $1.3 million on six companies in the past two years for such violations.

Challenge to the CPSC Lab Blows Up

The Eighth Circuit has upheld the CPSC's fireworks regulations enacted pursuant to the Federal Hazardous Substances Act (FHSA). [*Shelton* v. *CPSC*, No. 99-1450 (8th Cir. Jan. 23, 2002).] The CPSC found that fireworks imported by Shelton failed its performance tests and were a banned substance under the FHSA. The decision's impact likely will reach far beyond the field of fireworks regulation.

The Eighth Circuit held that the FHSA gave the CPSC jurisdiction over common fireworks and also upheld the CPSC regulations interpreting and applying the statute. The court also held that the CPSC's administrative review procedures, wherein a party whose products have been found to violate a regulation is given an opportunity to present contrary evidence to the agency, provided sufficient due process. Finally, the court turned back challenges to the CPSC's laboratory procedures and testing methods.

The *Shelton* opinion likely will embolden agency enforcers, when faced with challenges to interpretations of agency regulations or laboratory methods, as well as encouraging the Justice Department, which represents the agency, to find additional resources to assist the CPSC in future litigation.

Regulatory Developments:
Over Here; Over There – Non-U.S. Data

The CPSC has announced that it interprets the law to require companies to consider non-U.S. safety information in complying with mandatory safety reporting requirements. In the wake of the National Highway Traffic Safety's (NHTSA) experience with foreign information in connection with the Bridgestone/Firestone tire recall, the CPSC issued a policy statement and amended an interpretive rule to put companies on notice that the CPSC expects companies to consider information from both within the United States and abroad in determining whether the duty to notify the CPSC has been triggered.

Under the new interpretive rule, in assessing whether a reportable safety hazard exists, a company must consider "information, that [the] firm has obtained, or reasonably should have obtained...about product use, experience, performance, design, or manufacture outside the United States that is relevant to products sold or distributed in the United States." Thus, the CPSC may seek to impose a civil penalty against a company not only for an alleged failure to consider foreign safety information that the company has, in fact, received, but also such information that the company "reasonably should have obtained."

These CPSC pronouncements highlight the importance to a company of having appropriate internal controls in place with respect to the collection, tracking, and evaluation of safety information, particularly as the CPSC may hold a company responsible for information known anywhere within the company. For example, to help ensure compliance with the CPSC's mandatory reporting requirements, a company may want to (a) identify the various sources of safety information – both domestic and foreign – that reach the company or are reasonably available to it; (b) establish procedures to track such information on an ongoing basis; and (c) make certain that safety information, once collected, is evaluated periodically by individuals qualified to assess potential safety concerns and, where appropriate, determine whether there is a legal obligation to notify the CPSC.