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Expert Analysis

Assessing Impact of 'Bose' on Fraud Standard in Trademark Practice

In a prior article ("Fraud Doctrine on Trademark Applications Remains Minefield," NYLJ, Aug. 19, 2009), we discussed developments related to claims of fraud on the Patent and Trademark Office in obtaining trademark registrations and recent Trademark Trial and Appeal Board (TTAB) opinions on that issue. As anticipated, the U.S. Court of Appeals for the Federal Circuit weighed in on the issue in an Aug. 31 opinion titled *In re Bose Corp.* (Opposition No. 91/157, 315) and rejected the six-year-old standard for showing fraud—"should have known" of the falsity—which the TTAB had previously adopted in *Medinol Limited v. Neuro Vasx Inc.*, 67 USPQ2d 1205 (TTAB 2003). That standard, according to the Federal Circuit, constituted mere negligence and did not rise to the level of fraud. Rather, fraud requires a showing of "subjective intent to deceive." As explained in the opinion, intent to deceive generally implicates a knowing falsehood, which the facts in *Bose* simply did not support.

We discuss here what impact that decision will have on practice before the TTAB, what issues remain unresolved and what future developments in this area may be expected.

Standard Not Resolved

One significant unresolved issue is whether a showing of "reckless disregard for the truth" satisfies the fraud standard. The *Bose* opinion references that standard in a footnote, but simply states that even if the CAFC were to assume that it qualifies as fraud, the record in the case did not support such a finding.

We expect that in short order litigants before the TTAB will be claiming fraud based on recklessness. There is a strong legal argument to support that position. The Trademark Act permits a party to move to cancel a registered trademark on the grounds that the "registration was obtained fraudulently." 15 U.S.C. §1064(3). The term, "fraudulently," is nowhere defined in the statute. Thus, common law precedent should be instructive in interpreting the statute. In fact, the Supreme Court has repeatedly affirmed that "it is a well-established rule of construction that where Congress uses terms that have accumulated settled meaning under the common law, a court


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must infer, unless the statute dictates otherwise, that Congress means to incorporate the establish meaning of these terms." See, e.g., *Neder v. United States*, 527 U.S. 1, 23 (1999). This presumption is mandatory—absent an express indication otherwise, the common-law meaning controls.

As explained in our last article, it has long been the rule at common law that a representation of fact knowing that there is no real basis for believing it constitutes fraud. That was the holding of the New York Court of Appeals in *Hadcock v. Osmer,* 47 N.E. 923-24 (N.Y. 1897), and is set forth in the Second Restatement of Torts, §526(b) (fraudulent to make a false statement "if the maker…does not have the confidence in the accuracy of his representation that he states or implies.") The comments there note that "[i]t is enough that being conscious that he has neither knowledge nor belief in the existence of the matter he chooses to assert it as a fact." This is often termed acting "recklessly."

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Federal courts have often held that reckless conduct satisfies a finding of fraud in other contexts. For example, in securities fraud cases, "[e]very Court of Appeals that has considered the issue has held that a plaintiff may meet the scienter requirement by showing that the defendant acted intentionally or recklessly…" *Tellabs Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 319 n. 4 (2007) (wire fraud). Similarly federal criminal fraud statutes (mail fraud, wire fraud) have generally been held to be violated where a person acted with "reckless indifference to the truth." *United States v. DeRosier,* 501 F.3d 888, 897-98 (8th Cir. 2007)(wire fraud); *United States v. Munoz*, 233 F.3d 1117, 1136 (9th Cir. 2000)(mail fraud); *O'Malley v. New York City Transit Authority*, 896 F.2d 704, 707 (2d Cir. 1990) (mail fraud).

Thus we expect that the "recklessness" standard will likely be adopted by the Board in the near future.

Fact Pattern in 'Bose' Unusual

Bose's impact will, in our view, likely to be less than many have come to believe. As explained in our last article, the *Bose* facts were unusual and different from the typical cases under *Medinol* and its progeny. In *Bose*, the registrant had made some form of use of the mark for the goods listed (repair of previously sold goods bearing the mark); it was debatable whether such use qualified under the Trademark Act to renew a registration. The person affirming the registration honestly believed that the use was legally qualified. Although he was mistaken, under the circumstances that representation was not fraudulent.

That is very different from the typical case where an applicant affirms the use of the mark on multiple types of goods, when in fact the applicant is only using them on a subset of the types listed in the application. *Medinol* itself illustrates the more typical scenario: the applicant claimed use of its mark for neurological stents and catheters, but in fact had never used the mark on stents.

Query whether the outcome in *Medinol* would have been different if the *Bose* decision applied. One could make a cogent argument that the *Medinol* applicant's affirmation was made recklessly—it had in fact never used the claimed mark for one of the two types of goods listed. If the recklessness standard is adopted, then many cases are likely to be resolved the same way—albeit under a more exacting standard than before.

One must remember what is at issue in such cases. The representations such as in *Medinol* involve a party's own use of its own trademark. Who better than the trademark owner knows for which goods it is using its mark? A flippant disregard for the facts is inexcusable—and will often be construed as "reckless indifference to the truth" and hence fraud.

Impact on Pleading Fraud

One area where *Bose* will likely have an impact is pleading fraud in TTAB proceedings. The Federal Rules of Civil Procedure are generally applicable

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in proceedings before the Board. TBMP §101.02. Rule 9(b) of the Federal Rules governs allegations of fraud: "In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." Although the second sentence of that rule appears to state that there is no need to make particularized allegations as to state of mind when making a claim of fraud, the majority[1] of circuits have not taken that approach. Rather, they require a party alleging fraud to make specific factual allegations which permit an inference of fraudulent intent. The Federal Circuit—whose rulings control in the PTO—is among the majority of circuits that take that position.

A recent Federal Circuit case explicates what it expects in pleading fraud. In *Exegen Corp. v. Wal-Mart Stores Inc.*, 575 F.3d 1312 (2009), the Federal Circuit affirmed a district court's rejection of allegations of inequitable conduct in obtaining a patent. Inequitable conduct, like fraud, requires a showing of deceptive intent; allegations of inequitable conduct are subject to Rule 9(b). In fact, the *Exegen* ruling relied in part on trademark precedent from the Court of Customs and Patent Appeals (the Federal Circuit's predecessor) which dealt with cancellation of trademark registrations for fraud. Conversely, the *Bose* decision (issued only a few weeks after *Exegen*) relied in part on patent cases involving inequitable conduct in setting the standard for fraudulent intent. One can safely presume that the Federal Circuit's observations in *Exegen* will be applied in Board proceedings.

Under *Exegen*, a party must plead "sufficient underlying facts from which a court may reasonably infer that a party acted with the requisite state of mind." 575 F.3d at 1328. At the pleading stage, these specific facts must lead to a "reasonable inference" of fraudulent intent. "A reasonable inference is one that is plausible and that flows logically from the facts alleged, including any objective indications of candor and good faith." Id. n. 5. The Federal Circuit did acknowledge that the standard at the pleading stage is less rigorous than at trial—where the burden is on the party claiming fraud or inequitable conduct to prove it by clear and convincing evidence. "Whereas an inference of deceptive intent [at the complaint stage] must [only] be reasonable and drawn from a pleading's allegations of underlying fact to satisfy Rule 9(b), this inference must [at trial] be the single most reasonable inference able to be drawn from the evidence to meet the clear and convincing standard."

It is thus at the pleading stage where *Bose* may have its greatest impact. Indeed, in a Board decision issued shortly after issuance of the *Bose* opinion entitled *Societe Cooperative Veigneronne v. Albrecht-Piazza, LLC* (Opposition No. 91190040 Sept. 20, 2009), the TTAB cited *Bose* and rejected a counterclaim for cancellation on the basis of fraud for failure to make specific allegations as required by Rule 9(b).

This puts parties seeking to allege fraud in a bind. Even if one knows that an adversary's registrations are based on false information (e.g., they claim use on goods for which the trademark was never used, as in *Medinol*), that does not mean that there was fraudulent intent. Conversely, without discovery it will often be difficult to uncover evidence of fraudulent intent. What is likely to happen in the future is that parties will proceed with other bases for cancellation/opposition, seek to gather evidence of fraud during discovery, and then move to amend the Notice of Opposition/Cancellation to add a new basis for relief.

That being said, plaintiffs in Board proceedings should emphasize that at the pleading stage an inference of fraudulent intent need only be plausible and be sure to tell the story persuasively and in detail in their complaint. Once again, the facts of *Medinol* are instructive. It is difficult to believe that the person who verified the application for use of the mark on two goods had any basis for his belief, since the company had in fact never used the mark on one of the two types of goods claimed. Query whether a pleading setting forth those facts would be sufficient under *Bose* and *Exegen* to satisfy Rule 9(b)?

Higher Standard

Attorneys should be aware, however, that Trademark Office rules may require a higher standard and indeed might even lead to additional claims of fraud. The Lanham Act requires any applicant for registration to submit a verified statement that (1) the Applicant is the owner of the mark; (2) the facts recited in the application are accurate; (3) the mark is in use in commerce and (4) no other person has the right to use the mark in commerce in an identical or very similar form in a manner likely to cause confusion. 15 U.S.C. §1051(a)(3). Current Trademark Office practice only requires from the Applicant that the person verify (under penalty of perjury) "that all statements made of his/her own knowledge are true; and that all statements made on information and belief are believed to be true."

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Attorneys representing clients before the Trademark Office are subject to its rules. Trademark Rule 11.18, patterned after Rule 11 of the Federal Rules of Civil Procedure, provides that an attorney must sign any submission to the Trademark Office—and in so doing makes several representations. Among them are that "[t]o the best of the party's knowledge, information and belief, formed after an inquiry reasonable under the circumstances…the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery…" Trademark Rule 11.18. Violation of that rule can lead to both sanctions against counsel and the party.

Attorneys must therefore be sufficiently careful that assertions made in proceedings before the Trademark Office have an evidentiary basis after reasonable investigation. For example, a party asserting its own trademark rights and registrations in an opposition/cancellation proceeding will often make extensive allegations about its own use of and rights in a particular mark. An empty good-faith belief in the truth of the allegations is simply not enough—the attorney is representing that, after reasonable investigation for what is alleged, there is an evidentiary basis.

Indeed, there is another form of fraudulent intent recognized at common law which is pertinent to such situations—fraud as to the basis of knowledge. The Restatement Second of Torts, §526(c) states that a representation is fraudulent "if the maker…knows that he does not have the basis for his representation that he states or implies." The comments explain that, for example, if a representation is made on the maker's personal knowledge of the fact in question or "upon his personal investigation of the matter," and that collateral representation regarding the efforts to investigate the matter is false, then the primary representation is likewise fraudulent—"even though the maker is honestly convinced about its truth from hearsay or other sources that he believes to be reliable." Id. comment f. Thus a good faith belief in the truth of one's representation will not save one from fraud if one deliberately deceives the other party as to the basis of one's belief—e.g., based on due diligence or personal investigation.

In the future, Congress or the Trademark Office might wish to strengthen the language of the representations made to obtain a registration to match the Rule-11-type verification required in other proceedings before the Trademark Office. That would expand the universe of fraud cases to include "basis of knowledge" fraud.

Fraud Still a Minefield

While *Bose* did raise the standard for proving fraud in TTAB proceedings, for the reasons discussed, that has not and will not put an end to allegations of fraud. As discussed in our prior article, the fraud doctrine can be a minefield for parties seeking to register a trademark for a long list of goods—especially for many foreign applicants, who are used to different trademark regimes (everything in the class) than that in the United States. We continue to recommend that trademark registrants periodically review their portfolios to ensure that they accurately reflect the actual state of use of the mark—and to move quickly to correct any inaccuracies.

1. At least the First, Second, Third, Seventh and Federal Circuits have some version of such a rule. See, generally, 2 Moore's Federal Practice, §9.03[3] and nn. 44 and 45. The Ninth Circuit has expressly disagreed, holding, as the plain language indicates, that no specificity is required when alleging fraudulent intent. It should be noted also that in securities fraud cases, Congress has instituted a heightened pleading standard in the PSLRA.