

Tactical Use of Covenants Not To Sue Headed for Supreme Court



– by Uli Widmaier

The U.S. Supreme Court recently took up a trademark issue and granted *certiorari* in *Already LLC d/b/a Yums v. Nike, Inc.*, No. 11-982, — U.S. —, 2012 WL 425184 (June 25, 2012). The question before the Court: “Whether a federal district court is divested of Article III jurisdiction over a party’s challenge to the validity of a federally registered trademark if the registrant promises not to assert its mark against the party’s then-existing commercial activities.” *Petition for Writ of Certiorari*, 2012 WL 441275 (February 8, 2012). The case will be heard during the 2012-2013 term.

At issue is a tactic – used more frequently in patent than in trademark litigation – whereby the plaintiff shuts down the defendant’s counterclaim challenging the validity of plaintiff’s rights by (1) giving defendant a unilateral and unsolicited covenant not to sue, (2) dismissing its claims against defendant with prejudice, and (3) moving to dismiss defendant’s counterclaims as moot. Nike successfully did exactly that in its trademark infringement case against Yums. See *Nike, Inc., v. Already LLC d/b/a/ Yums*, No. 09 Civ. 6366, 2011 WL 310321 (S.D.N.Y. Jan 20, 2011), *aff’d Nike, Inc., v. Already LLC d/b/a Yums*, 663 F.3d 89 (2d Cir. 2011).

With the Supreme Court’s grant of *certiorari*, the effectiveness of this tactic may be in for a change.

I. The Problem: Trademarks with Issues

Some trademarks are more enforceable than others. A mark may be an important corporate asset, yet have certain vulnerabilities. Priority, continuous use in commerce, abandonment, naked licensing, functionality, descriptiveness, genericness – these and other issues may make a company

think twice before filing suit against even a clear infringer. Even an “incontestable” trademark registration is open to challenge on grounds such as abandonment, functionality, and genericness. Configuration marks are often vulnerable for lack of secondary meaning or functionality. And so on.

A defendant’s counterclaim to invalidate plaintiff’s rights and registrations may be a battle the plaintiff does not want to fight. In a recent Seventh Circuit case, *Georgia-Pacific Consumer Products LP v. Kimberly-Clark Co.*, 647 F.3d 723 (7th Cir. 2011), Georgia-Pacific sued Kimberly-Clark for infringing its heavily advertised, well-known, and incontestably registered configuration mark, a diamond pattern embossed on its QUILTED NORTHERN bathroom tissue. Kimberly-Clark counterclaimed for cancellation, the district court invalidated Georgia-Pacific’s mark as functional, the Seventh Circuit affirmed, and Georgia-Pacific had lost a valuable corporate asset.

So what is a victim of infringement to do when its “at-risk” mark is knocked off? Suing the infringer may draw a possibly meritorious counterattack. But simply standing by and watching the infringer exploit the plaintiff’s goodwill is not an attractive option either. Furthermore, “[a] trademark holder is required to police his mark; else, it may become generic, diluted, or otherwise lessened in value.” *Fuji Photo Film Co., Inc. v. Shinohara Shoji Kabushiki Kaisha*, 754 F.2d 591 (5th Cir. 1985).

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II. A Tactical Solution: a Unilateral Covenant Not to Sue

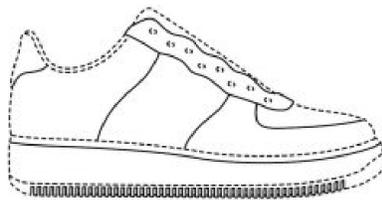
A practice that is well-established in patent litigation has offered some promise in the past. File an infringement action. If an early settlement is reached, the validity issue goes away (the settlement may even help build an enforcement portfolio, strengthening the mark's future enforceability). If the defendant counterclaims for declaratory judgment of noninfringement, or for cancellation or a finding of invalidity, send the defendant a unilateral covenant not to sue in the future for defendant's current or similar conduct; voluntarily dismiss your claims against the defendant with prejudice; and move to dismiss the defendant's counterclaims on the ground they have become moot.

In principle, the covenant estops the plaintiff from suing the defendant in the future for defendant's current infringing conduct. See, e.g., *Super Sack Mfg. Corp. v. Chase Packaging Corp.*, 57 F.3d 1054, 1059 (Fed. Cir. 1995). With further legal action by plaintiff precluded, "any controversy sufficiently actual to confer jurisdiction over [the] case" is removed, and the court is deprived of subject matter jurisdiction over defendant's counterclaims under the mootness doctrine. *Id.* In other words, a unilateral covenant not to sue can shut down a defendant's counterattack on the plaintiff's mark, reducing the risk to the plaintiff of filing the action in the first place.

III. A Seemingly Routine Case

Nike sued Yums in 2009 for infringing the configuration of Nike's Air Force I athletic shoe, *Nike, Inc., v. Already LLC d/b/a/ Yums*, No. 09 Civ. 6366, 2011 WL 310321, at *1 (S.D.N.Y. Jan 20, 2011), as shown in Nike's U.S. Trademark Registration No. 3,451,905 (the broken lines are not part of the mark):

Yums counterclaimed, alleging the mark and registration are invalid, the 905 Registration should be cancelled pursuant to Section



37 of the Lanham Act, 15 U.S.C. § 1119, and Yums "has not infringed any rights that Nike may have in the configuration." *Nike, id.* Discovery commenced. Nike reconsidered. "In the middle of discovery, Plaintiff delivered a covenant not to sue . . . to Defendant." *Nike, id.* The covenant stated that Yums's actions "no longer infringe or dilute the Nike Mark at a level sufficient to warrant the substantial time and expense

of continued litigation." *Id.* Nike "unconditionally and irrevocably covenants to refrain from making any claim(s) or demand(s), or from commencing, causing, or permitting to be prosecuted any action in law or equity against defendant" for trademark infringement, dilution, and related claims "based on the appearance of any of [Yums's] current and/or previous footwear designs, and any colorable imitations thereof," regardless of whether that footwear is produced or sold before or after the date of the covenant. *Id.*

Nike then dismissed its claims against Yums and moved to dismiss Yums's counterclaims for lack of subject matter jurisdiction. The district court granted Nike's motion. Concerning Yums's declaratory judgment counterclaim, the court held that Yums "bears the burden of demonstrating that the Court has subject matter jurisdiction over its counterclaims." *Id.* at *2. That burden consists of the following: "Defendant must, under all circumstances, demonstrate a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment in order for the Court to retain jurisdiction over its counterclaim." *Id.* at *4, quoting *MedImmune, inc., v. Genentech, Inc.*, 549 U.S. 118, 127 (2007) (quotation marks omitted).

Because of Nike's covenant, the court found that Yums could not meet that burden. *Id.* Nike's covenant "clearly extends to future sales of defendant's current footwear designs, ... as well as to future sales of 'colorable imitations' of those shoes." *Id.* Therefore, the *MedImmune* "substantial controversy" standard for maintaining declaratory judgment actions was not met.

On Yums's cancellation counterclaim, the court found that "if an event subsequent to the pleadings strips a court of jurisdiction over the action, the court is also stripped of the ability to order cancellation of a registered trademark pursuant to Section 1119." *Id.* at *7. Thus, Yums's cancellation counterclaim was also dismissed.

Yums appealed. The Second Circuit affirmed the district court's decision on essentially the same grounds. *Nike, Inc., v. Already LLC d/b/a Yums*, 663 F.3d 89 (2d Cir. 2011). The court noted that "Yums cites only one case, *Bancroft & Masters, Inc., v. Augusta National Inc.*, 223 F.3d 1082 (9th Cir. 2000), in support of its argument that a court may retain jurisdiction over a § 1119 claim notwithstanding the end of case or controversy with respect to the rest of the action." *Id.* at 99. The court distinguished the Ninth Circuit's decision in *Bancroft* by noting that the covenant not to sue in

that case “failed to end the case or controversy”, and the Ninth Circuit’s statement that “even an unqualified promise would not have mooted the separate request for § 1119 cancellation of the trademarks is therefore dictum” that the Second Circuit chose not to follow. *Id.* (citation and quotation marks omitted).

Yums then successfully petitioned the Supreme Court for a writ of *certiorari*.

IV. What Can We Expect from the Supreme Court’s Decision?

It is difficult to pin down what motivated the Supreme Court to grant *certiorari*. Was it the circuit split between the Second Circuit’s *Nike* decision and the Ninth Circuit’s *Bancroft* decision, as Yums urged in its petition? Unlikely. As the Second Circuit had already found, and as Nike pointed out in its response to Yums’s petition, the relevant statement in *Bancroft* is dicta.

Is it that the Supreme Court believes the burden of demonstrating that the court retains jurisdiction over the counterclaims should not have been shifted to the defendant, as the district court held and the Second Circuit affirmed? Does the Court believe this makes avoiding challenges to plaintiff’s intellectual property rights too easy?

As Yums argued in its *cert.* petition, this burden shifting was criticized in a dissent by Judge Dyk in *Benitec Australia, Ltd. v. Nucleonics, Inc.*, 497 F.3d 1340, 1350 (Fed. Cir. 2007) as subverting the “strong public interest in permitting accused infringers to challenge invalid or unenforceable patents.” The Supreme Court has previously articulated a “strong federal policy favoring the full and free use of ideas in the public domain,” *Lear v. Adkins*, 395 U.S. 653, 674 (1969); warned against “scarecrow” intellectual property rights, *Cardinal Chemical Co. v. Morton Int’l, Inc.*, 508 U.S. 83, 96 (1993); and noted the “importance of protecting the right of society at large to use words or images in their primary descriptive sense,” *KP Permanent Make-Up, Inc., v. Lasting Impressions I, Inc.*, 543 U.S. 111, 122 (2004) (citation and quotation marks omitted).

If such a broader policy concern is the reason behind the Supreme Court’s decision to grant *certiorari*, the practice of terminating defendant’s challenge to plaintiff’s trademark or patent rights by issuing a unilateral covenant not to sue may be substantially curtailed. In the meantime, potential litigants should take great care before counting on this tactic as a part of their litigation strategy. ■

APPOINTMENTS

Phillip Barengolts has been appointed as a liaison from the American Bar Association Section of Intellectual Property Law to ICANN’s Intellectual Property Constituency.

Thad Chaloeintiarana has been appointed Chair of The Trademarks and Unfair Competition Division for the American Bar Association Section of Intellectual Property Law, effective August 1, 2012.

Robert W. Sacoff has been reappointed liaison between AIPPI and the American Bar Association Section of Intellectual Property Law for 2012-2013.

PRESENTATIONS

Phillip Barengolts spoke at an AIPLA online seminar entitled “Counterfeiting - A Dangerous Reality: Legal Tactics and Corporate Best Practices for Combating Counterfeiters,” on June 20, 2012.

Jonathan S. Jennings will speak on “Right of Publicity Law Meets Social Media” at the ABA Annual Meeting program on “Social Media Promotions and the Potential Implications of the Right of Publicity,” on August 5, 2012, in Chicago, Illinois.

Alexis E. Payne will speak in the same program on “How the FTC’s Guides on Testimonials & Endorsements Affect Social Media and the Right of Publicity.”

Janet A. Marvel spoke on “Trademarks: Utilitarian and Aesthetic Functionality” at a Strafford Live Seminar, on June 12, 2012.

Alexis E. Payne co-organized and moderated an ABA Promotion and Marketing Law Roundtable entitled “Emerging Technology and the Impact on Marketing and Promotions.” The roundtable was held on June 28, 2012 at the offices of **Pattishall, McAuliffe, Newbury, Hilliard & Geraldson LLP**. On September 25, **Lexy** will also speak on “Ethical Issues in Advertising Counseling” for the Advertising Law Institute 2012 Conference.

HONORS AND AWARDS

Jonathan S. Jennings will be recognized in the 2013 Edition of *Marquis Who’s Who in America*, to be published in the Fall.

David C. Hilliard, Robert W. Sacoff, Belinda J. Scrimenti and **Joseph N. Welch II** have been recognized by Who’s Who Legal as being among the world’s leading trademark lawyers.

The Legal 500 United States 2012 has recognized **Pattishall, McAuliffe, Newbury, Hilliard & Geraldson LLP** for having “a longstanding reputation for handling trademark trials, appeals and TTAB proceedings” and for acting “for companies from many industries, such as consumer goods, manufacturing, retail, and software...” Also recognized: “Senior Partner **David Hilliard** is recommended, as is **Phillip Barengolts** for his experience in anti-counterfeiting and trade dress disputes. **Jonathan S. Jennings** has handled various TTAB proceedings and is also recommended, and **Robert Sacoff** focuses on trademark infringement and unfair competition cases.”

FIRM UPDATE & ANNOUNCEMENTS

PUBLICATIONS

Ashly Iacullo Boesche's article entitled "Required Disclosures in Social Media" was published in the May 2012 issue of *National Products Insider*.

Phillip Barengolts' article entitled "The Ethics of Deception: Pretext Investigations in Trademark Cases" was published in *The Akron Intellectual Property Journal*. **Phil** was also quoted by the *Chicago Daily Law Bulletin* on June 1, 2012, on the U.S. International Trade Commission's ruling on *In the Matter of Certain Handbags, Luggage, Accessories, and Packaging Thereof*, Investigation No. 337-TA-754, in an article entitled "Louis Vuitton victory starts longer fight."

David C. Hilliard, Joseph N. Welch II and Uli Widmaier co-authored the Ninth Edition of their widely used law school casebook, *Trademarks and Unfair Competition*, published by LexisNexis in July 2012.

Jonathan S. Jennings and J. Michael Monahan co-authored the book "*Trademarks and Unfair Competition: Critical Issues in the Law*," published by Law Journal Press of New York in June 2012. This concise one-volume guide to trademark

and unfair competition law addresses the emerging issues of greatest importance to businesses today. It provides in-depth analysis, real-world samples, and valuable strategic information on everything from the trademark registration process to anti-counterfeiting and gray market goods litigation, to right of publicity, anti-dilution and social media issues. It is available in print or digital formats at http://www.lawcatalog.com/product_detail.cfm?productID=17593.

Jonathan S. Jennings was quoted by the *Chicago Tribune* on May 4, 2012, in an article entitled "Radio station's Blagojevich billboards cause static." He commented on the applicability of the Illinois Right of Publicity Act to a dispute involving former Governor Rod Blagojevich.

Uli Widmaier published an article entitled "'Sensible Agnosticism' or 'Quintessential Actual Confusion'?" Fourth Circuit Reassesses Consumer Uncertainty about Sponsored Links" in the June 2012 edition of *Intellectual Property Today*. The article discusses the Fourth Circuit's recent decision in *Rosetta Stone v. Google*.

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