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Court Examines Trademark Claims Against 'Compatible' Coffee Pods

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Brand protection is a tricky game. Companies often walk a fine line between maintaining a reputation for quality and angering consumers by shutting out competition. Intellectual property lawyers have observed that balancing act in a number of markets, from auto parts to printer ink to (most recently) single serving coffee pods. In these cases and many others, manufacturers have employed a mix of technological and legal tools to limit third parties from providing parts or services for their products.

But when limitations become too aggressive, the market tends to reject them regardless of their legal foundation, and they have to be modified or eliminated. For example, in the early 2000s, printer manufacturers added identifying microchips to their ink cartridges and installed software in their printers that locked out third-party cartridges. Competitors who copied the chips and sold compatible cartridges at a lower price were sued under the anti-circumvention provisions of the Digital Millennium Copyright Act. Cases were brought in different federal courts with different results—but the market's response was universally negative. These days, the ID chips still exist, and your printer will warn you if you use an off-brand cartridge. But the litigation has largely ceased.

If printer companies learned their lesson, coffee companies apparently didn't. In 2014, Keurig announced that its new "Keurig 2.0" machines would use a similarly restrictive system for its "K-Cup" pods. This time, the market response was swift—so swift that Keurig had to scale back its plan. But only somewhat: its machines still reject unlicensed pods. This allows Keurig to control the quality of the beverages dispensed by its machines, but it comes at a cost in customer goodwill due to higher prices and more limited selection.

It appears that the other giant in the coffee pod arena, Nespresso, chose a different route. After the recent expiration of certain key patents, many companies entered the coffee-pod market. But rather than employing a technological lock-out to prevent consumers from using non-Nespresso products, Nespresso chose to pursue a legal strategy with a specific focus on protecting its brand. A recent case in the Southern District of New York shows how the company maximized the protection of its name and image by bringing well-established claims of trademark and trade dress infringement. The opinion is a good example of how traditional legal tools can be put to work by businesses facing novel market issues.

'Nespresso v. Libretto'

In July 2015, Nespresso USA sued Africa America Coffee Trading Co. d/b/a Libretto in the Southern

District of New York.[1] Nespresso, known for its single-serve coffee capsules and machines, sued Libretto, a new competitor that, according to Nespresso, had the sole mission of offering "Nespresso Compatible" capsules for use with Nespresso's machines.

Nespresso alleged that Libretto's capsules and packaging were designed "to be nearly identical" to Nespresso's, replicating their "size, shape, colors and appearance." Libretto's packaging used Nespresso's trademarks, specifically the Nespresso name and logo. And Libretto's website allegedly included the word "NESPRESSO" among its metatags—words and phrases in a website's code that are not seen by viewers but are used by search engines to direct users to the website.

In short, Nespresso claimed that it was being harmed because Libretto was selling nearly identical coffee capsules—paradigmatic substitute goods—and it was selling them using the Nespresso brand.

Nespresso sued Libretto for trademark and trade dress infringement, cybersquatting, and false designation of origin under the Lanham Act, along with related state law claims. It sought an injunction, a monetary award of Libretto's profits, an award for damage caused by Libretto's infringement, and an order requiring the destruction of Libretto's products. Libretto neither answered Nespresso's complaint nor opposed its motion for default judgment. Libretto never showed up at all.

Judge Laura Taylor Swain granted default judgment on all of Nespresso's claims except the cybersquatting claim.[2] First, the court applied the factors for determining whether to grant a default judgment: whether Libretto's default was willful, whether Libretto had a meritorious defense, and the prejudice to Nespresso from denying the motion. Finding that the factors supported a default judgment, the court went on to analyze the merits of Nespresso's claims.

The court began with the trademark infringement claims. Under §1114(1) of the Lanham Act, Nespresso had to show that it possessed a valid mark entitled to protection and that Libretto's use of it was likely to cause confusion.[3] Nespresso's complaint attached its registration from the U.S. Patent and Trademark Office for the word mark "Nespresso," which is prima facie evidence of the mark's validity and entitlement to protection. Because this was not rebutted, the court focused on the likelihood of confusion, which is analyzed using an eight-factor test established in *Polaroid v. Polarad Elecs.*, 287 F.2d 492, 495 (2d Cir. 1961).

The court held that the first *Polaroid* factor, the "strength" of the mark, favored Nespresso, which had registered its mark. Once the USPTO grants a registration, the mark is presumed to be distinctive for the goods or services covered by the registration.

The second factor, similarity of the marks, also favored Nespresso. Some aspects of Libretto's use argued against this: Its packaging added the word "compatible" to the trademarked word "Nespresso," and Libretto's name was larger than the phrase "Nespresso compatible." But the word "Nespresso" was styled identically to the Nespresso trademark, and the phrase "Nespresso compatible" was prominent, brightly colored and "highly stylized" on the Libretto box, in contrast to the more subtle presentation of "Libretto." The court found this was "likely to be particularly eye-catching to the consumer" and tended to create a likelihood of confusion.

The third and fourth factors—the proximity of the products in the marketplace and the likelihood of Nespresso "bridging the gap"—also favored Nespresso. Libretto used Nespresso's mark to compete in the market for coffee capsules—a product Nespresso already sold. There was therefore perfect proximity and no gap to bridge.

On the fifth factor, consumer confusion, the court held that it could make no ruling absent discovery; it therefore was neutral. The court reached the same conclusion on the sixth factor: Libretto's bad faith (or lack thereof) in using the mark. On the seventh factor, the relative quality of the products, the court interestingly held that the concededly *lower* quality of Libretto's product—Libretto pods being made of plastic rather than aluminum—weighed *against* a finding of confusion and favored Libretto.

Finally, the court held that the eighth *Polaroid* factor, the sophistication of the relevant market, favored Nespresso. It held that coffee pods were "relatively inexpensive goods," whose consumers were "unlikely to be exceptionally sophisticated and were "therefore more likely to be confused." Weighing all of the *Polaroid* factors together, the court found that there was a likelihood of confusion.

That did not end the inquiry, however. The court next turned to the question of "nominative fair use." In the Second Circuit, the doctrine of nominative fair use allows a defendant to use a plaintiff's trademark without authorization to identify its own goods, so long as there is no likelihood of confusion about the source of the goods or the mark-holder's sponsorship or affiliation.[4] Courts look at three factors to determine if a use is protected under this doctrine: Is the product readily identifiable *without* use of the mark; did the defendant use only as much of the mark as necessary to identify the product; and did the defendant do anything to suggest sponsorship or endorsement by the mark holder.

On first glance, Libretto's use seems nominative—using the Nespresso mark to describe the compatibility of its pods. But the court held that, under the Second Circuit's three-factor test, Libretto had gone to far. It found that the need to use Nespresso's mark was at least questionable. (Libretto itself suggested its capsules might be compatible with other machines). But more importantly it held that the eye-catching placement and stylized presentation of the Nespresso name on Libretto's packaging crossed the line from an identifying description to a confusing sales tactic. It therefore denied Libretto protection under the nominative fair use defense. Having found a likelihood of customer confusion, with no defense, the court granted default judgment on most of Nespresso's claims relating to trademark and trade dress infringement.

Notably, the court also granted Nespresso's claim relating to the metatags on Libretto's website, finding that the tags, although invisible to consumers, could constitute a false designation of origin when used by search engines. Customers searching for Nespresso's products might be directed to the Libretto website, causing confusion. And even if such confusion did not occur, the court noted, Libretto might simply benefit from additional internet traffic from visitors looking for Nespresso—a theory known as "initial interest confusion." The court, however, denied Nespresso's metatag claim under §1125(d) of the Lanham Act, the Anti-Cybersquatting Consumer Protection Act. The court held that cybersquatting liability arises from a company's confusing URL or domain name, which is visible to consumers, not a website's hidden metatags.

Conclusion

Generally speaking, customers like choices and dislike efforts to limit them. But real choice requires good information, and there is no reason for a company to stand by while a competitor takes advantage of its good name. Today, if you choose an off-brand ink cartridge for your HP printer, you will see a message letting you know that HP is not to blame if you don't like what comes out of the machine. The *Nespresso* case accomplishes the same thing using legal, rather than technical, tools. It ensures that customers understand that pods in a Libretto box don't come from Nespresso, so Nespresso is not to blame if they don't like what comes out of the machine. Although the territory is somewhat unfamiliar, this is exactly the policy these laws were designed to serve.

Endnotes:

1. Complaint, *Nespresso USA v. Africa Am. Coffee Trading Co. d/b/a/ Libretto*, No. 15-cv-05553-LTS (S.D.N.Y. July 16, 2015).

2. *Nespresso USA v. Africa Am. Coffee Trading Co. d/b/a/ Libretto*, 2016 WL 3162118 (S.D.N.Y. June 2, 2016).

3. *Nespresso*, 2016 WL 3162118, at *2 (citing *Time v. Petersen Pub. Co.*, 173 F.3d 113, 117 (2d Cir. 1999)); see 15 U.S.C. § 1114(1).

4. *Tiffany (NJ) v. eBay*, 600 F.3d 93, 102 (2d Cir. 2010).

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