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February 18, 2005

LITIGATION ALERT

SECOND CIRCUIT REINSTATES OBESITY CLAIMS AGAINST MCDONALD'S: WHAT DOES IT MEAN FOR YOUR COMPANY?

On January 25, 2005, the U.S. Court of Appeals for the Second Circuit reversed a district court's dismissal of claims against McDonald's that alleged violations of New York's deceptive trade practices laws. In remanding *Pelman v. McDonald's Corporation* back to the district court for further proceedings, the Second Circuit has given new life to the plaintiffs' claims that the restaurant chain's promotional representations, failure to disclose the use of particular additives and failure to provide nutritional information to its customers caused the plaintiffs to develop obesity, diabetes, heart disease and other harmful conditions.

Early in 2003, the trial court first heard the plaintiffs' arguments that McDonald's should be liable for deceptive practices and false advertising under New York's Consumer Protection Act. The court dismissed the claims because the plaintiffs failed to properly identify specific deceptive acts and advertisements as bases for their claims. Nonetheless, the court granted the plaintiffs leave to amend their complaint to address its deficiencies.[1]

In the Amended Complaint, the plaintiffs alleged claims of deceptive acts in practices in violation of the Consumer Protection Act, New York General Business Law §§349 and 350, as members of a putative class action of minors residing in New York State who have consumed McDonald's products. Plaintiffs alleged (i) that McDonald's misled the plaintiffs, through advertising campaigns and other publicity, into thinking that its products were easily part of a healthy lifestyle if consumed on a daily basis, (ii) that McDonald's failed adequately to disclose the fact that certain of its foods were substantially less healthy, as a result of processing and ingredient additives, than represented by McDonald's in its advertising campaigns and other publicity, and (iii) that McDonald's engaged in unfair and deceptive acts and practices by representing to the New York attorney general and to New York consumers that it provides nutritional brochures and information at all of its stores when in fact such information was and is not adequately available to the plaintiffs at a significant number of McDonald's outlets.

[1] *Pelman v. McDonald's Corp.*, 237 F. Supp. 2d 512 (2003).

The second time the trial court heard the case, it dismissed the claims again.[2] The trial court specifically noted that the plaintiffs had made no explicit allegations that they witnessed any particular deceptive advertisement, and that they had not provided McDonald's with enough information to determine whether its products are the cause of the alleged injuries. Finally, the court noted that the one advertisement which plaintiffs implicitly allege to have caused their injuries was "objectively non-deceptive."

On appeal, the Second Circuit, however, disagreed with the trial court's finding that the claims alleging violations of Section 349 of New York's deceptive trade practices law should be dismissed. Recognizing that Section 349 does not require proof of reliance on the defendant's representations, the Second Circuit held that an action under this law need only meet minimal notice-pleading requirements of Rule 8(a) of the Federal Rules of Civil Procedure. The Second Circuit specifically disagreed with the trial court's conclusion that information regarding what other foods the plaintiffs ate, how much they exercised and whether they had a family history of the diseases allegedly caused by McDonald's foods need be included in the pleadings. Rather, the Second Circuit held that the plaintiffs' more general pleadings regarding causation were sufficient and that this information is an appropriate subject for discovery.

CAN DEFENDANTS AVOID BURDENSOME DISCOVERY BY OBTAINING COURT ORDERS SEQUENCING OR OTHERWISE LIMITING DISCOVERY?

The Second Circuit's decision reopens the case to the extent that it allows the claims to survive procedurally for at least one round of discovery. According to Professor John Banzhaf of George Washington University Law School, "[t]he decision opens the door not only to many more obesity law suits, but also to unearthing previously secret documents which may help plaintiffs persuade juries to hold fast food companies liable for their fair share of the expenses of the obesity to which they contribute." Plaintiffs' lawyers pursuing obesity claims have not shied away from drawing comparisons to the tobacco litigation and the success they procured by mining internal company documents obtained through discovery.[3] Professor Banzhaf has articulated specifically the kinds of document discovery he is looking for from food companies, including "any memo about whether additives and food processing techniques might make food substantially less healthy in the sense of being substantially higher in fat, trans fat, cholesterol, calories, etc., or that certain techniques might tend to increase any tendency of fast foods to have addictive effects on some of the purchasers."[4]

It is still uncertain how far the trial court will allow discovery to progress before revisiting the merits of these claims and considering dismissal for yet a third time. Indeed, with no proof of reliance on the defendants' representations regarding the nutritional content of the food, a strong argument can be made that discovery should progress in stages, with the plaintiffs required to produce evidence of their consumption habits and other issues bearing on their claims that the food could have caused their illness before the defendants should be required to open their documents for review. Case management orders sequencing discovery have long been an important tool for litigants in products liability cases where expansive discovery requests may be unduly burdensome in light of the factual circumstances.

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[2] *Pelman v. McDonald's Corp.*, 2003 U.S. Dist. LEXIS 15202 (2003).

[3] Jeremy Grant, "Fast Food Sellers Fear the Fat Will Start Suing Them," *Financial Times*, February 2, 2005.

[4] Professor John F. Banzhaf III, "McDonald's Obesity Suit Reinstated," January 25, 2005, at http://www.banzhaf.net/mcback.html.

HAS THE SECOND CIRCUIT'S DECISION ENCOURAGED ADDITIONAL OBESITY SUITS?

In allowing the *Pelman* suit to go forward under New York's General Business Law §349, which is similar to the consumer protection statutes of other states, the Second Circuit may have encouraged prospective plaintiffs to file their own obesity suits. The *Pelman* decision, combined with specific threats of litigation and the plaintiffs' bar's express desire to seek "tobacco-like" documents, raises interesting questions as to the circumstances under which companies should reasonably anticipate litigation such that documents or other evidence need to be preserved.

The *Pelman* decision has broad ramifications for all consumer class actions given that many states have deceptive trade practice statutes that do not require a showing of actual reliance on the misrepresentation. California courts, for example, may impose liability and civil penalties without individualized proof of reliance under California's unfair practices laws. *See People v. Dollar Rent-A-Car Systems, Inc.*, 211 Cal. App. 3d 119, 131 (1989) (imposing liability under Cal. Bus. & Prof. Code §§17200, 17500 for defendant's sale of misleading collision damage waivers to car rental customers even though the customers may not have read the contracts); *see also Day v. AT&T Corp.*, 63 Cal. App. 4th 325, 332-34 (1998) (holding that plaintiffs stated a cause of action under California law without alleging reasonable reliance on defendants' deceptive packaging of phone cards). The rationale behind these state statutory schemes is to provide the broadest protections for the public against fraud and deceit by enabling suit to be filed whenever members of the public are likely to be deceived. There has been a noticeable trend in products liability cases toward framing claims under consumer protection statutes to ensure class certification particularly since failure to warn claims alleging personal injury may not be susceptible to class treatment because of the need for individualized proof on medical causation. There have been dangerous precedents set in tobacco cases framed as consumer fraud cases. For example, in a case in Madison County, Illinois, the jury awarded $7.1 billion in a case that made allegations regarding the use of the word "Light" and reduced tar and nicotine representations.[5] The plaintiffs did not seek recovery for personal injury but rather sought compensation in the form of sales rebates as a percentage of the purchase price on the theory that they were induced to think the cigarettes were a healthier choice.

WILL THE CONTINUATION OF THE *PELMAN* CASE REINVIGORATE EFFORTS TO OBTAIN TORT REFORM?

While the Second Circuit's decision has already been touted as a victory in a battle of the bulge by obesity plaintiffs' lawyers, it has also been seized upon by tort reform advocates as evidence of the need for change. Interestingly, this decision comes just as the battle on tort reform is heating up and has become a major focus for the new Bush administration.[6] Tort reform advocates have used the obesity issue to frame the debate for reform as evidenced recently in an advertising campaign in which a hostile plaintiffs' lawyer cross-examines a Girl Scout on the witness

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[5] *See* judgment in *Price v. Philip Morris Inc.*, No. 00-L-112 (Ill. Cir. Ct., March 21, 2003), available at http://news.findlaw.com/hdocs/docs/tobacco/pricepm32103jud.pdf.

[6] At the time of this alert's publication, key legislative measures to curb obesity litigation were gaining momentum. On February 18, 2005, President Bush signed the Class Action Fairness Act, which provides federal courts with original jurisdiction of interstate class actions in excess of $5 million. *See* http://www.akingump.com/docs/publication/728.pdf." In addition, the House had passed the Personal Responsibility in Food Consumption Act, which would bar suits claiming that a food manufacturer's products caused weight gain or obesity.

stand for selling irresistible cookies that have made his client fat.[7] The advertisement's message that obesity suits are frivolous is not lost on the viewer despite the humor in the advertisement. While approximately 14 states have passed legislation banning obesity lawsuits,[8] suits have already been filed in California, Illinois and the state of Washington.

The potential costs of obesity suits against McDonald's or other members of the food industry are yet to be seen. McDonald's has set aside reserves for "legal charges" but has not announced how much of its reserves, if any, it has set aside for the *Pelman* case. See Melanie Warner, "Sales Growth at McDonald's is Highest in 17 Years," *The New York Times*, January 29, 2005. In past SEC filings, McDonald's has referenced disputes arising out of advertising and nutritional disclosures. Similarly, other companies in the food industry have made disclosures in their public filings stating, for example, that future results could be "affected by consumer perception of health-related issues including obesity" or that the obesity issue is a "risk that could potentially adversely affect their industry."

WHAT DOES THE DECISION MEAN FOR YOUR COMPANY'S MARKETING ACTIVITIES DIRECTED TOWARD CHILDREN?

One clear lesson learned that has emerged from the class action litigation against the food and beverage industry is that companies need to make certain they can keep promises they make to consumers regarding their products. McDonald's recently settled a class action lawsuit filed on behalf of consumers over the company's use of trans-fats or partially hydrogenated oils for $8.5 million. The suit alleged that McDonald's failed to reduce the level of dangerous trans-fats in its cooking oil as it promised to do in 2003. The litigation in essence forced the company to honor that commitment regardless of how justified a delay in meeting that goal may have been. While the vast majority of the settlement dollars will be donated to charity, companies feeling pressure to respond to public criticism of their product ingredients should carefully consider how they respond since the response can form the basis for allegations of misrepresentation in future lawsuits. Misrepresentation claims against the food industry are not novel. Earlier cases against the food and drink industry for misrepresentation as to product contents or composition were based on affirmative representations regarding the product or its health benefits. For example, in the early 1990s, the FTC issued a series of consent decrees against food industry companies who made representations regarding the amount of total fat, saturated fat or cholesterol in its products or that their products were connected with reduced blood sugar, blood pressure or heart disease.[9] Similarly plaintiffs' lawyers have been bringing cases against the food industry for representations regarding their health effects associated with the consumption of their products for many years.[10] The

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[7] Award-Winning TV Ad Takes Swipe at Trial Lawyers and Obesity Lawsuits, PRNewswire, February 2, 2005. The commercial can be found at www.consumerfreedom.com/advertisements_detail.cfm/ad/6.

[8] For the status of various state initiatives regarding legislation to prevent lawsuits against restaurants, go to http://www.restaurant.org/government/state/nutrition/bills_lawsuits.cfm#ga.

[9] *Kraft, Inc. v. FTC*, 970 F.2d 311 (7th Cir. 1992) (FTC alleged that Kraft, in an ad campaign, misrepresented information regarding the amount of calcium contained in certain cheese foods); *Bertolli USA, Inc.*, FTC Dkt. No. C-3396, 57 FR 39687 (1992) (FTC alleged that company made representations that olive oil produced health benefits such as reducing blood pressure and blood sugar, with no corroborating scientific evidence); *Campbell Soup Co.*, FTC Dkt. No. 9223 (1992) (FTC alleged that company made representations that there was a connection between its soups and a reduction in the risk of heart disease); Nestlé FTC Dkt. No. C-3365 (1992) (FTC alleged that company misrepresented amount of total fat, saturated fat and cholesterol in Coffee-mate); see *also ITT Continental Baking Co. v. FTC*, 532 F.2d 207 (2d Cir. 1976) (FTC brought action alleging false, misleading and unfair advertising for representation that Wonder Bread was an extraordinary food for producing dramatic growth in children when it was not).

[10] *Committee on Children's Television, Inc. v. General Foods Corp.*, 35 Cal. 3d 197 (Cal. 1983) (in case alleging that defendants' advertising of sugared breakfast cereals was fraudulent and deceptive, court held that plaintiffs could not prove the damages element of fraudulent advertising claim).

difference between these earlier cases and the recent McDonald's settlement, however, is that the recent class action was based not on misrepresentations regarding the product or its health effects but rather on what the Company had promised to do in the future to address a perceived risk to consumers.

The Second Circuit's decision may have significant impact on claims involving marketing to children more generally, especially since the deceptive trade practices claims were allowed to survive regardless of pleading of actual reliance on the marketing representations. The media and public interest groups have heightened awareness recently regarding children's advertising, and the FTC has become increasingly aggressive with respect to marketing activities related to children more generally.[11] Significant research is ongoing regarding whether marketing activities directed to children have adverse consequences regarding children's health, values and behavior, and some have considered whether such advertising is ethical.[12]

As plaintiffs' lawyers attempt to pursue the tobacco model into new arenas, claims of unfair or deceptive advertising to children may emerge even where the child plaintiffs and their parents cannot allege "reliance" or other proof of what particular advertising led to the alleged adverse consequences. The alcohol industry has been battling recently filed cases alleging that alcohol companies negligently focus their advertising on underage drinkers.[13] These cases have been brought under state unfair competition statutes; for example, a suit against Anheuser-Busch in California was brought under the Unfair Competition Law, Bus. & Prof. Code §17200. Rather than plead "reliance," the element keyed into by the plaintiffs in *Pelman*, lawyers in the alcohol suits have instead alleged that a barrage of advertisements — including "television advertisements, magazine advertisements, radio advertisements, marketing strategies, promotional activities, promotional websites and toy and product offerings" — "exploit minors and lure them into unhealthy and potentially life-threatening addictions before they have the maturity necessary to make an informed decision."[14]

CONCLUSION

Widely considered one of the most influential courts in the country, the Second Circuit is often looked to for guidance on novel legal questions. The ramifications of its recent decision in *Pelman* will likely reach across the country. While many consider obesity suits frivolous, regardless of how one might feel about the merits of the claims in *Pelman*, the Second Circuit's decision deserves close attention. The Court allowed the plaintiffs' deceptive trade practices act claim to survive a motion to dismiss without a particularized showing of reliance or casual connection, and many states have similar statutes with no requirement of proof of reliance. The decision has import for any company that markets its products to consumers in New York and beyond.

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[11] In February 2004, for example, the FTC fined Hershey $40,000 for mining kids for information on a Web site; the FTC sanctioned Mrs. Fields $100,000 and UMG Recordings $400,000 for similar offenses.

[12] *See generally* Susan Linn, *Consuming Kids*, The New Press (2004).

[13] *See* Molly McDonough, "Battle Over Liquor Just Beginning," *ABA Journal E-Report*, February 10, 2005, available at http://www.abanet.org/journal/ereport/f11drink.html. The tobacco precedent establishes the use of unfair business practice statutes to go after alleged activity to induce and increase minors' illegal purchases of cigarettes. *See Mangini v. R.J. Reynolds*, 875 P.2d 73 (Cal. 1994).

[14] *See, e.g., Goodwin* Complaint at ¶ ¶ 287, 289 at http://www.hagens-berman.com/files/Busch-Miller%20Complaint1075907015476.pdf. The *Goodwin* case was dismissed recently by Superior Court Judge Peter D. Lichtman, who stated that "the regulating of alcohol ads is not the job of the courts." *See* Jason B. Plemens, "Alcohol Ads Lawsuit Dismissed," *Fresno Bee*, February 7, 2005. The Goodwins have appealed the decision.

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