

Due Diligence Deficit Sinks Fraud Claims in Trademark Battle

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The US Court of Appeals for the Second Circuit affirmed the dismissal of an independent action asserting “fraud on the court” based on the finding that the alleged fraud on the US Patent & Trademark Office (PTO) should have been uncovered by the exercise of due diligence in a prior action. *Marco Destin Inc. v. Levy et al.*, Case No. 23-1330 (2d Cir. Aug. 8, 2024) (Jacobs, Sack, **Sullivan**, JJ.)

In 2007, L&L Wings filed a lawsuit against Marco Destin and related entities (collectively, Marco Destin) in the District Court for the Southern District of New York, asserting claims of breach of contract and trademark infringement related to Marco Destin’s unauthorized use of L&L’s unregistered trademark WINGS on beach apparel. Although L&L and Marco Destin entered into an allegedly valid temporary licensing agreement in 1998, L&L alleged that Marco Destin continued to use the mark after the agreement expired in 2006. Post-discovery, L&L revealed a recent trademark registration for the WINGS mark, causing L&L and Marco Destin to enter a stipulated order of settlement and dismissal in 2011. Marco Destin paid L&L \$3.5 million, ceased using the WINGS mark, and agreed to never bring an action based on the WINGS mark or the 1998 temporary licensing agreement.

More than a decade later, Marco Destin sued L&L again in the Southern District of New York for “fraud on the court” and “fraud” and demanded *vacatur*, sanctions and damages due to key facts revealed in a separate unrelated Eastern District of North Carolina action. In relevant part, it was discovered that L&L was not the owner of the WINGS mark. Rather, an entity named Shepard Morrow owned the WINGS mark and licensed it to L&L for a brief period in the 1990s. L&L stopped paying the required licensing fees to Shepard Morrow and improperly licensed the unregistered WINGS mark to other entities (including Marco Destin). As a result, the Eastern District of North Carolina granted sanctions against L&L for failing to disclose Shepard Morrow’s trademark registration and license agreement, and L&L’s WINGS mark registration was cancelled as a consequence of L&L’s false representations to the PTO. L&L moved to dismiss Marco Destin’s New York complaint pursuant to FRCP 12(b)(6). The district court granted the motion to dismiss, concluding that the “fraud on the court” claim was an independent action for relief from a judgment under Rule 60(d)(3) and Marco Destin had a reasonable opportunity to discover L&L’s false representations during the initial litigation. Marco Destin appealed.

The Second Circuit affirmed, reviewing the dismissal of an independent action for fraud on the court under FRCP 60(d)(3) for abuse of discretion. A party challenging a judgment may file either a timely

motion within a fixed time window – one year under FRCP 60(b)(3) – or an independent action any time after that pursuant to FRCP 60(d)(3). Independent actions require a more demanding showing of fraud (such as fraud on the court itself) than a timely motion, and generally claimants seeking equitable relief through independent actions must:

- Show that they have no other available or adequate remedy
- Demonstrate that their own fault, neglect or carelessness did not create the situation for which they seek equitable relief and
- Establish a recognized ground – such as fraud, accident or mistake – for the equitable relief.

A district court has discretion in determining whether to entertain independent actions for relief. Following this precedent, the Second Circuit agreed with the district court that Marco Destin had a reasonable opportunity to uncover the fraud during the discovery phase of the initial action and that the district court acted within its discretion when declining to vacate the 2011 stipulated order of settlement and dismissal.

Practice Note: Even when an opposing party commits fraud in a related proceeding and/or fraud on the court, the non-fraudulent party must act with diligence in the initial action to prevail in a request for *vacatur*.

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