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COVID-19: Price Gouging, Consumer Fraud and Defective Products

While the COVID-19 pandemic/public health crisis has often brought out the best in people, it is also bringing out the worst in others. Though we have seen generous donations, such as distilleries converting their operations from cocktails to much needed hand sanitizer, we have also seen numerous instances of fraud, scams, and price gouging. This Client Alert explores just a few of the more devious actions out there and what is being done to combat these scams. It also explores how buyers and sellers can protect themselves during the pandemic.

Price Gouging

It goes without saying that Personal Protective Equipment (“PPE”) has been in high demand and is in short supply. This PPE (such as face masks, gowns and N95 protective masks) is critical to the protection of first responders and hospital workers as they treat patients who have contracted COVID-19. While it is rational to expect prices on these types of PPE to rise due to increased demand, several bad actors have sought to exploit the market and “price gouge” the ultimate buyers of these products, including hospitals and the federal government.

To combat against these types of actions, a mask manufacturer has filed several lawsuits against companies across the country that are attempting to sell N95 protective masks at grossly inflated prices. For example, this manufacturer has filed lawsuits in New Jersey, Texas, California and Florida against companies and sellers that tried to sell N95 masks at high prices and, allegedly, claimed a false affiliation with the manufacturer.

There are a few issues that the manufacturer has pointed out in these types of lawsuits. First, the manufacturer has not raised the price of N95 masks because of the pandemic. Second, the manufacturer made clear that the companies wanting to sell these masks at these rather high prices likely do not have any masks, or certainly do not have anywhere near the quantity of masks that they claimed to have. In one case, the manufacturer brought claims for trademark infringement, unfair competition, false association, false endorsement, false designation of origin, trademark dilution, and false advertising.

In another case, the manufacturer is asking a court to order the offending companies to pay damages for its misrepresentations and that the manufacturer would subsequently donate any damages received to corona-virus related nonprofits. In another similar case, the manufacturer has requested a cease-and-desist order against a company that tried to sell masks at a 600% markup over list price. In another case, the manufacturer sued a company that falsely claimed to have a relationship with the manufacturer that allowed to provide masks.

Furthermore, while not a lawsuit, *per se*, Amazon CEO Jeff Bezos recently told investors that Amazon has suspended more than 6,000 vendors, totaling more than 500,000 listings for price gouging during the COVID-19 pandemic. Amazon also said that it turned over information about sellers that it suspected of engaging in price-gouging to numerous state attorneys generals offices.

The moral of this price gouging story is to vet large purchases and deals diligently, especially during a crisis. What a seller “claims” to have or “claims” to be, may not be what it seems.

Consumer Fraud

The coronavirus crisis has created an ideal situation for general consumer fraud and scam activity. Because people are more isolated and spending more time online, people may be more easily distracted. In a statement in March 2020, Minnesota Attorney General Keith Ellison said that “As we come together to combat COVID-19, Minnesotans need to be vigilant about protecting their pocketbooks from scammers as they are about keeping themselves and their communities healthy.”

The Minneapolis Star Tribune¹ recently highlighted the Federal Trade Commission (“FTC”) database of consumer fraud complaints which had reported 18,000 complaints and \$13.4 million in losses due to coronavirus scams nationally. According to the article, some of the more common schemes targeted at consumers are (1) fake treatment and miracle cures; (2) suspicious emails or texts from organizations or government agencies like the World Health Organization or the Centers for Disease Control and Prevention; (3) false relief inquires (such as calls promising relief and goods in exchange for consumers’ money up front); (4) fake charities; and (5) employment scams (which request personal information immediately in exchange for job possibilities).

Like anything these days, most of these scams are targeted to vulnerable individuals, many of whom are working remotely, and can come in the form of social media messages, phone calls, emails and even text messages. There have been text messages to individual cell phones telling people that someone that they were in close contact with has tested positive for COVID-19. The text message also includes a blue hyperlink. However, if the unsuspecting consumer clicks on the link embedded in the text message, the link can cause malware or other nefarious actions on their phones. Do not click on links from numbers that you do not know!

Defective Products

Regardless of price gouging and generic consumer fraud claims coming from the COVID-19 crisis, there remains the generic “defective product” lawsuits that will continue for several years in the future. Take this hypothetical scenario for example: a hospital or medical provider, in desperate need of PPE for its front-line workers, contracts to buy 10,000 N95 masks. The medical provider pays top dollar for the masks. They arrive late, and when they do arrive, the medical provider finds out that while the masks are helpful, they are not rated to pertinent N95 standards.

Or, take this real-life example. An emergency room director spends \$500,000.00 to buy 20,000 coronavirus rapid COVID-19 test kits. However, a week later, the health workers using the tests quickly determined that the tests were unreliable and therefore, unusable. Just a week later, the Food and Drug Administration (“FDA”) seized the entire shipment of tests. That is exactly what happened to officials and medical providers in the South Texas City of Laredo in late March.² While, the medical provider purchased the tests from a relatively unknown medical supply source, these actions further go to show that private sector businesses and governments are taking risks that they normally would not take.

But was that purchase on unreliable test kits a fraudulent act on behalf of the seller? Time will tell. Regardless of whether there was fraud in that specific Texas case, what steps can buyers and sellers take to make sure to address defective product issues now, before the sale? Here are few easy tips that everyone in a COVID-19 transaction should take to protect themselves:

- *Escrow.* Any decent-sized deal will probably require, or recommend, the escrowing of any funds from buyer to seller so that the buyer can evaluate the actual product before buying the product. Most law firms can hold client money in their trust accounts while a deal between parties is being facilitated.

¹<https://www.startribune.com/authorities-warn-consumers-to-beware-of-coronavirus-related-scams/569736562/>

²<https://www.propublica.org/article/he-spent--500-000-to-buy-coronavirus-tests-health-officials-say-theyre-unreliable>

Banks and other financial institutions may have this ability as well. The last thing buyers, especially those in the health care space, need now is to have parted with a significant sum of money only to find out later that the products they bought are fraudulent or defective. Escrowing buyers' funds gives confidence to the seller while also protecting the buyer

- *Due Diligence.* Due diligence means undertaking an actual investigation before closing a deal. Words and representations are not enough. Buyers, and also sellers, need to engage professionals in the due diligence sphere, whether attorneys or otherwise. Due diligence in this space means making quick work and investigation of what a buyer is buying and what a seller is selling. Spending the time and money up front, before the deal closes and money changes hands, is paramount.
- *Contract Language.* One of the final steps in any deal, but especially during the COVID-19 pandemic, is finalizing contract language. Buyers need to be aware of the risk they are taking in entering into a contract and properly protect themselves. How do buyers do this? Make sure that there are attorneys' fees provisions in the contract providing that the prevailing party is subject to recovering its attorneys' fees in the event of litigation. Personal guarantees may also be wise. Finally, recognizing that a contract may take several years to enforce or litigate, partial payments, followed by full payment over time, may be critical to ensuring that buyers get the benefit of their bargain.

And what happens after the fact? What happens if a buyer needs sue a seller, or a seller needs to enforce a contract with a buyer? Resorting to courts when many courts are partially shuttered can be risky. It can also be time-consuming and unpredictable. However, be sure to check state and federal statutes on consumer fraud, as many of those statutes allow for the prevailing party to recover attorneys' fees. Also check state statutes regarding the Uniform Commercial Code ("UCC"). This standardized body of law controls many sales of "goods".

Finally, resorting to a good old-fashioned public relations campaign has its place. There is an outflowing of public goodwill for hospitals, health care workers and other front-line workers, working to keep us safe. The last thing that a seller or provider of allegedly fraudulent medical equipment wants is to be dragged through the mud or to be exposed. While courts may be slow, getting the truth out there about a deal gone bad is quick. Of course, check with an attorney first, before resorting to making claims that may or may not be true. The last thing a buyer or consumer needs is be sued for defamation because they are making unsupported claims.

Conclusion

For more information about any of the matters discussed in this Client Alert, please contact an attorney listed below.

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