To Our Clients and Friends:

On March 25, 2014, the U.S. Supreme Court issued a decision that resolves a split among the courts of appeals on the requirements for standing to bring a false advertising claim under the federal Lanham Act. In particular, the Seventh, Ninth, and Tenth Circuits had strictly limited standing to plaintiffs who are in direct competition with the defendant or can point to a defined "competitive" injury. The Third, Fifth, Eighth and Eleventh Circuits had adopted a more flexible five-factor test derived from the Supreme Court's antitrust jurisprudence. And the Second Circuit and Sixth Circuits had advocated yet another "reasonable interest" test to determine if a false advertising plaintiff had standing. In *Lexmark International, Inc. v. Static Control Components, Inc.*, No. 12-873, the Court held that plaintiffs have statutory standing to sue under the Lanham Act when they "allege an injury to a commercial interest in reputation or sales" that "flow[s] directly from the deception wrought by the defendant's advertising." Slip op. at 13, 15. The Court's decision, moreover, also offers defendants the prospect of an intriguing new defense to a broad range of federal statutory claims.

**Background**

The counterclaim defendant, Lexmark International, Inc. ("Lexmark"), markets laser printers and associated printer cartridges directly to consumers. Although Lexmark printers are designed to work only in conjunction with Lexmark cartridges, third-party entities known as "remanufacturers" regularly acquire depleted Lexmark cartridges, refurbish them, and sell them back to consumers in direct competition with Lexmark. In an attempt to extinguish this practice, Lexmark developed and began utilizing a microchip that automatically disables cartridges once they run out of toner.

The counterclaim plaintiff, Static Control Components, Inc. ("Static Control"), makes replacement parts for third-party remanufacturers who in turn sell refurbished printer cartridges that compete with Lexmark's cartridges. As a result, Static Control was not in direct competition with Lexmark--although it developed its own microchip that "mimic[s]" Lexmark's microchip and allowed remanufacturers to reactivate depleted cartridges. Slip op. at 2.

Lexmark initially filed a complaint against Static Control alleging copyright violations based on similarities between the two chips. Static Control counterclaimed, alleging that (1) statements made by Lexmark to remanufacturers concerning the "illegal[ity]" of selling remanufactured cartridges generally, and (2) statements made by Lexmark to remanufacturers concerning the "illegal[ity]" of using Static Control's microchips specifically, both constituted false advertising under §43(a)(1)(B) of the Lanham Act, codified at 15 U.S.C. §1125(a)(1)(B). *Id.* at 3. Lexmark successfully filed a motion...
to dismiss this counterclaim on the ground that Static Control lacked "prudential standing" to bring a §1125(a) claim under a five-factor test borrowed from Associated Gen. Contractors of Cal., Inc. v. Carpenters, 459 U. S. 519 (1983) (establishing test for standing to bring a private antitrust action under §4 of the Clayton Act). Slip op. at 4. On appeal, the Sixth Circuit rejected the five-factor antitrust test and instead followed the Second Circuit's "reasonable interest" test for standing. Finding that Static Control did possess a "reasonable interest" sufficient to confer standing, the Sixth Circuit reversed the dismissal of Static Control's §1125(a) counterclaim.

The Supreme Court's Decision in Lexmark v. Static Control

The Supreme Court granted certiorari to resolve this circuit split and determine "the appropriate analytic framework for determining a party's standing to maintain an action for false advertising under the Lanham Act." Slip op. at 5-6. In a unanimous decision, the Supreme Court rejected all of these tests and instead promulgated a new test specific to §1125(a) of the Lanham Act. Id. at 15-16.

The Court began by clarifying that this case raised only a question of statutory standing, and did not raise questions of "constitutional standing" (because both parties conceded that Static Control could allege "a concrete and particularized injury in fact that is fairly traceable to the challenged action . . . and likely to be redressed by a favorable judicial decision") or "prudential standing" (because a "zone-of-interests analysis [inherently] asks whether [a] particular class of persons ha[s] a right to sue under [a specific] substantive statute"). Id. at 6-8 (emphasis added, internal quotations omitted). Accordingly, the Court was faced with "a straightforward question of [whether] Static Control falls within the class of plaintiffs whom Congress has authorized to sue under §1125(a)." Id. at 9-10.

First, the Court evaluated "the zone of interests protected by" the Lanham Act to determine what kinds of plaintiffs fall into that zone. Id. at 10-13 (emphasis added). The Court began its analysis by looking to the Lanham Act's "extraordinarily helpful detailed statement of . . . purpose." Id. at 12. Observing that a typical false-advertising case will implicate the Lanham Act's stated goal of "protecting persons engaged in commerce within the control of Congress against unfair competition," and further observing that the general concept of "unfair competition" has long been "understood to be concerned with injuries to business reputation and present and future sales," the Court held the "zone of interests for false advertising under §1125(a)" extends to encompass any plaintiff who can "allege an injury to a commercial interest in reputation or sales." Id. at 12-13 (emphasis added). (Importantly, the Court simultaneously reaffirmed that consumer interests do not fall under this aegis: "A consumer . . . cannot invoke the protection of the Lanham Act." Id.)

Second, the Court went on to observe that standing under a federal statutory cause of action is also "limited to plaintiffs whose injuries are proximately caused by violations of the statute." Id. at 13 (emphasis added). The Court "read §1125(a) as [implicitly] containing" a proximate cause requirement notwithstanding the statute's broad language, and observed that an analysis of proximate cause looks at "whether the harm alleged has a sufficiently close connection to the conduct the statute prohibits." Id. at 14. A plaintiff suing under §1125(a), the Court held, "ordinarily must show economic or reputational injury flowing directly from the deception wrought by the defendant's
advertising." *Id.* at 15 (emphasis added). The Court cautioned that while such a showing may be made "when deception of consumers causes them to withhold trade from the plaintiff," this element will generally not be satisfied "when the deception produces injuries to a fellow commercial actor that in turn affect the plaintiff." *Id.* The Court provided the following illustration: while "a competitor who is forced out of business by a defendant's false advertising generally will be able to sue for its losses" under the §1125(a), "the same is not true of the competitor's landlord" if the competitor is subsequently unable to pay its rent. *Id.*

Having articulated these two applicable statutory limitations on §1125(a) standing, the Court applied them to the facts before it. **First**, the Court found that Static Control fell "within the class of plaintiffs whom Congress authorized to sue under §1125(a)." *Id.* at 18. While conceding that Static Control's alleged injuries do "not present the classic Lanham Act false-advertising claim in which one competitor directly injures another by making false statements about his own goods or the competitor's goods and thus inducing customers to switch," the Court stressed that such familiar fact patterns are "not the only type of injury cognizable under §1125(a)." *Id.* at 19. In particular, the Court cited instances "where a defendant denigrates a plaintiff's product by name" and "where the defendant damages the product's reputation by, for example, equating it with an inferior product." *Id.* at 19-20 (citations omitted).

**Second**, the Court went on to find that Static Control had adequately pled proximate causation by alleging that Lexmark told remanufacturers that Static Control's microchip was illegal: "When a defendant harms a plaintiff’s reputation by casting aspersions on its business, the plaintiff’s injury flows directly from the audience's belief in the disparaging statements." *Id.*

But additionally--and independently from Lexmark's statements about the specific illegality of Static Control's microchip--the Court also found that Lexmark's broader statements about the illegality of remanufacturing cartridges that used Static Control's microchips in general had "necessarily injured Static Control as well," because Static Control operated within a closed market where "there is likely to be something very close to a 1:1 relationship between the number of refurbished . . . cartridges sold (or not sold) by the remanufacturers and the number of . . . microchips sold (or not sold) by Static Control." *Id.* at 21. The Court stressed that as a general matter, the concept of proximate causation should not be "stretch[ed] . . . beyond the first step," but found that the requirement was satisfied under the "relatively unique" circumstances of the case at hand, where "the remanufacturers are not more immediate victims than Static Control." *Id.* (citation and internal quotation marks omitted). Accordingly, *both* of the Lexmark statements at issue were found to independently satisfy the two statutory standing requirements of §1125(a).

**Broader Implications**

First and foremost, the Supreme Court's decision expands the class of potential Lanham Act false advertising plaintiffs in those jurisdictions--e.g., the Third, Fifth, Seventh, Eighth, Ninth, Tenth, and Eleventh Circuits--that had previously adopted a more restrictive test for standing under §1125(a). As the Court stressed, however, individual consumers will still not be able to "allege an injury to a commercial interest in reputation or sales" as required under §1125(a). Slip op. at 13 (emphasis
added). This holding does not apply directly to consumer false advertising class actions brought under state law because the Court's decision is based on the particular text and statutory history of the federal Lanham Act. It may be influential, though, to the extent that individual states have passed false advertising laws that mimic the Lanham Act.

The Court's decision also has potentially broad implications for defendants facing federal statutory claims. The Court has now unanimously suggested that absent an express indication to the contrary, proximate causation is a necessary element of every federal cause of action and must be sufficiently pled in order to survive a motion to dismiss. Id. at 13, 15 n.6 ("[W]e generally presume that a [federal] statutory cause of action is limited to plaintiffs whose injuries are proximately caused by violations of the statute . . . . If a plaintiff's allegations, taken as true, are insufficient to establish proximate causation, then the complaint must be dismissed; if they are sufficient, then the plaintiff is entitled to an opportunity to prove them."). While it remains to be seen how lower courts will interpret this language, Lexmark certainly suggests that litigants should consider--and courts should entertain--motions to dismiss complaints that assert statutory causes of action but do not sufficiently allege how the plaintiff's injury was proximately caused by the defendant's alleged violation of the statute.

Finally, the Court's decision also may be cited by companies who are accused of engaging in a business that is of questionable legality, such as gray market sales, to support a claim for false advertising against brands that view competitive sales as unlawful. The decision, however, does not eliminate the requirement that an allegedly wrongful statement must be made in the context of "advertising" rather than in a statement of a company's legal position. "The touchstone of whether a defendant's actions may be considered . . . advertising or promotion under the Lanham Act is that the contested representations are part of an organized campaign to penetrate the relevant markets." Fashion Boutique of Short Hills, Inc. v. Fendi USA, Inc., 314 F.3d 48, 56 (2d Cir. 2002). The Lexmark decision does not address that analysis.

Gibson Dunn & Crutcher's lawyers are available to assist with any questions you may have regarding these issues. For further information, please contact the Gibson Dunn lawyer with whom you usually work or the authors of this alert:

Howard S. Hogan - Washington, D.C. (202-887-3640, hhogan@gibsondunn.com)
Adam L. Yarian - Los Angeles (213-229-7972, ayarian@gibsondunn.com)

Please also feel free to contact any of the following practice group co-chairs:

Fashion, Retail and Consumer Products Group:
Lois F. Herzeca - New York (212-351-2688, lherzeca@gibsondunn.com)
David M. Wilf - New York (212-351-4027, dwilf@gibsondunn.com)
Howard S. Hogan - Washington, D.C. (202-887-3640, hhogan@gibsondunn.com)
Intellectual Property Group:
Josh Krevitt - New York (212-351-2490, jkrevitt@gibsondunn.com)
Wayne Barsky - Los Angeles (310-557-8183, wbarsky@gibsondunn.com)
Mark Reiter - Dallas (214-698-3360, mreiter@gibsondunn.com)

Media, Entertainment and Technology Group:
Ruth E. Fisher - Los Angeles (310-557-8057, rfisher@gibsondunn.com)
Scott A. Edelman - Los Angeles (310-557-8061, sedelman@gibsondunn.com)
Orin Snyder - New York (212-351-2400, osnyder@gibsondunn.com)

Appellate and Constitutional Law Group:
Theodore B. Olson - Washington, D.C. (202-955-8500, tolson@gibsondunn.com)
Theodore J. Boutrous, Jr. - Los Angeles (213-229-7000, tboutrous@gibsondunn.com)
Daniel M. Kolkey - San Francisco (415-393-8200, dkolkey@gibsondunn.com)
Thomas G. Hungar - Washington, D.C. (202-955-8500, thungar@gibsondunn.com)
Miguel A. Estrada - Washington, D.C. (202-955-8500, mestrada@gibsondunn.com)

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