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"MADE IN THE U.S.A." DECISION THREATENS RETURN TO THE "WILD WEST" FOR CALIFORNIA UNFAIR COMPETITION LAW CLASS ACTIONS

To Our Clients and Friends:

California's Unfair Competition Law (Cal. Bus. & Prof. Code § 17200 *et seq.*, the "UCL") is an expansive statute that historically has been popular among plaintiffs' lawyers. Until recently, private parties could bring "representative," non-class UCL lawsuits even though they had no business dealings with the defendant and despite any showing of actual injury. But in 2004, California voters responded to high-profile abuses of the UCL by adopting Proposition 64. This initiative required private plaintiffs to comply with class certification requirements and to demonstrate actual "injury in fact" and "lost money or property as a result of" the alleged unfair competition.

On January 27, 2011, the Supreme Court of California interpreted these amendments in a way the dissenting justices criticized as "effectively making it *easier* for a plaintiff to establish standing," despite the electorate's intent to strictly limit a private plaintiff's ability to sue. *Kwikset Corp. v. Superior Court*, No. S171845, 2011 Cal. LEXIS 532, at *68 (Chin, J., dissenting) (emphasis in original).

The 5-2 *Kwikset* opinion establishes a test for standing that is important to anyone litigating UCL claims, especially in cases predicated on product mislabeling. Now, "plaintiffs who can truthfully allege that they were deceived by a product's label into spending money to purchase the product, and would not have purchased it otherwise, have 'lost money or property' within the meaning of Proposition 64 and have standing to sue." *Id.* at *4. According to the majority, the consumer has "lost money" by paying more for the mislabeled product than he or she subjectively believed it was worth--even if the mislabeled product functioned perfectly and it was no more expensive than functionally equivalent products with accurate labels.

This alert reviews *Kwikset*, discusses the potential impact of the decision, and identifies ways defendants may resist plaintiffs' attempts to use this opinion to undo gains achieved after Proposition 64.

I. Proposition 64 and Prior Litigation in *Kwikset*

Voters approved Proposition 64 in the November 2004 general election by an impressive margin. The initiative revised the UCL, and the companion False Advertising Law (Cal. Bus. & Prof. Code § 17500 *et seq.*), to bring these statutes in line with other states' consumer protection laws and to require actual injury and class certification for representative actions. As amended, the new standing provisions require private plaintiffs to show an "injury in

fact" and "lost money or property as a result" of the alleged unfair competition or false advertising.

Following the passage of Proposition 64, courts grappled with the meaning and impact of the amendments. In *Californians for Disability Rights v. Mervyn's LLC*, 39 Cal. 4th 223 (2006), the Supreme Court of California ruled that these amendments applied to pending cases. Next, the Court determined that Proposition 64 eliminated "representative" actions and required private plaintiffs to satisfy class certification requirements. *Arias v. Superior Court*, 46 Cal. 4th 969, 975 (2009); *Amalgamated Transit Union v. Superior Court*, 46 Cal. 4th 993, 998 (2009). Shortly thereafter, the Court held that in cases alleging a misrepresentation theory, Proposition 64 required private plaintiffs to establish actual reliance on the allegedly misleading statements but did not require that absent class members also establish standing. *In re Tobacco II Cases*, 46 Cal. 4th 298 (2009).

In *Kwikset*, the primary issue was whether plaintiffs could show that they "lost money or property" due to Kwikset Corporation's alleged misrepresentation that its locksets were "Made in the U.S.A." Plaintiffs claimed that this statement violated the UCL because the locksets contained some foreign-made pins and screws. The case had been pending when voters passed Proposition 64, and the trial court had entered judgment in favor of plaintiffs following a bench trial. Proponents of the initiative cited this case as a "shakedown" lawsuit that the initiative was designed to curb. An appellate judge in an earlier appeal also warned that sanctioning plaintiffs' claims would create a hostile business environment in which "a single spool of foreign thread is enough to sustain a lawsuit." *Benson v. Kwikset Corp.*, 126 Cal. App. 4th 887, 933 (2005) (Sills, J., dissenting).

After voters approved Proposition 64, plaintiffs limited their claims to injunctive relief, and added new class representatives who could meet the initiative's standing requirements. The trial court refused to dismiss the case, but Kwikset sought writ relief. In a lengthy opinion, the appellate court concluded that while plaintiffs demonstrated adequate injury in fact because they were induced into purchasing a product that was mislabeled in violation of a statute, they could not show "lost money or property." Despite their frustrated "patriotic desire to buy fully American-made products," plaintiffs received a fully functioning lockset (the "benefit of their bargain"), they did not claim that they paid a premium based on the "Made in the U.S.A." label, and they did not assert that the lockset was defective or inferior to a product containing all-American components.

The Supreme Court of California granted review in June 2009, to address whether plaintiffs' claim that they bought the products in reliance on alleged misrepresentations made on the product's label sufficed to show that they "lost money" and had standing to sue under the UCL.

II. The *Kwikset* Majority Eases Private Plaintiffs' Burden To Establish Standing

The Supreme Court of California reversed and held that plaintiffs lost money because they "bargained for locksets that were made in the United States" and "got ones that were not." The five-justice majority ruled that the "plain language" of Proposition 64 requires that

private parties "(1) establish a loss or deprivation of money or property sufficient to qualify as injury in fact, i.e., *economic injury*, and (2) show that the economic injury was the result of, i.e., *caused by*, the unfair practice or false advertising that is the gravamen of the claim." 2011 Cal. LEXIS 532 at *16. The Court addressed each of the three principal elements of the UCL's amended standing requirements as follows:

- **"Injury in Fact"**: The Court concluded that this term has a "well-settled meaning" under federal law: "an invasion of a legally protected interest which is (a) concrete and particularized; and (b) actual or imminent, not conjectural or hypothetical." *Id.* at *16-17.
- **"Lost Money or Property"**: The majority then concluded that "lost money or property--economic injury--is itself a classic form of injury in fact" and "[i]f a party has alleged or proven a personal, individualized loss of money or property in any nontrivial amount, he or she has also alleged or proven injury in fact." *Id.* at *20.
- **Reliance/Causation**: Reaffirming *Tobacco II*, the majority held that "a plaintiff must show that the misrepresentation was an immediate cause of the injury producing conduct," but the plaintiff "is not required to allege that the challenged misrepresentations were the sole or even the decisive cause of the injury-producing conduct." *Id.* at *27; *see also In re Tobacco II Cases*, 46 Cal. 4th at 326-28.

The majority concluded that it is irrelevant whether or not a plaintiff received a properly functioning product or paid a premium because of a purported error in a product label. Instead, a plaintiff who relied on a label when making a purchase will have suffered economic harm by having "*paid more for* [a product] than he or she otherwise might have been willing to pay if the product had been labeled accurately." 2011 Cal. LEXIS 532 at *35-36. The majority concluded that any other result "would bring an end to private consumer enforcement of bans on many label misrepresentations, contrary to the apparent intent of Proposition 64." *Id.* at *38.

"Simply stated," Associate Justice Kathryn M. Werdegar wrote, "labels matter," and consumers who purchase a mislabeled product satisfy the Proposition 64 standing requirements. *Id.* at *31-32. A "consumer who relies on a product label and challenges a misrepresentation contained therein can satisfy the standing requirement of [Proposition 64] by alleging, as plaintiffs have here, that he or she would not have bought the product but for the misrepresentation." *Id.* at *36-37. The economic injury may be measured as the difference between what the consumer *would* have spent had he/she known the truth about the product, and the amount actually spent.

As has been its practice in other significant UCL decisions, the Court was careful to limit its ruling to the particular case presented--here, the sufficiency of standing allegations as a matter of pleading in a misrepresentation action. *Id.* at *27 n.9. As the majority explained, courts must accept the allegations as true at the demurrer stage, and "[a]t the succeeding stages, it will be plaintiffs' obligation to produce evidence to support, and eventually to

prove, their bare standing allegations. . . . If they cannot, their action will be dismissed." *Id.* at *45 n.18.

Acting Chief Justice Joyce L. Kennard and Associate Justices Marvin R. Baxter, Carlos R. Moreno, and former Chief Justice Ronald M. George (sitting by designation) joined Associate Justice Werdegar's majority opinion.

III. The Dissenting Opinion Criticizes the Majority's Holding as Dismantling Proposition 64 and Undermining Voter Intent

Associate Justice Ming W. Chin wrote a dissenting opinion (joined by Associate Justice Carol A. Corrigan) that sharply criticized the majority's holding as standing "[i]n direct contravention of the electorate's intent," because it "effectively mak[es] it *easier* for a plaintiff to establish standing" after Proposition 64. *Id.* at *56 (emphasis added). Justice Chin explained that the majority effectively collapsed the "injury in fact" and "loss of money or property" requirements into a combined "economic injury" element that requires only a showing that private plaintiffs "lost" the "price the consumer paid for the product," and an allegation that plaintiffs "would not have bought the mislabeled product." *Id.* at *73. The dissenting opinion also criticized the majority for using extreme examples such as a counterfeit Rolex watch and food products mislabeled as "kosher," "halal," or "organic." *Id.* at *64.

IV. Potential Impact on Future UCL Litigation

If Justice Chin's warnings are accurate, the Court's ruling may spark a return to the pre-Proposition 64 world of questionable and even frivolous lawsuits that turned California into the "Wild West" of consumer class action litigation. However, just as the "sky is falling" predictions immediately after *Tobacco II* proved unwarranted (for the reasons discussed below), the same may very well be true of any initial overreaction to *Kwikset*. Looking ahead, businesses facing UCL claims still have strong defenses to liability, and the breadth of *Kwikset*'s impact will ultimately be resolved through litigation in the Courts of Appeal.

1. Potential Limits On *Kwikset* Holding. Despite some broad language in the majority's opinion, *Kwikset* may be limited to specific types of misrepresentations. In particular, the "Made in the U.S.A." claim violated specific regulations that restricted the use of this label. 2011 Cal. LEXIS 532 at *5. As the decision followed a trial, the majority also cited evidence showing many consumers (including the United States Government) have a strong preference for American-made products. *Id.* at *44 & n.17. For other types of claims, it might not be so easy for private plaintiffs to establish that their personal predilections about the importance of intangible and aesthetic values are material and therefore actionable.

2. Extension Beyond Misrepresentation Context? The applicability of *Kwikset*'s holding to other contexts may be more limited. For example, many courts have held that plaintiffs cannot rely on certain statements about a product, such as "puffery" that a product is "great," "improved," or "better than ever." Moreover, in cases predicated on an omission (rather than an affirmative misrepresentation), courts have dismissed cases on the ground that a defendant was not obliged to disclose the allegedly concealed fact. *See, e.g., Daugherty v.*

Am. Honda Motor Co., 144 Cal. App. 4th 824, 835 (2006); *Buller v. Sutter Health*, 160 Cal. App. 4th 981, 988 n.3 (2008).

3. *The Increasing Importance Of Reliance.* Post-*Kwikset*, the focus also may shift from "injury in fact" to reliance ("as a result of . . ."). See, e.g., *Durrell v. Sharp Healthcare*, 183 Cal. App. 4th 1350, 1364 (2010) (dismissing complaint for failing to claim actual reliance on alleged misrepresentation). *Tobacco II* establishes that in misrepresentation cases, plaintiffs must plead and prove "actual reliance . . . in accordance with well-settled principles regarding the element of reliance in ordinary fraud actions." *In re Tobacco II Cases*, 46 Cal. 4th at 306.

4. *Deferred Attacks On Standing At Summary Judgment.* The majority in *Kwikset* also makes clear that plaintiffs will have to establish the pleaded facts in discovery. 2011 Cal. LEXIS 532 at *45 n.18. Defendants may respond by shifting their focus to later stages of the litigation. A thorough investigation and targeted deposition may reveal that the named plaintiff never saw the labeling at issue, that the label was not "material" to the purchase decision, that the plaintiff would have purchased the product despite the alleged labeling error, or that the plaintiff continued to purchase the product after discovering the truth about the alleged misrepresentation.

5. *Class Certification.* In addition, because much of the *Kwikset* opinion rests on a plaintiff's subjective valuations, there likely will be many opportunities to challenge class certification on the grounds that the named plaintiffs are not typical of the class (because they have an unusual attachment to the importance of the label), or that the class itself is not reasonably ascertainable. In particular, the majority opinion in *Kwikset* acknowledges that while "labels matter," only some consumers are concerned about whether a product is "organic," "kosher," or "Made in the U.S.A." In such cases, is the proper class *all* purchasers, or only those for whom the label matters? And if it is the latter, can that class be appropriately defined and identified? For a class of label-conscious purchasers, would common issues predominate over their individualized and subjective motivations for wanting to purchase a product based on its particular label, and over the variations in subjective value attached to a product that is, for example, "Made in the U.S.A."?

While it is true that *Tobacco II* concluded that only *named* class representatives, and not *absent* class members, must satisfy the Proposition 64 standing requirements (*In re Tobacco II Cases*, 46 Cal. 4th at 324), that majority also held that even if the named plaintiffs establish standing, a trial court still must determine if a proposed class meets California's other requirements for class certification, including ascertainability, typicality, predominance. *Id.* at 313. Consequently, many of the same arguments and much of the same evidence that defendants would use to attack the standing of absent class members may be relevant to the later certification inquiry. Since the *Tobacco II* decision, several courts have denied certification on these grounds, which appear to be very strong "class busters" in cases pleaded on a *Kwikset* theory. See, e.g., *Cohen v. DirecTV, Inc.*, 178 Cal. App. 4th 966, 981 (2009), *rev. denied* 2010 Cal. LEXIS 954 (Feb. 10, 2010); *Pfizer v. Superior Court*, 182 Cal. App. 4th 622, 633 (2010), *rev. denied* 2010 Cal. LEXIS 6162 (June 17, 2010).

6. *Applicability In Federal Cases.* The Class Actions Fairness Act has moved a significant portion of UCL litigation to federal court. In addition to the standing provisions as modified by Proposition 64, a federal court also must apply the requirements of Article III. While the majority concluded that the Proposition 64 standing requirements are *more* stringent than Article III, 2011 Cal. LEXIS 532 at *20, in practice federal "injury in fact" precedent may provide more ammunition to defendants than *Kwikset*. See, e.g., *Waste Mgmt. of N. Am., Inc. v. Weinberger*, 862 F.2d 1393, 1397-98 (9th Cir. 1988) ("[I]t is not enough that a litigant alleges that a violation of federal law has occurred Absent injury, a violation of a statute gives rise merely to a generalized grievance but not to standing."); *Cronson v. Clark*, 810 F.2d 662, 664 (7th Cir. 1987) ("A plaintiff, in order to have standing in a federal court, must show more than a violation of law").

7. *Remedies.* It is one thing for a plaintiff to allege "lost money," but it is another thing entirely for that plaintiff to obtain a monetary recovery under the UCL. Accordingly, whether a plaintiff may prove and recover restitution will likely be a key focus of post-*Kwikset* litigation. Because it rests on standing grounds, the majority's opinion provides no guidance for how trial courts should assess the difference between what a consumer paid for a mislabeled product, and what the consumer would have been willing to pay for the product had it been labeled accurately. 2011 Cal. LEXIS 532 at *37-38 n.15. In another "Made in the U.S.A." case, the Court of Appeal held that an award of restitution must be "based on a specific amount found owing," and must be "supported by substantial evidence." *Colgan v. Leatherman Tool Grp.*, 135 Cal. App. 4th 663, 699 (2006). If future plaintiffs offer nothing more than subjective beliefs and generalized valuations, courts may reject claims for restitution.



Gibson, Dunn & Crutcher's Class Actions Practice Group is available to assist in addressing any questions you may have regarding this decision, or any other related issues. Please contact the Gibson Dunn attorney with whom you work or any of the following members of the Class Actions Practice Group:

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