Litigation Alert:
Supreme Court's *Lexmark* Decision Creates Uniform Federal False Advertising Standing Requirement

MARCH 27, 2014

On March 25, the Supreme Court issued its opinion in *Lexmark International v. Static Control Components*, ruling that Static Control may proceed with its false advertising counterclaim under Section 43(a) of the Lanham Act against Lexmark even though the parties are not direct competitors. This decision resolved a longstanding split among the circuit courts over Section 43(a)'s standing requirement, in which certain circuits–including the Ninth Circuit—had applied a more restrictive test that allowed only actual competitors to sue under the law.

The Supreme Court unanimously held that a plaintiff who alleges injury to a commercial interest in reputation or sales flowing directly from the defendant's actions in violation of the statute falls within the "zone of interests" Section 43(a) was designed to protect, and thus has standing to assert a claim, regardless of whether the parties are in direct competition. The opinion by Justice Scalia rejected all current tests in various circuits as well as the parties' proposals, fashioning a new national standard. While the new standing requirement applies explicitly to only federal false advertising claims, the Court's analytical process in formulating this standard, which rested strongly on the language of the statute, may apply equally to other federal statutory torts.

Case Background

Lexmark manufactures and sells printer cartridges and offers cartridge replacement services to customers. Lexmark developed and sold special toner cartridges in an attempt to compete with cartridge "remanufacturers," which offer competing cartridge replacement services. Lexmark cartridges contained a microchip with software that disabled cartridges when they became empty, so that customers would have to turn to Lexmark for replacement cartridges. Respondent Static Control does not itself manufacture or refurbish cartridges for Lexmark printers. Instead, it supplies components that remanufacturers use to refurbish used Lexmark cartridges and sell them in competition with Lexmark. Static Control furnished remanufacturers a microchip designed to mimic the disabling microchip in Lexmark cartridges. Lexmark, in an attempt to prevent use of Static Control's microchips, warned its customers that they were legally bound by the terms of their license agreement to return their used cartridges to Lexmark for replacement. Lexmark also sent letters to remanufacturers stating that their use of Static Control's microchips was illegal.

Lexmark brought suit against Static Control in 2002 in the Eastern District of Kentucky alleging violations of the Copyright Act and the Digital Millennium Copyright Act. (The lawsuit produced a landmark decision by the Sixth Circuit in 2004 that the anticircumvention provisions of the Digital Millennium Copyright Act did not provide a cause of action in the context of replacement products.) Static Control counterclaimed under Section 43(a) of the Lanham Act, alleging that Lexmark's statements to customers and remanufacturers were false and misleading. Static Control also alleged that Lexmark's false statements had diverted sales from Static Control and had "substantially injured [its] business reputation" by "leading consumers and others in the trade to believe that [Static Control] is engaged in illegal conduct."

Relying on the Supreme Court's decision in *Associated Gen. Contractors of Cal., Inc. v. Carpenters*, 459 U. S. 519 (1983), the district court dismissed Static Control's Lanham Act counterclaim on the ground that Static Control did not have standing because the injury allegedly suffered as a result of Lexmark's statements was "remote" and that it was the cartridge remanufacturers, as direct competitors, who were the "more direct plaintiffs." Adopting and applying the Second Circuit's "reasonable interest" test, the Sixth Circuit reversed and held that Static Control *did* have standing because it had "alleged a cognizable interest in its business reputation and sales to remanufacturers and sufficiently alleged that th[o]se interests were harmed by Lexmark's statements…"[1] Lexmark sought review, and the Supreme Court granted certiorari to decide a narrow issue: the

1 *Static Control Components, Inc. v. Lexmark Int'l, Inc.*, 697 F.3d 387 (6th Cir. 2012).

appropriate framework for determining a party's standing to maintain a false advertising action under the Lanham Act.

The Supreme Court's Decision

In holding that Static Control could sue for false advertising under the Lanham Act, the Court surveyed and rejected various divergent tests for standing that several federal courts of appeals had applied. For example, the Court rejected a categorical "bright line" test that the Seventh, Ninth and Tenth Circuits applied, which accorded standing only to direct competitors.[2] In rejecting that limitation, the Supreme Court noted "[i]t is… a mistake to infer that because the Lanham Act treats false advertising as a form of unfair competition, it can protect *only* the false-advertiser's direct competitors." The Court also rejected the Second and Sixth Circuits' "reasonable interest"[3] test as vague and vulnerable to "widely divergent application" (and thus potentially broader than the test the Court ultimately adopted). Finally, the Court considered and rejected an "antitrust standing" multifactor test that the Third, Fifth, Eighth and Eleventh Circuits applied in light of *Associated Gen. Contractors of Cal., Inc. v. Carpenters*, 459 U. S. 519 (1983).

The Court also expressly rejected the concept of "prudential" standing limitation, a judicial doctrine courts have used in recent decades to dismiss claims that, in essence, they think the plaintiff does not have the right to bring. Justice Scalia observed that this doctrine is "not exhaustively defined" but includes at least three broad principles: (1) the general prohibition against raising another person's legal rights; (2) the bar against adjudication of generalized grievances better suited for resolution by the representative branches; and (3) the requirement that a plaintiff's complaint fall within the zone of interests protected by the law invoked.

Instead, Justice Scalia concluded that courts should employ "traditional tools of statutory interpretation" to determine whether a federal statutory cause of action encompasses a particular plaintiff's claim. Thus the question here was whether Static Control "falls within the class of plaintiffs whom Congress has authorized to sue under [Section 43(a)]." Using this approach, the Court held that the proper test consists of a two part inquiry: (1) whether the claim is within the "zone of interests" protected by the Lanham Act and (2) whether the alleged conduct proximately caused the alleged injury. The Court held that to meet the former, the plaintiff must plead "an injury to a commercial interest in reputation or sales." To meet the latter, the plaintiff must plead "economic or reputational injury flowing directly from the deception wrought by the defendant's advertising" and that the deception causes consumers to withhold business from the plaintiff.

Applying this new test, the Court readily concluded that Static Control's claims fell within the "zone of interests" the Lanham Act protects, because Static Control's alleged injuries—lost sales and damage to its business reputation—are "precisely the sorts of commercial interests the Act protects." Next, analyzing proximate causation, the Court held that, although the suit is not a "classic Lanham Act false advertising claim" involving direct competitors, injury in direct competition is not the only type of injury that the statute recognizes. The Court reasoned that Static Control met the proximate causation requirement, despite no direct competition with defendant, by alleging that Lexmark disparaged both its business reputation and its products with statements that their sale was illegal. The Court held that Static Control further satisfied a proximate causation requirement by allegations that Static control designed, manufactured, and sold microchips that both "(1) were necessary for, and (2) had no other use than refurbishing Lexmark toner cartridges." The Court observed, however, that the alleged injury to Static Control constituted a "relatively unique" case in which there is a "1:1 relationship" between the harm suffered by the direct and indirect competitors, since Static Control's allegations suggested that every refurbished cartridge not sold by a remanufacturer as a result of Lexmark's statements resulted in the same number of microchips not sold by Static Control. (It is not clear whether the Court intended such a 1:1 relationship to be a necessary element of claims by non-competitors.)

---

2 *See, e.g., L.S. Heath & Son, Inc. v. AT & T Info. Sys., Inc.*, 9 F.3d 561 (7th Cir. 1993).

3 *See, e.g., Famous Horse Inc. v. 5th Ave. Photo Inc.*, 624 F.3d 106 (2d Cir. 2010). The "reasonable interest" test requires a plaintiff to demonstrate "(1) a reasonable interest to be protected against the alleged false advertising and (2) a reasonable basis for believing that the interest is likely to be damaged by the alleged false advertising."

Implications of the Decision

Lexmark provides a useful national standard that may curb forum shopping in federal false advertising litigation under Section 43(a) of the Lanham Act. It significantly liberalizes standing in circuits formerly applying a more restrictive, competitor-only, standing test for Section 43(a) claims, including the Ninth Circuit.

Beyond the false advertising litigation arena, however, the Court's clear framework for analyzing how to determine standing to sue for federal statutory torts may have a much broader effect. The Court's focus on statutory purposes and their implication for what a statute *authorizes*¸rather than a focus on how so-called "prudential" considerations may *limit* standing, may shift the debate over who can sue under a wide variety of federal laws. While we expect the effect of this case to be both immediate and predictable in advertising litigation, it may have longer-term, farther-reaching, and more debatable effects in other areas of litigation.

For more information please contact:

Andrew P. Bridges, 415.875.2389; *abridges@fenwick.com*
Jennifer Kelly, 415.875.2426; *jkelly@fenwick.com*
Ronnie Solomon, 650.335.7295; *rsolomon@fenwick.com*
