

High Court Resolves Lanham Act Circuit Split

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By, David B. Sandelands, Esq.

In its recent opinion in *Lexmark International v. Static Control Components Inc.*, 2014 DJDAR 3736 (March 25, 2014), the U.S. Supreme Court resolved a three-way split among the circuit courts regarding who has standing to bring a Lanham Act false advertising claim. Prior to *Lexmark*, some circuits, including the 9th U.S. Circuit Court of Appeals, applied a relatively narrow, categorical test limiting false advertising claimants to direct competitors only. Other circuits applied a relatively expansive “reasonable interest” test that granted standing to essentially any plaintiff who had a reasonable interest to be protected and who reasonably believed he was harmed by the defendant’s alleged false advertising. Yet other circuits applied multifactor balancing tests derived from factors previously established by the court to evaluate antitrust standing. In *Lexmark*, the court declined to adopt any of the above tests.

The facts of *Lexmark* presented a variant on the typical false advertising case where the parties are direct competitors. Lexmark manufactures and sells laser printers. Lexmark also manufactures and sells toner cartridges for its printers. As is common practice in the industry, Lexmark’s toner cartridges work only with Lexmark printers and Lexmark works hard to ensure that it dominates the market for replacement cartridges. To combat toner cartridge remanufacturers who refill empty cartridges and sell the refilled cartridges, typically at lower prices in direct competition with printer manufacturers, Lexmark incorporates a microchip bearing copyrighted software in each cartridge it sells. The microchip disables the cartridge after it runs out of toner and thereafter prevents its operation, even if refilled. Thus, to remanufacture a Lexmark cartridge, a replacement microchip is required.

Static Controls is in the business of selling to remanufacturers the components necessary to refurbish toner cartridges. Of particular importance in this case, Static Controls itself is not in the business of remanufacturing toner cartridges. Seeing a business opportunity in the market for remanufactured Lexmark toner cartridges, Static Controls reverse engineered the software on Lexmark’s microchip and began selling replacement microchips to toner cartridge remanufacturers. Consequently, the market for remanufactured Lexmark compatible toner cartridges blossomed.

Not taking kindly to the unexpected competition, Lexmark sent letters to most of the companies in the toner cartridge remanufacturing business advising that it was illegal to remanufacture used Lexmark cartridges using Static Controls’ microchip and brought suit against Static Controls for copyright infringement. Static Controls counterclaimed for false advertising pursuant to the Lanham Act asserting that Lexmark’s letters to the cartridge remanufacturers falsely claimed that Static Controls had engaged in illegal conduct and consequently harmed its business.

Lexmark moved to dismiss Static Controls' false advertising claim on the grounds that Static Controls lacked prudential standing to assert the claim. The district court granted the motion and the 6th Circuit reversed on appeal. The Supreme Court affirmed the 6th Circuit's decision, but declined to adopt its reasoning.

The court surveyed the three general approaches used by the circuit courts to establish Lanham Act standing for false advertising claims, i.e., the direct competitors test (applied by the 9th Circuit), the reasonable interest test (applied by the 6th Circuit), and the multifactor balancing tests based upon antitrust jurisprudence (favored by many circuits), and found each approach lacking.

The court declined to adopt the "direct competitors" test finding it too narrow noting that while such tests provided an easy-to-apply bright-line rule, they did so at the expense of precluding claims within the zone of interests covered by the statute. Per the court, both the Lanham Act and its predecessor, the common law tort of unfair competition, were understood to encompass claims by non-direct competitors. The court also declined to adopt any of the multifactor balancing tests based upon antitrust jurisprudence on the grounds that such tests were complex, typically had duplicative factors, and that experience had shown that such open-ended balancing tests often yielded unpredictable and at times, conflicting results. The court further rejected the "reasonable interest" test as being too general and lending itself to "widely divergent application."

Rather than adopt one of the existing tests, the court determined instead that the appropriate inquiry to determine whether a plaintiff has standing to pursue a Lanham Act false advertising claim is whether the claim pled falls within the zone of interests sought to be protected by the statute and whether the harm alleged is proximately caused by the alleged false advertising. Per the court, the zone of interests the Lanham Act protects is "an injury to a *commercial* interest in reputation or sales." Injury occurs when the deception caused by the defendant's advertising causes consumers to "withhold trade from the plaintiff."

In applying its new test, the court noted that Lexmark had "directly targeted Static Controls" when it falsely advertised that Static Controls had engaged in illegal conduct. Per the court, when a defendant casts aspersions on a plaintiff's business, the plaintiff's harm flows directly from the audience's belief in the disparaging statements. Although Lexmark and Static Controls were not direct competitors, nevertheless Lexmark's false statements were the proximate cause of Static Controls' economic harm because if the toner cartridge remanufacturers sold "10,000 fewer cartridges because of Lexmark's false advertising," than it would more or less automatically follow that "Static Controls sold 10,000 fewer microchips."

With its decision in *Lexmark*, the court has resolved a substantial split among the circuit courts, broadened the class of plaintiffs who may seek relief under the Lanham Act (at least in the 9th and other circuits that had followed the direct competitors test), and established a

workable set of standing criteria for Lanham Act false advertising claims that largely eliminates the need for speculative proceedings or intricate or uncertain inquires.

David B. Sandelands is an attorney with Cislo & Thomas LLP. He can be reached at dsandelands@cislo.com.