California Supreme Court Establishes Economic Injury Threshold for Unfair Competition and False Advertising Claims

January 27, 2011 by Brian Thompson

The California Supreme Court has declared that "labels matter," and that under California's Unfair Competition Law, a consumer's subjective sense of feeling duped translates to a cognizable economic injury.

The Court's majority opinion in *Kwikset Corporation v. Superior Court (.pdf)*, issued today, January 27th, held that plaintiffs "who can truthfully allege 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,'" and therefore have standing to sue under California's Unfair Competition Law and False Advertising Law. The Court reversed a decision of the Fourth District Court of Appeal, and potentially opened the door to class action litigation brought by plaintiffs who have experienced no dissatisfaction with the actual function or performance of a manufacturer's product.

The plaintiffs brought a class action lawsuit alleging that they purchased locksets manufactured by Kwikset in reliance upon representations that the locks were "Made in U.S.A." or similarly designated. The locks contained components made in Taiwan or involved latch sub-assembly performed in Mexico. The plaintiffs alleged violations of California's Unfair Competition Law (Cal. Bus. & Prof. Code § 17200) for unlawful, unfair, and fraudulent business practices. Their complaint further alleged violation of California's False Advertising Law (Cal. Bus. & Prof. Code § 17500.)

Specifically, the complaint alleged that each of the plaintiffs, in purchasing Kwikset's locksets:
saw and read [d]efendants' misrepresentations . . . and relied on such misrepresentations in deciding to purchase . . . them. [Each plaintiff] was induced to purchase and did purchase [d]efendants' locksets due to the false representation that they were "Made in U.S.A." and would not have purchased them if they had not been so misrepresented. In purchasing [the] locksets, [each plaintiff] was provided with products falsely advertised as "made in U.S.A.," deceiving him [or her] and causing him [or her] to buy products he [or she] did not want. Defendants' "Made in U.S.A." misrepresentations caused [each plaintiff] to spend and lose the money he [or she] paid for the locksets. [Each plaintiff] has suffered injury or loss of money as a result of [d]efendants' conduct.
In 2004, while this case was pending, the California electorate enacted Proposition 64, which amended the UCL and FAL to provide that, except for actions brought by the Attorney General or other public prosecutors, only a "person who has suffered injury in fact and has lost money or property as a result of . . . unfair competition" or false advertising may file suit. (*See* Cal. Bus. & Prof. Code §§ 17204, 17535.)

Kwikset demurred to plaintiffs' complaint, arguing that the allegations failed to satisfy Proposition 64's requirements for standing. The trial court overruled the demurrer. Kwikset sought and obtained writ relief from the Court of Appeal, which held that while the plaintiffs spent money, they received locksets in return – locksets

they did not allege were overpriced or defective. Thus, while their "patriotic desire to buy fully American-made products was frustrated," that injury was insufficient to satisfy the UCL's and FAL's standing requirements.

The Supreme Court disagreed. The Court's analysis began by examining the purpose of Proposition 64, which was to "eliminate standing for those who have not engaged in any business dealings with would-be defendants," thereby eliminating the ability of such unaffected parties to file "shakedown lawsuits," while also "preserving standing for those who *had* had business dealings with a defendant and had lost money or property as a result of the defendant's unfair business practices." The Court held: "To satisfy the narrower standing requirements imposed by Proposition 64, a party must now (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 that economic injury was the result of, i.e., *caused by*, the unfair business practice or false advertising that is the gravamen of the claim. Under the first element, the Court held that if a plaintiff successfully alleges or proves an "individualized loss of money or property in any nontrivial amount, he or she has also alleged or proven injury in fact." Under the second element, a plaintiff must show that the misrepresentation was the immediate cause of the injury-producing conduct, but is not required to allege that the misrepresentation was "the sole or even the decisive cause" of the same.

The Court then declared that labels matter: consumers will choose one product over another based on its label. Such things as processes and places of origin matter, as consumers may choose one product over another based on "various tangible and intangible qualities they may come to associate with a particular source," such as a desire to support domestic jobs, a belief about quality, concerns about overseas environmental or labor conditions, or simple patriotism. The Court cited as examples kosher foods, conflict-free diamonds, counterfeit Rolexes, and products harvested or manufactured by union workers. For a consumer who relies on such labeling representations, the Court reasoned that he or she has suffered economic harm by paying more for the mislabeled product than he or she otherwise might have been willing to pay – whether or not the product the consumer purchased is the "functional equivalent" of a product actually made in the U.S.A.

The Court held that a consumer who relies on a product label and challenges a misrepresentation contained therein can satisfy the standing requirement of the UCL by alleging that he or she would not have bought the product but for the misrepresentation. The allegations in the present complaint revealed that the plaintiffs valued the lockset as labeled more than the money they paid, that they valued the money paid more than the lockset as it actually is, and that the plaintiffs allegedly paid more than they otherwise would have. That increment – the extra money paid – is economic injury that establishes plaintiffs' standing to sue.

Addressing the conclusions of the Court of Appeal below, the Court found that requiring an allegation that the product was of inferior quality or functionally defective in order to establish standing under the UCL and FAL would detach the consumer's cause of action from its false advertising moorings. The consumer's injury – purchase of a dysfunctional lockset – would now no longer be causally related to the alleged mislabeling. Next, the Court held that, as alleged in the complaint, the plaintiffs did not receive the benefit of their bargain: "[t]hey bargained for locksets that were made in the United States; they got ones that were not." The Court noted that

whether the "Made in U.S.A." representation was a material part of the bargain in the mind of the plaintiffs is an issue of fact, though it suggested that Kwikset intended its representations to be material in the minds of consumers: "Kwikset packaged its products with labels like 'All American Made & Proud Of It' and 'Made in U.S.A.' because it determined such marketing might sway reasonable people in their purchasing decisions."

Justice Chin, in dissent, argues that the majority collapses two distinct requirements for standing under the UCL – that a plaintiff allege injury in fact *and* a loss of money or property. Where the majority holds that allegation of the latter necessarily establishes the former, Justice Chin contends that the majority has merely avoided defining what constitutes "lost money or property." He further argues that "a person has not 'lost' money simply when the money is 'no longer in his or her possession'" because this proposed definition would "encompasses every purchase or transaction where a person pays with money."

Justice Chin also takes issue with a consumer's allegations of subjective intent as a means to establish standing, complaining that it is "simply too low a threshold to meet." He insists the statute as amended by Proposition 64 requires an allegation of "an actual measurable loss of money or property," and that a consumer's personal preference is not reflected in any cost differential between a mislabeled and correctly labeled product. In his view, a consumer's assertion that "I would not have bought the product but for the misrepresentation" cannot be all that is required to satisfy both the cognizable injury requirement and the causation requirement.
Finally, Justice Chin points out that though the majority purports to consider the intent of the electorate in enacting Proposition 64, the proponents of Proposition 64 specifically cited the present lawsuit as an example of the type of "shakedown lawsuit" Proposition 64 was meant to curb.

The Court's opinion leaves two related problems. First, the Court requires a plaintiff to allege an "individualized loss of money or property in any nontrivial amount," but does not define a "nontrivial amount." The problem is that many UCL actions arise in the context of class action lawsuits, which by definition involve "paltry potential recoveries." (*See Amchem Prods., Inc. v. Windsor* (1997) 521 U.S. 591, 617.) Thus, the Court has left an unresolved tension between the standing requirements under the UCL and a significant procedural vehicle used to assert violations of the statute.

Second, the Court also did not articulate a means for measuring the value of the product to the consumer *as labeled* versus the value of the product to the consumer *as it actually is* – the difference between the two being the measure the economic damage the consumer has allegedly suffered. This, as Justice Chin suggests, leaves the measure of economic damage entirely to the subjective whim of the plaintiff-consumer, who will almost certainly allege his or her loss is the entire price paid, claiming the product as-is has no value whatsoever to him or her.

This "subjective" approach condoned by the majority further renders the UCL incompatible with class action treatment because it will require an individualized determination for each class member: that is, what is the mislabeled product worth to each member of the class? This individualized issue would, in most cases, overwhelm class-wide issues.