

6/23/03 Legal Times 60
2003 WLNR 18321437

Legal Times
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June 23, 2003

Volume 26; Issue 25

Section: Commentary and Analysis

**BIG FOOT, BIG MOUTH
NIKE'S FREE SPEECH CLAIM IS JUST AN ARGUMENT FOR FALSE ADVERTISING.**

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The market needs protection against imperfect information. State and federal regulators -- instead of those within the market -- sometimes need to provide this protection. As in any game, there will be times when it is rational for players in the market to misinform others in order to gain a competitive advantage. Enron and other scandals show that the monetary incentives to be gained from not properly providing accurate information to the market can outweigh the chances of, and the penalties that would result from, being caught.

The Supreme Court is now in the process of deciding a case, *Kasky v. Nike Inc.*, that deals with all these issues. In fact, its decision in January to review the case could be a sign that the Court believes that the market can take care of itself, even when some of the most powerful and able players in the market do not have incentive to provide that care.

In *Kasky*, the California Supreme Court held that the commercial speech doctrine encompasses factual statements about labor practices made by a corporation in order to maintain and increase its sales and profits. In response to negative publicity about its labor practices in overseas factories run by foreign subcontractors, Nike issued statements to sponsors, such as university presidents and athletic directors, claiming, among other things, that "workers who make Nike products . . . are not subjected to corporal punishment and/or sexual abuse," and that "Nike pays average line workers double-the-minimum wage in Southeast Asia."

DECEPTIVE AND UNLAWFUL

According to the suit, these statements violate portions of the California Business and Professional Code, which prohibit unfair competition and false advertising. Statements that are intended to promote or maintain sales of a service or product, and that negligently, recklessly, or intentionally misrepresent material facts about the nature of the service or product, are unlawful.

Under the First Amendment, false or misleading statements made in the political realm are protected from governmental regulation. On the other hand, deceptive or untruthful commercial speech may be regulated by states, and even prohibited entirely. Under U.S. Supreme Court precedent, speech is commercial when it is made by a person or

entity "engaged in commerce"; aimed at "actual and potential purchasers"; and comprised of "representations of fact of a commercial nature."

The Supreme Court has set forth three reasons why commercial speech should receive less protection than non-commercial speech. First, the truthfulness of commercial speech is more easily verifiable by its disseminator than news reporting or political commentary. In other words, merchants have firsthand knowledge of their products; news reporters and political commentators, on the other hand, often receive their information second hand. Second, commercial speech is less likely than other speech to be chilled by regulation, because it is motivated by profit, rather than by political or social concerns. Third, government's power to regulate commerce justifies its authority to regulate speech that is inextricably linked to those transactions.

In a 4-3 decision, the California Supreme Court applied these legal principles to Nike's statements and found them to be commercial. According to the court's opinion, Nike is engaged in commerce because it produces, distributes, and sells athletic apparel and footwear. In addition, the court found Nike's statements to be economically motivated because they were directed toward consumers, such as the presidents and athletic directors of major universities. Finally, the factual content of Nike's statements was commercial in nature because they concerned the manner and nature in which Nike's shoes were made.

PROTECTING THE CONSUMER

The California Supreme Court's Kasky decision is a good one because it protects the right of consumers to make informed purchasing decisions. By making a company's factual statements about its labor practices susceptible to regulation under California law, the California Supreme Court has given companies a disincentive against providing consumers with false or misleading factual information about the nature of the products or services being sold.

The right of consumers to make informed purchasing decisions derives from the fact that information is the lifeblood of the modern market. We all have limited funds and time to allocate toward our purchases. And because the market is so complex, it is impracticable to use trial and error to determine which goods and services we will buy and sell. By exchanging product and pricing information with one another, buyers and sellers serve their own self-interests by lowering their search costs immensely.

As a result, tainted information hurts the market. When inaccurate information about a good or service is dispersed into the market, buyers and sellers are not given the chance to allocate their resources in a rational manner.

For example, the cost of the Enron debacle includes the drop in the value of the investors' stock, but also the opportunity cost of the investors' decisions. The funds that were diverted toward Enron stock could have been used for more worthwhile and lucrative causes.

Moreover, the free market cannot be counted on to correct itself all of the time. For one thing, individuals and corporations can profit from breaking market rules. This is true because the penalties associated with the violation are often hard to quantify, and are frequently miniscule when compared with the revenues to be gained.

For instance, the California laws at issue in Kasky generally limit a private plaintiff's remedies to injunctive relief and restitution on behalf of injured California residents. While the amount of restitution may be quantified by disgorging the monies gained from Nike's misleading statements about its labor practices, it is unclear how such a number may be arrived at accurately.

But even if there were an accurate way to determine such a number, the amount would still be inadequate because the suit is only on behalf of California residents, while Nike's business is nationwide. So any restitution awarded in this case will be undervalued. In the end, even with California's penalties, Nike gets a bargain.

Collective action problems also help explain why the market often will not correct itself. Nike has a proverbial war chest to defend its business practices. In 1997, Nike reported annual revenue of \$9.2 billion, with annual expenditures for advertising and marketing of almost \$1 billion. This obviously dwarfs the resources of any single average Nike consumer. Given these unequal resources, it is no wonder that consumers need to harness the power of the state.

Of course, a consumer can boycott Nike, but the effect of the consumer's decision on Nike's bottom line would be negligible. And the consumers whose purchasing or sponsoring decisions have more effect on Nike may not have an incentive to take action. For instance, Nike is a large sponsor of the University of Oregon. So even if the school did not like Nike's labor practices, it receives so much funding that rocking the boat would be costly.

NO SPEECH VIOLATION

Finally, to return to the terms of the legal debate, Kasky does not impinge upon Nike's free speech rights. Nike can still tout the way it treats its labor force. Clearly opinionated statements, otherwise known as "puffing," are not actionable under California's state unfair competition and false-advertising laws. A used car salesman can legally state that his cars are "beautiful looking" even when they are plagued with problems. Likewise, a merchant can claim his laborers are treated "justly" or "with love" without making himself susceptible to liability under California law.

But where, as here, Nike makes objectively verifiable statements about the nature and quality of goods being sold, the company should be truthful. There is no principled distinction for treating such statements about the labor environment in which a product was made differently than any other factual claim regarding the nature of the product. A local coffee retailer is not at liberty to advertise in letters to consumers that her coffee is organic when, in fact, it is not. The rule should be no different for Nike.

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--- INDEX REFERENCES ---

COMPANY: UNIVERSITY OF OREGON; OFFICIAL STARTER LLC; NIKE INC; CVEO CORP

NEWS SUBJECT: (Legal (1LE33); Intellectual Freedoms & Civil Liberties (1IN08); Sales & Marketing (1MA51); Judicial (1JU36); Civil Rights Law (1CI34); Business Management (1BU42))

INDUSTRY: (Footwear (1FO74); Sponsorship (1SP44); Apparel (1AP19); Apparel & Textiles (1AP20); Advertising & Public Relations (1AD83); Sportswear (1SP87); Consumer Products & Services (1CO62))

REGION: (North America (1NO39); USA (1US73); Americas (1AM92); California (1CA98))

Language: EN

OTHER INDEXING: (ARGUMENT; CALIFORNIA; CALIFORNIA SUPREME COURT; COURT; DECEPTIVE; NIKE; NIKE INC; PROTECTING; STATE; SUPREME COURT; US SUPREME COURT; UNIVERSITY OF OREGON) (BIG; Collective; Enron; Finally; Kasky; Likewise; Professional Code; Ryan E. Long; SPEECH VIOLATION)

Word Count: 1530
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