

COMMENTS

WINKING IN THE DARK:* AN ANALYSIS OF CORRECTIVE-ADVERTISING DAMAGES UNDER THE LANHAM ACT AND THE EFFECT ON THE AMERICAN ECONOMY

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*Doing business without advertising is like winking at a girl in
the dark. You know what you are doing, but nobody else does.*

— Joseph Kaselow¹

I. INTRODUCTION

Small businesses are an integral part of the American economy.² They play a crucial role in “technological change and productivity growth.”³ The United States government, recognizing the vital role of small businesses, often creates and disseminates publications stressing their importance.⁴ Despite these efforts,

* Joseph Kaselow, *Advertising Field*, N.Y. Herald Trib. § 2, 9 (Oct. 30, 1956) (quoting Stuart Henderson Britt).

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1. Kaselow, *supra* n. *, at § 2, 9.

2. U.S. Small Bus. Administration, *The New American Evolution: The Role and Impact of Small Firms* <http://www.sba.gov/advo/stats/econ_arch/evol_pap.html> (June 1998).

3. *Id.*

4. *E.g. id.* (describing the role of small businesses in the American economy and

some federal courts interpret the Lanham Act in false-advertising suits in ways that fail to consider the importance of protecting small enterprises.⁵ Specifically, these decisions lower the burden of proof necessary to recover corrective-advertising damages.⁶ In doing so, these decisions threaten the economy and ultimately risk negative long-term consequences to American consumers. To clarify the quandary that could result from the current trend in the law governing false-advertising damages, consider the following hypothetical.

A. Hypothetical

George Jones owns Natural Resources, an organic-food grocery store in his hometown of 100,000 people. It is a small market that sells solely organic products. Natural Resources is the only store of its kind in Jones's hometown, although Michaelson's, a national supermarket chain, has a modestly sized organic section in its store. On a shoestring budget, Natural Resources advertises in the local newspaper each Sunday, announcing its specials for the week.

After experiencing a few years of success with his hometown store, Jones decides to expand and opens additional locations in two neighboring cities. Jones realizes that the success of these new stores will require publicity to establish the Natural Resources name in these new communities, and he hires a production company to create a series of television spots.

Although he seeks creative input from the production company, Jones has distinct ideas about the advertising campaign. During the first few years at his hometown location, Jones used the following tagline in his Sunday newspaper ads: "Your groceries are toxic if they aren't Natural Resources." Jones came up with the slogan after attending a few meetings of his hometown chapter of Healthnuts, a group to which much of his clientele belong. Because Jones finds his slogan quite popular among the

comparing it to that of European nations); *see generally* U.S. Small Bus. Administration, *Small Business Economic Indicators: 2000*, at 5 n. 2 <<http://www.sba.gov/advo/stats/sbei00.pdf>> (accessed Mar. 15, 2002) (defining "small business" as a firm with less than 500 employees, but noting that individual industries may use other statistics). Part IV of this Comment presents in greater detail the Small Business Administration's (SBA) position on the role of small business in the American economy.

5. *Infra* pt. II(D).

6. *Infra* pt. II(D).

Healthnuts in his hometown, he wants to use this line in the advertisements for his new stores.

After a couple of weeks of dealing with the production company, Jones realizes that producing commercials is tedious and more expensive than he originally anticipated. Likewise, the cost of airing a single network-television spot is mind-blowing to the hometown grocer.⁷ However, he understands that the new stores need the exposure to jump-start business and compete with Michaelson's, which already attracts some of the Healthnut-type clientele to its small selection of organic products.

The commercials succeed. In fact, business in each of the new shops exceeds that of his original, hometown location. Jones receives positive feedback from his new customers, many of whom are newly converted organic-food enthusiasts. Every one of his customers expresses relief that they finally have an alternative to Michaelson's supermarket. Jones is relieved that he is able to start paying off massive debts he incurred to start up and advertise his new stores. But Jones's celebration of Natural Resources' success is cut short when he is served with a complaint in which Michaelson's claims that the Natural Resources television commercials constitute false advertising under the Lanham Act. Jones wonders, "What can Michaelson's really expect to recover from a small-time grocer who is barely making ends meet?"⁸

B. Scope of This Comment

The somewhat complex answer to Jones's question lies in the judicial interpretation of the Lanham Act, Title 15 United States Code Section 1125. Laypersons sometimes can recognize ads using "puffing,"⁹ exaggerated, or whimsical claims. However, it is often difficult to distinguish between fact and fiction.

7. *Infra* n. 56 (providing estimates of the cost of television-commercial production and placement).

8. For purposes of this Comment, assume that Michaelson's can prove liability, leaving only the issue of remedies to consider. See Roberta Jacobs-Meadway, *Trademarks, Copyrights, and Unfair Competition for the General Practitioner and the Corporate Counsel* 358-359 (ALI-ABA Course of Study Materials, Course No. SD68, Apr. 29, 1999) (available in WL SD68 ALI-ABA 351) (citing the Fifth, Ninth, and Sixth Circuits as applying a five-element test for false advertising claims).

9. See J. Thomas McCarthy, *McCarthy on Trademarks and Unfair Competition* vol. 4, § 27.38, 27-64 (4th ed., West 2002) (defining puffing as "exaggerated advertising, blustering, and boasting upon which no reasonable buyer would rely" and explaining that puffery is a defense to a false advertising claim); Jean Wegman Burns, *Confused Jurisprudence:*

One of the original purposes of the 1946 Lanham Act was to promote fair competition and to protect consumers from deceitful claims that blur the line between fact and fiction.¹⁰ Today, the Act is part of federal legislation and prescribes remedies such as injunctive relief, market damages, and damage-control costs for competitors harmed by false advertising.¹¹ However, over the years, courts slowly have muddied the waters that define what plaintiffs must prove to obtain one of these remedies.¹² Perhaps this change is due to a scholarly push toward easing seemingly rigid standards for recovery.¹³ Regardless of the cause, easing these standards is dangerous, as demonstrated below.

Before following this trend, courts should evaluate recent decisions in this area and the ramifications on smaller businesses.¹⁴ A heightened threat of incurring mass-media bills that are undeserved might discourage small-business owners from advertising. Also, small-business owners could become vulnerable to large companies that realize their capacity to extinguish less-financially-secure competitors with one lawsuit, especially when a lower burden of proof is available.¹⁵ Because small businesses are the key ingredient to the recipe for a prosperous economy, this threat could have severe consequences.¹⁶ Additionally, modern economic concepts do not support a movement in this direction.¹⁷

Part II of this Comment will acquaint the reader with the legislative and case-law history, as well as the policy considerations underlying the Lanham Act. The Comment then will explore current remedies available to plaintiff competitors for false advertising, including a recent development in the expansion of corrective-advertising awards. Part II also will discuss various scholarly views for interpreting the Lanham Act's language on remedies, which some commentators argue is ambiguous, and discuss the

False Advertising under the Lanham Act, 79 B.U. L. Rev. 807, 883 (1999) ("A prime reason for excluding opinion, puffing, and non-fact from culpability is that buyers do not rely on them in making their purchasing decisions.").

10. McCarthy, *supra* n. 9, at § 27:7, 27-12.

11. *Id.* at § 27:40, 27-71; see 15 U.S.C. § 1117(a) (2000) (prescribing the Lanham Act remedies).

12. *Infra* pt. II(D).

13. *Infra* pt. II(E).

14. *Infra* pt. III.

15. *Infra* pt. III.

16. *Infra* pt. III.

17. *Infra* pt. IV(B).

available remedies for false advertising. Part III introduces the views of the U.S. Small Business Administration (SBA) regarding the importance of small businesses in the economy. Subsequently, Part IV will analyze the false-advertising remedies both historically and under various law-and-economics schools of thought, to demonstrate how higher standards for recovery of corrective-advertising damages are in the best interests of small business, the economy, and ultimately, American consumers. In conclusion, Part V of this Comment will call for judicial conservatism and for congressional intervention to articulate a proconsumer, proeconomy Lanham Act social policy through an amendment to prevent the judiciary's expansion of false-advertising litigation.

II. HISTORICAL BACKGROUND BEHIND FALSE-ADVERTISING LEGISLATION

A. The Evolution of the Lanham Act

The Lanham Act, enacted in 1947 and originally cited as Section 43(a) before it was codified at Title 15 United States Code Section 1125(a), resulted in false-advertising lawsuits as we know them today.¹⁸ The creation of the Lanham Act has been described as the “creation of a ‘new statutory tort’ intended to secure a [marketplace] free from deceitful marketing practices.”¹⁹ The Act afforded broader protection from false advertising than provided at common law, but had a slow start due to narrow judicial interpretations that pigeonholed the Act's applicability to trademark infringements.²⁰ In time, however, the breadth of the Lanham Act's applicability greatly expanded when there was an “explosion of [Section] 43(a) litigation in the 1970s and 1980s” that successfully challenged the belief that the Lanham Act only applied to trademark infringement and not to deceitful statements about products or services.²¹

18. McCarthy, *supra* n. 9, at § 27:7, 27-12. The Act's original purpose was to “create a general federal law of unfair competition,” and included “[Section] 43(a) as a minor, but useful section, which would ease the restrictive requirements of proof in the common law false advertising cases.” *Id.* The drafters' hopes of creating federal unfair competition laws ironically never came to pass, leaving only Section 43(a) as its legacy. *Id.*

19. *Johnson & Johnson v. Carter-Wallace, Inc.*, 631 F.2d 186, 189 (2d Cir. 1980).

20. McCarthy, *supra* n. 9, at § 27:8, 27-16. One scholar described the Act as being “largely dormant for almost thirty-five years.” Burns, *supra* n. 9, at 816.

21. McCarthy, *supra* n. 9, at § 27:8, 27-17.

Ultimately, Congress amended the Act in 1989, taking into consideration more liberal case-law interpretations and adopting federal legislation to protect consumers from false advertising as well as trademark violations.²² Today, the Act has a two-pronged scope.²³ One prong covers trademark infringement, and the other prong covers false advertising, the topic of this Comment.²⁴ Although the two prongs are “separate in their substantive rules and applicability,” they share procedural criteria.²⁵ For example, jurisdiction, standing, and remedial elements are uniform under both areas of the Lanham Act.²⁶

B. Changes in the Lanham Act’s Statutory Language

One explanation for the slow start to modern false-advertising litigation is the statutory language.²⁷ Before 1988, the Lanham Act read as follows:

Any person who shall affix, apply, or annex, or use in connection with any goods or services, or any container . . . for goods, a false designation of origin, or any false description or representation, including words or other symbols tending falsely to describe or represent the same . . . shall be liable to a civil action by any person doing business in the locality falsely indicated as that of origin . . . , or by any person who believes that he is or is likely to be damaged by the use of any such false description or representation.²⁸

The limited legislative history accompanying this language suggested that the Lanham Act’s intent was only to fill gaps in the common law related to unfair competition.²⁹ Nothing in the

22. *Id.*; *infra* n. 32 and accompanying text (providing the amended language of 15 U.S.C. § 1125(a) (2000)).

23. McCarthy, *supra* n. 9, at § 27:9, 27-18. When Congress adopted the Lanham Act, it rewrote and renumbered the subsections, which might be confusing when switching between cases dated before and after the Trademark Law Revision Act of 1988. *See id.* (explaining in detail the changes made to the Lanham Act in 1989).

24. *Id.* Only the false-advertising prong is analyzed in this Comment.

25. *Id.*

26. *Id.*

27. Burns, *supra* n. 9, at 814.

28. *Id.* at 816 (citing 15 U.S.C. § 1125(a) (1982)).

29. *Id.* A common belief is that the *Erie Railroad* decision, a 1938 Supreme Court case that eliminated common-law unfair trade practices, motivated the Lanham Act’s creation. McCarthy, *supra* n. 9, at § 27:7, 27-14 (citing *Erie R.R. v. Tompkins*, 304 U.S. 64 (1938)).

previously adopted language alluded to false advertising in particular.³⁰

However, following the Trademark Law Revision Act of 1988, Congress amended this language and designated a specific section for false advertising.³¹ The amended statute reads:

(A)(1) Any person who, on or in connection with any goods or services, or any container for goods, uses in commerce any word, term, name, symbol, or device, or any combination thereof, or any false designation of origin, false or misleading description of fact, or false or misleading representation of fact, which . . . (B) in *commercial advertising or promotion*, misrepresents the nature, characteristics, qualities, or geographic origin of his or her or another person's goods, services or commercial activities, shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act.³²

Despite this language, which clearly makes the Act applicable to false advertising,³³ the Act still is criticized sharply as lacking any clear legislative intent to guide the judiciary.³⁴ Without such guidance, a question central to corrective-advertising damages remains unanswered: To whom is the Act referring when it purports "to protect persons engaged in such commerce?"³⁵ Whom should the Lanham Act be protecting: competitors or consumers?³⁶

30. Burns, *supra* n. 9, at 814.

31. *Id.* at 820.

32. *Id.* (citing 15 U.S.C. § 1125(a)(1)(B) (1988)) (emphasis added).

33. *Id.*

34. *See id.* at 819–822 (arguing that Congress knowingly dodged false-advertising controversies such as consumer standing); Sen. Rpt. 100-515 at 40-41 (May 12, 1988) (articulating the purpose of 15 U.S.C. § 1125(a) as furthering public policy against unfair competition). This statutory purpose is ambiguous as it fails to pick either competitors or consumers as the primary beneficiary. Burns, *supra* n. 9, at 819–822. This ambiguity spawned a vast collection of issues surrounding false advertising not addressed in this Comment. *Id.*

35. Burns, *supra* n. 9, at 834 (quoting 15 U.S.C. § 1127). The fact that only competitors have standing in false-advertising suits further amplifies the importance of this question.

36. *Id.* Some sources state that consumer protection is the undoubted purpose behind the Lanham Act. McCarthy, *supra* n. 9, at § 27:25, 27-44. Other scholars are not quite as convinced. *Infra* pt. III.

C. Overview of Concepts and Terminology of Lanham Act Remedies

To fully appreciate a discussion focused on corrective-advertising damages, it is helpful to have a basic understanding of each of the Lanham Act remedies. The remedies for false-advertising violations of the Lanham Act are in Title 15 United States Code Section 1117.³⁷ Three types of relief are available to parties subjected to their competitors' false advertising: (1) injunctive relief, (2) market damages, and (3) corrective advertising.³⁸ However, as discussed below, many courts group the second and third types into one group — monetary damages.³⁹ Recall the Natural Resources hypothetical to better understand the following distinctions between the three categories.⁴⁰

A plaintiff-competitor can obtain injunctive relief for false advertising if a plaintiff successfully meets the appropriate burden of proof: "likelihood of damage."⁴¹ This standard requires only a "reasonable basis for the belief that the plaintiff is likely to be damaged as a result of the [defendant's] false advertising."⁴² In the Natural Resources hypothetical, if Michaelson's can show that the Natural Resources advertising campaign had a tendency to deceive, even without actual proof of deception, Jones would have to discontinue using his slogan.⁴³ Michaelson's need show only that the parties compete in a broadly defined market, and that there was a causal connection between any decline in sales, for example, and Jones's advertising.⁴⁴ The total harm alleged does not have to be significant to obtain injunctive relief.⁴⁵

37. 15 U.S.C. § 1117.

38. *Id.* Jacobs-Meadway, *supra* n. 8, at 376. The term "corrective advertising" encompasses two remedies: (1) a defendant's "affirmative corrective statement in future advertising" and (2) damages for plaintiff's self-conducted advertising campaign, also called damage-control costs. *Id.* at 377. In rare cases, attorney's fees are awarded. *Id.* at 376.

39. 15 U.S.C. § 1117; Jacobs-Meadway, *supra* n. 8, at 376.

40. *Supra* pt. I(A).

41. *Johnson & Johnson*, 631 F.2d at 190; McCarthy, *supra* n. 9, at § 27.36, 27-62.

42. *Johnson & Johnson*, 631 F.2d at 190.

43. *See id.* (describing the factors to consider when determining a "likelihood of damage").

44. *See id.* at 189-191 (analyzing the likelihood of damage in a case of two competitors in the hair-removal market). The causal connection must be corroborated by specific evidence such as sales statistics or consumer-witness testimony. *Id.* at 191.

45. *Id.*

Market damages include lost profits, loss of goodwill, lost sales, and even disgorgement of the defendant's profits.⁴⁶ The burden of proof necessary to recover market damages is "actual damage," not speculation, but only harm actually proven to have directly resulted from the defendant's actions.⁴⁷ As a general rule, recovery of damages under the Lanham Act requires a showing of actual damages.⁴⁸ This higher burden is justified because, unlike injunctive relief that directly benefits consumers via protection, monetary damages directly affect only the plaintiff-competitor.⁴⁹ Additionally, constraint is arguably less financially burdensome than the payment of money, causing much less defendant disparity and reducing the risk of plaintiff windfall.⁵⁰ Actual damage is proved most commonly through customer surveys or testimony from dealers, distributors, customers, or experts.⁵¹ However, causation is too remote if the only evidence is a chronology of events.⁵² As noted below in Part II(D), other factors such as the veracity of the defendant's statements and the defendant's intent might be relevant when proving actual damage, but this Comment does not address these issues specifically.⁵³ In the Natural Resources hypothetical, if Michaelson's met the burden of proof for market damages, Jones would owe Michaelson's, for example, the lost sales from the newly converted Healthnuts or the cost of the supermarket's organic food stock.

Corrective advertising can be one of two things.⁵⁴ First, it can be a defendant's own advertisement with a statement retracting and correcting false advertisements of the past, or second, it can be an amount of money awarded to a plaintiff-competitor to be used in correcting perceived false beliefs through its own media

46. Jacobs-Meadway, *supra* n. 8, at 378.

47. *Am. Council of Certified Podiatric Phys. & Surgeons v. Am. Bd. of Podiatric Surgery, Inc.*, 185 F.3d 606, 618 (6th Cir. 1999); McCarthy, *supra* n. 9, at § 27:42, 27-77.

48. *Am. Council of Certified Podiatric Phys.*, 185 F.3d at 614; McCarthy, *supra* n. 9, at § 27:29, 27-49.

49. McCarthy, *supra* n. 9, at § 27:29, 27-49.

50. *Id.* The plaintiff receives only what he or she is already entitled to: "a market free of false advertising." *Johnson & Johnson*, 631 F.2d at 192.

51. *Schutt Mfg. Co. v. Riddell, Inc.*, 673 F.2d 202, 207 (7th Cir. 1982); McCarthy, *supra* n. 9, at § 27:43, 27-77.

52. McCarthy, *supra* n. 9, at § 27:41, 27-72.

53. *Infra* pt. III(D).

54. McCarthy, *supra* n. 9, at § 27:43, 27-78; Jacobs-Meadway, *supra* n. 8, at 377.

campaign.⁵⁵ Either way, a defendant is required to pay for an inevitably costly media budget.⁵⁶ In the Natural Resources hypothetical, Jones might have to pay Michaelson's damages equal to the amount Michaelson's spent to repair misconceptions about the healthiness of its store and products.⁵⁷ Potentially, Michaelson's, not the court, will determine this amount.⁵⁸ The plaintiff's burden of proof for corrective-advertising damages is the central issue of this Comment.

D. Highlights of Relevant Case Law for Lanham Act Remedies

Case law has developed over the years regarding each of the previously described Lanham Act remedies and when these remedies are appropriate.⁵⁹ Historically, there were two generally accepted burdens of proof for Lanham Act remedies: (1) a lower burden for injunctive relief and (2) a higher level applied when monetary awards were at stake.⁶⁰ However, a recent decision in the Sixth Circuit, *Balance Dynamics Corporation v. Schmitt Industries, Incorporated*,⁶¹ deviated from the traditional two-burden method related to seeking false-advertising remedies under the Lanham Act.⁶²

55. Jacobs-Meadway, *supra* n. 8, at 377.

56. Advertising is a multi-billion-dollar industry, grossing \$73.2 billion in 1997. Ronald Goettler, *Advertising Rates, Audience Composition, and Competition in the Network Television Industry 2* <www.gsia.cmu.edu/andrew/goettler/papers/ad-GSIA-1999-E28.pdf> (Aug. 8, 1999). The average cost to produce a thirty-second television spot can range between \$500 and \$350,000. Gary Davis Media, *Television Advertising FAQ* <<http://televisionadvertising.com/faq.htm>> (accessed Mar. 31, 2002). The SBA estimates a production cost of between \$2,500 and \$20,000 and recommends purchasing spots that will be viewed by each customer between five to seven times to be effective. Edmond A. Breneau, U.S. Small Bus. Administration, *Advertising* <<http://www.sba.gov/library/pubs/mt-11.doc>> (accessed Mar. 31, 2002).

57. However, the money spent does not have to "expressly . . . rebut [the false-advertising] claim." *ALPO Petfoods, Inc. v. Ralston Purina Co.*, 997 F.2d 949, 952 (D.C. Cir. 1993). Plaintiffs need to show only that the sole reason for the campaign was to counteract any influence the false ads had on the market. *Id.*

58. District courts have discretion to award plaintiffs up to twice the amount of money the defendant spent on the false-advertising campaign. *U-Haul Intl., Inc. v. Jartran, Inc.*, 793 F.2d 1034, 1041 (9th Cir. 1986). However, when a plaintiff has already performed a corrective-advertising campaign, there is no limit to the amount recovered at trial. *Id.*

59. *Am. Council of Certified Podiatric Phys.*, 185 F.3d at 614.

60. *See id.* (explaining the proof required of defendants depending on "whether damages or injunctive relief is sought").

61. 204 F.3d 683 (6th Cir. 2000), *cert. denied*, 121 U.S. 306 (2001).

62. *Id.* at 689; *infra* nn. 87-94 and accompanying text.

The form of relief under the Lanham Act with the lowest burden of proof is injunctive relief, in which only a likelihood of damage is necessary to satisfy the Statute.⁶³ The United States Court of Appeals for the Second Circuit clearly defined this standard in *Johnson & Johnson v. Carter-Wallace, Incorporated*.⁶⁴ A plaintiff baby-oil manufacturer appealed a district court's dismissal of its suit seeking injunctive relief against its competitor for failing to prove that it suffered actual damages from its competitor's false advertising.⁶⁵ The Second Circuit reversed and remanded the case, stating that "a plaintiff seeking an injunction, as opposed to money damages, need not quantify the losses actually borne."⁶⁶ Instead, the court held that only a reasonable basis is needed to obtain such relief.⁶⁷ In that case, the combined decline in sales, consumer-witnesses' testimony of their switch to the defendant's product, and surveys indicating deceit were sufficient to meet this standard.⁶⁸

In contrast to injunctive relief, the burden to recover monetary damages, such as lost sales, corrective-advertising expenses, and attorney's fees, is higher.⁶⁹ The plaintiff in *Otis Clapp & Son, Incorporated v. Filmore Vitamin Company*⁷⁰ appealed a trial court's denial of unrealized growth potential and its award of only

63. McCarthy, *supra* n. 9, at § 27:26, 27-47. The Lanham Act states that anyone who promulgates false advertising "shall be liable . . . [to] any person who believes that he or she is likely to be damaged by such act." 15 U.S.C. § 1125(a)(1).

64. 631 F.2d at 189-192; *see generally Parkway Baking Co. v. Freihofers Baking Co.*, 255 F.2d 641, 649 (3d Cir. 1958) (stating that an injunction for false advertising requires only a "showing of likelihood of damage" and plaintiffs do not have to "await[] the actuality"); *Black Hills Jewelry Mfg. Co. v. Gold Rush, Inc.*, 633 F.2d 746, 753 (8th Cir. 1980) (affirming the district court's grant of injunction based on a "likelihood of confusion to consumers as to the origin of the [defendant's] products"); McCarthy, *supra* n. 9, at § 27:36, 27-62 (citing cases among various district courts that apply the likelihood-of-damage standard).

65. *Johnson & Johnson*, 631 F.2d at 187-189.

66. *Id.* at 188-189.

67. *Id.* at 190. Only a "logical causal connection" is necessary. *Id.*

68. *Id.* at 191.

69. *See generally Schutt Mfg. Co.*, 673 F.2d at 206-207 (7th Cir. 1982) (stating that a higher burden of proof — actual damage — applies to the recovery of monetary damages, which can be proven through evidence of diverted sales and customer surveys reflecting "actual consumer deception"); *Walker-Davis Publications, Inc. v. Penton/IPC, Inc.*, 509 F. Supp. 430, 437 (E.D. Pa. 1981) (holding that "[w]ithout a showing that the buying public was actually deceived, a claim for damages under [the Lanham Act] cannot succeed"); McCarthy, *supra* n. 9, at § 27:42, 27-77 (explaining the "actual damage" rule and how consumer reliance can be proven through buyer testimony or customer surveys).

70. 754 F.2d 738, 742 (7th Cir. 1985).

limited attorney's fees.⁷¹ The United States Court of Appeals for the Seventh Circuit held that plaintiffs are not entitled to recover if they fail to prove that the defendant, in this case a competitor in the pharmaceutical industry that published false allegations about the plaintiff's products, caused the plaintiff actual harm.⁷² The plaintiff presented testimony from concerned consumers. However, the consumers were "not influenced enough to cease and desist from using [the plaintiff's] products," so the plaintiff failed to prove that even a single customer switched to the competition.⁷³ Additionally, the court found other evidence, using mathematical methods to prove unrealized growth, questionable and insufficient to prove actual harm.⁷⁴ Finally, the court noted that attorney's fees are appropriate in only extreme cases when defendants' Lanham Act violations are "malicious, fraudulent, deliberate, or willful" and that such actions can be mitigated by a plaintiff's "overly aggressive . . . defense" of its trademark, product, or company.⁷⁵ Therefore, the Seventh Circuit affirmed the lower court's decision.⁷⁶

There are three exceptions to the rule that actual damage is required to recover damages.⁷⁷ The United States Court of Appeals for the Ninth Circuit stated the first exception to the normal burden for false-advertising remedies in *U-Haul International, Incorporated v. Jartran, Incorporated*.⁷⁸ In *U-Haul*, the court eased the actual-damage burden of proof and awarded corrective damages without evidence of customer deception, holding that there is a presumption of actual deception when a competitor makes a deliberate publication of false comparative claims.⁷⁹ As an example, the court awarded \$13.6 million even though the defendant spent only \$6 million on its false-advertising campaign.⁸⁰ The court justified this exception with the overall difficulty in proving actual damage, stating that "[h]e who has attempted to

71. *Id.* at 745.

72. *Id.*

73. *Id.* at 741–746.

74. *Id.* at 746.

75. *Id.* at 746–747.

76. *Id.* at 747.

77. *Infra* nn. 78–94 and accompanying text.

78. 793 F.2d 1034 (9th Cir. 1986).

79. *Id.* at 1040–1041.

80. *Id.* at 1037.

deceive should not complain when required to bear the burden of rebutting a presumption that he succeeded.”⁸¹

*PPX Enterprises, Incorporated v. Auto Fidelity Enterprises, Incorporated*⁸² presented a second exception to the actual-damage requirement to recover monetary false-advertising damages.⁸³ In *PPX Enterprises*, the United States Court of Appeals for the Second Circuit held that the literal falsity of a record label advertising recordings by Jimi Hendrix was sufficient to waive the burden of actual damage.⁸⁴ However, the court characterized this as a limited exception because the success of the record implied actual damage.⁸⁵ Literal falsity is not a typical substitute for the actual-damage requirement, although some circuits award injunctive relief for literally false advertising.⁸⁶

Finally, the most recent case to put a new twist on false-advertising remedies is *Balance Dynamics Corporation v. Schmitt Industries, Incorporated*.⁸⁷ In *Balance Dynamics*, the United States Court of Appeals for the Sixth Circuit developed a test for the recovery of corrective-advertising damages based on a likelihood of damage without proof of actual confusion.⁸⁸ The court reasoned that soliciting one’s own customers to prove actual damages to recover for damage control might make plaintiffs “justifiably hesitant to alienate or upset their customers.”⁸⁹ Also, the court deviated from the actual-damage standard out of concern that this burden penalizes successful mitigation efforts and presents practical concerns about the difficulty in proving actual damage.⁹⁰ Therefore, the court held that plaintiffs who are unwilling or unable to meet this higher burden should be entitled to more than

81. *Id.* at 1041; *contra* Garrett J. Waltzer, *Monetary Relief for False Advertising Claims Arising under Section 43(a) of the Lanham Act*, 34 UCLA L. Rev. 953, 968 (1987) (giving three reasons why the *U-Haul* exception is improper: (1) the result was punitive, (2) the plaintiffs received a windfall, and (3) the decision will have an anti-competitive effect because it will encourage predatory litigation).

82. 818 F.2d 266 (2d Cir. 1987).

83. *Id.* at 273.

84. *Id.* at 272–273.

85. *Id.* at 272.

86. *See Balance Dynamics*, 204 F.3d at 694 (citing cases in which injunctive relief is allowed using this standard).

87. *Id.* at 683.

88. *Id.* at 691.

89. *Id.* at 692.

90. *Id.*

just injunctive relief when there is a likelihood of damage.⁹¹ Further, the court denied the plaintiff damages for harm to goodwill, despite the literal-falsity exception,⁹² reasoning that this exception really had never been applied “without other proof that such damages occurred.”⁹³ Therefore, the court distinguished corrective-advertising damages from other monetary-damages awards in this case of first impression in the Sixth Circuit.⁹⁴

Looking back on the Natural Resources hypothetical, this shift in law and policy away from the flat actual-damage requirement for damages makes Jones’s predicament difficult. Are corrective-advertising damages more akin to injunctive relief or to other, monetary “marketplace” damages? Traditionally, it seems courts answered this question with the latter option, holding recovery of these damages requires a higher burden of proof: actual harm.⁹⁵ However, the court in *Balance Dynamics* chose the former option, requiring only a “likelihood of confusion or damages.”⁹⁶ When an entity violates the Lanham Act and promulgates false information about its competitor, should not the burden for recovery of damage-control costs, specifically corrective-advertising damages, be higher than that of injunctive relief, thus requiring actual confusion rather than a mere likelihood of confusion? Although both remedies are designed to prevent consumer confusion, corrective-advertising damages require an out-of-pocket financial expense, whereas injunctive relief simply requires restraint.⁹⁷ Due to the risk of defendant disparity without an actual-confusion requirement, there should be higher standards to recover this money.⁹⁸

91. *Id.* at 692, 693.

92. *Id.* at 693.

93. *Id.*

94. *Id.*

95. Two exceptions apply to this standard, as mentioned above. *Supra* pt. II(E).

96. *Balance Dynamics*, 204 F.3d at 692.

97. Economists may argue that this is a real economic consequence, but injunctive relief restrains only one specific claim, whereas damages preclude all advertising in general with a chilling effect as advertising becomes too financially burdensome.

98. *Infra* pt. IV.

E. Policy and Legislative Intent behind False-Advertising Remedies

The Trademark Law Revision Act of 1988, which revised the Lanham Act's language,⁹⁹ resulted in a great swelling of false-advertising litigation that will continue to expand unless (1) the courts are careful to preserve the Act's intended reach or (2) Congress amends the Act to clarify the Statute.¹⁰⁰ Has lowering the burden of proof for corrective-advertising damages caused litigation to expand too far? The answer depends on which constituency the Lanham Act seeks to protect. Here, the views are diametrical.

Congress designed the Lanham Act to protect the interests of two entities: (1) consumers and (2) "commercial interests."¹⁰¹ Often, these interests coincide.¹⁰² However, when these interests compete with each other, legislative history is not clear about which interest is predominant.¹⁰³

There are at least three viewpoints on what the Lanham Act policy should be and which direction its legislation should take. Some scholars see the policy behind the Lanham Act as plaintiff protection,¹⁰⁴ while others have described the policy as a mixture of plaintiff and competitor protection.¹⁰⁵ The third view is that because false-advertising litigation has created confused jurisprudence on this topic as a result of Congress's failure to articulate the Act's policy, litigation should focus on what is best for the consumer.¹⁰⁶

99. *Trademark Law Revision Act of 1988*, Pub. L. No. 100-667, § 102, 102 Stat. 3935 (1988) (codified as amended at 15 U.S.C. §§ 1116-1118 (2000)).

100. See Bruce P. Keller, "It Keeps Going and Going and Going": *The Expansion of False Advertising Litigation under the Lanham Act* 165 (PLI Corp. L. & Prac. Course Handbook Series No. B4-7202, 1997) (describing the evolution of the Lanham Act as an expansion in litigation).

101. McCarthy, *supra* n. 9, at § 27:25, 27-42; see generally Sen. Rpt. 100-515, at 4 (setting forth the legislative purpose of the Lanham Act: to protect both consumers and producers because "[t]rademarks encourage competition, promote economic growth and can raise the standard of living of an entire nation").

102. See McCarthy, *supra* n. 9, at § 27.25, 27-42 (noting that protecting consumers serves public policy).

103. *Id.*

104. *Infra* nn. 107-110 and accompanying text.

105. *Infra* nn. 111-113 and accompanying text.

106. *Infra* nn. 114-120 and accompanying text.

Professor Arthur Best wrote that the laws governing monetary damages for false advertising are too restrictive.¹⁰⁷ He advocates growth of Lanham Act litigation and takes the pro-plaintiff approach that would make monetary damages more readily available, thus protecting market competitors.¹⁰⁸ Additionally, in Professor Best's view, if more plaintiffs seek monetary damages, this would create a "greater incentive [for businesses] to avoid false advertising" and "strengthen the Federal Trade Commission's ability to regulate advertising."¹⁰⁹ According to Professor Best, the need for greater regulation to control the level of false advertising on the market outweighs what he coins the "windfall phobia."¹¹⁰

A second theory suggests that easing the actual-damages burden of proof for monetary relief might be a more balanced, commercially realistic approach to false-advertising damages.¹¹¹ Underlying this theory is the notion that making monetary damages more readily available through exceptions for both literally and intentionally false information balances the two competing policies: protecting competitors and protecting consumers.¹¹² Scholars who support this theory believe that exceptions to the actual-damages burden of proof are a step in the right direction.¹¹³

A third perspective on the proper policy behind false-advertising litigation is that of Professor Jean Wegman Burns.¹¹⁴ Professor Burns proposes that the law regarding the plaintiff's burden of proof to recover damages is confused as a result of the

107. Arthur Best, *Monetary Damages for False Advertising*, 49 U. Pitt. L. Rev. 1, 3-5 (1987).

108. See *id.* at 5 (citing *U-Haul*, 793 F.2d at 1034, and asserting that the *U-Haul* decision in the Ninth Circuit was a proper, progressive movement toward more liberal awards of all types of damages).

109. *Id.* at 30.

110. See *id.* at 14-35 (posing the argument that courts should distinguish between trademark and false-advertising remedies because injunctive relief is not sufficient for the latter area of law).

111. James M. Keating, Jr., Student Author, *Damage Standards for False Advertising under the Lanham Act: A New Trend Emerges*, 20 Rutgers L.J. 125, 151 (1988).

112. See *id.* at 150 (citing *PPX Enters., Inc. v. Autofidelity Enters., Inc.*, 818 F.2d 649 (3d Cir. 1954) and *U-Haul*, 793 F.2d at 1034, and supporting both the *PPX Enters.* and *U-Haul* decisions).

113. See generally *id.* at 148-150 (citing policy justifications for a lower burden of proof).

114. Burns, *supra* n. 9, at 888.

lack of legislative policy.¹¹⁵ To cure this problem, Professor Burns proposes that the courts follow a policy focused strictly on consumers.¹¹⁶ If the courts follow this purpose, the burden of proof will be clearer.¹¹⁷ Doing so would require plaintiffs' injuries to derive from actual consumer deception.¹¹⁸ Thus, all remedies for false advertising would require plaintiff-competitors to prove some amount of consumer deception that caused harm to the plaintiff-competitor.¹¹⁹ However, if the courts continue to develop exceptions to the actual-damage burden of proof, false-advertising litigation will continue on a trivial path because "competitors cannot be relied upon to pursue those cases of false advertising which are most injurious to purchasers."¹²⁰

III. THE ROLE OF SMALL BUSINESSES IN THE ECONOMY

With a clearer picture of the legal standards Jones faces in this lawsuit, next consider the importance of small businesses, like Natural Resources, to the American economy. Both small business and economic theory, as will be discussed in this section, have a substantial impact on the economy. This section explains how the two influences overlap and explains the cumulative effect they have on the economy. With the aid of this information, one can better understand the impact a lower burden of proof for corrective-advertising damages will have on the economy.

A. Theories about the Role of Small Businesses in the Economy

Austrian economist Joseph Schumpeter is frequently cited for his visionary economic theory, "creative destruction," which stresses the importance of small business in the economy.¹²¹ This is in sharp contrast to the traditional "economies of scale" theory

115. *Id.* at 874.

116. *See id.* at 888 (supporting this shift as a legitimate result of the 1988 Congressional amendments). It is not sufficient to have a dual-purpose approach, protecting both consumers and competitors, because many cases require a tiebreaker when the interests conflict. *Id.* at 876-877.

117. *Id.* at 883-884.

118. *Id.* at 879-880.

119. *Id.* at 879-881. Professor Burns also supports this higher standard with an analogy to federal securities law. *Id.* at 878.

120. *Id.* at 877-878.

121. *E.g.* Gary S. Becker, *Make the World Safe for "Creative Destruction,"* Bus. Week (Feb. 23, 1998) (available in 201998 WL 8130792) (explaining creative destruction as a tool for rejuvenating the economy).

that views the large company as the “cornerstone of the modern economy.”¹²² The traditional theory began to lose ground, most notably around the same time as the Lanham Act began to realize its full potential, in the late 1970s and early 1980s.¹²³

Also within this time frame, in 1976, Congress created the Office of Advocacy of the U.S. Small Business Administration to monitor small business’ impact and function in the American economy.¹²⁴ The Office of Advocacy examines “current and historical data on the small business sector and the state of competition” and compiles the information into various reports.¹²⁵ It is the SBA’s position that influencing the government to “eliminat[e] barriers to entry, lower[] transaction[al] costs, and minimiz[e] monopoly profits by large firm[s]” makes the economy more small-business friendly, and ultimately more stable.¹²⁶ It is not uncommon for Congress or state legislatures to pass legislation that favors these objectives.¹²⁷

University of Chicago Professor and 1992 Nobel laureate Gary S. Becker explains that the biggest hindrance to new, and most often small, businesses is “regulations and red tape.”¹²⁸ Taxes and licenses are some examples of such “red tape.”¹²⁹ Although start-up businesses can be risky, Professor Becker sees them as essential to Schumpeter’s idea of entrepreneurial progress.¹³⁰ “Most [new companies] fail when they try to carry out their ideas. Still, these dreams drive an economy to new heights when encouraged by a sympathetic regulatory atmosphere”¹³¹ Furthermore, two main advantages flow to an economy that fos-

122. U.S. Small Bus. Administration, *supra* n. 2. This theory thrived during the Industrial Revolution. *Id.*

123. *Id.*

124. U.S. Small Bus. Administration, *supra* n. 4, at 2.

125. *Id.*

126. U.S. Small Bus. Administration, *supra* n. 2.

127. See generally Roy Beth Kelley, *Wal-Mart Stores, Inc. v. Am. Drugs, Inc.: Drawing the Line between Predatory and Competitive Pricing*, 50 Ark. L. Rev. 103 (1997) (examining both federal and Arkansas law regarding “the pricing bar in advertising retailing”). Although not a result of SBA efforts, legislation such as the Robinson-Patman Act and the Sherman Antitrust Act are examples of federal laws that promote small-business welfare by preventing retail monopolies. *Id.* at 108–115.

128. Becker, *supra* n. 121.

129. *Id.*

130. *Id.*

131. *Id.*

ters small business: (1) job growth and (2) renewal of existing large corporations.¹³²

B. SBA's Statistics on the American Economy

In a 1998 report, the SBA outlined the two competing economic theories¹³³ on the role of small businesses and further supported the reasoning behind abandoning the old "economies of scale" viewpoint.¹³⁴ As opposed to the "static theory," which promotes the policy of "shift[ing] economic activity away from small firms and toward large enterprises,"¹³⁵ the SBA argues for the "dynamic theory," which has a public policy "to implement policies that encourage the entry of new firms, support their survival, and promote their growth."¹³⁶

The SBA gives two broad reasons for adopting the "dynamic theory" of small business efficiency.¹³⁷ First and foremost, small businesses renew the economy's market structure.¹³⁸ Second, small businesses serve a derivative social function when they "creat[e] opportunities for women, minorities[,] and immigrants."¹³⁹

Unlike the old industrial economy, the "information economy" demands change.¹⁴⁰ The constant entry of new small-sized businesses satisfies this need.¹⁴¹ At first glance, this "[m]assive reshuffling of factors of production" might seem to be a disadvantage, yet "[m]arket economies seem to handle this overwhelming 'churn' with remarkable success."¹⁴² Meanwhile, it is this "churn" that stimulates the advancement of technology and a growing job market.¹⁴³ In fact, in the last five years, "almost half of the net

132. *Id.*

133. U.S. Small Bus. Administration, *supra* n. 2 (comparing in detail the "static theory" versus the "dynamic theory," the latter of which SBA supports).

134. *Id.* The statistics compiled in this report are compelling, even taking into consideration that the SBA is in the business of promoting small business.

135. *Id.* (citing Leonard W. Weiss, *The Structure-Performance Paradigm and Antitrust*, 127 U. Pa. L. Rev. 1104 (1979)).

136. *Id.*

137. *Id.*

138. *Id.*

139. *Id.*

140. *Id.*

141. *See id.* (stating that "[a]bout 10–16 percent of firms are new each year and about 9–14 percent exit each year").

142. *Id.*

143. *Id.*

new employment increase” was a result of new businesses in manufacturing industries.¹⁴⁴ Astonishingly, between 1990 and 1995, new businesses accounted for sixty-nine percent of all new jobs in this country.¹⁴⁵ Under the “dynamic theory” of small businesses, “small firms are needed to provide the entrepreneurship and variety required for macroeconomic growth and stability.”¹⁴⁶

The second function of small businesses in the economy is one of a socioeconomic nature, providing women, minorities, and immigrants with greater opportunity to enter the business world.¹⁴⁷ Interestingly, “since the 1970s, women’s share of small business[es] increased from 5 percent to 38 percent,” and between the years of 1987 and 1992, minority business ownership increased 3.7 percent.¹⁴⁸ Furthermore, a study suggests that ethnic entrepreneurship plays a particularly important role in the economy because individuals with ethnically diverse backgrounds are more likely to “build[] a community and develop[] networks, and therefore will grow and prosper in the future.”¹⁴⁹

IV. ANALYSIS OF THE LANHAM ACT AND ITS JUDICIAL INTERPRETATION

The court in *Balance Dynamics* awarded corrective-advertising damages without requiring proof of actual confusion.¹⁵⁰ In its opinion, the Sixth Circuit expressed concern that a higher burden would penalize successful mitigation efforts, alienate customers, and be impractical because proving actual confusion is difficult.¹⁵¹ From both a historical and law-and-economics standpoint, it was improper for the Sixth Circuit to lower the burden of proof for corrective-advertising damages.

144. *Id.*

145. *Id.*

146. *Id.* Statistical information about Europe’s economy further supports the theory that “creative destruction” and the dynamic view of small businesses are superior to an all-large-firm economy. *Id.* In Europe, governments put up many of the barriers to new business that Professor Becker discourages. Becker, *supra* n. 121. The result is “essentially no overall employment growth in the private sector in recent decades” and, unlike the U.S., where the wealthiest companies are only a few decades old, Europe’s largest companies have become old without any threat of “small companies [growing too] big.” *Id.*

147. U.S. Small Bus. Administration, *supra* n. 2.

148. *Id.*

149. *Id.* (emphasis omitted).

150. 204 F.3d at 686.

151. *Id.* at 692.

Under a historical analysis, this holding is contrary to legislative history, other judicial decisions, and basic principles that have emerged in this area since the Lanham Act's enactment over fifty years ago.¹⁵² Put simply, this standard is not in accord with the Lanham Act's social policy, because it puts small-business owners, such as Jones, at a competitive disadvantage and harms the economy as a result. Ultimately, this creates a substantial risk to all American consumers, who could face a decline in the quality of the economy. This concern greatly outweighs the Sixth Circuit's concern that occasionally surveying customers would alienate a nominal amount of customers.

Additionally, the position that the choice to lower the burden of proof was incorrect is backed by an analysis from the law-and-economics perspective, which finds the lower burden inefficient.¹⁵³ Analysis using two law-and-economics models shows that, due to the high costs of media, simply requiring a likelihood of damage is inefficient and jeopardizes the future of Natural Resources, the hypothetical grocery store, and other smaller-sized market competitors, placing them at a high risk of incurring devastating costs.¹⁵⁴

A. Historical Analysis

Case law, statutory language, and the social policy found in the Lanham Act's legislative history all contradict the Sixth Circuit's decision to lower the burden of proof for corrective-advertising damages.¹⁵⁵ There are two major points to support this argument. First, the award is monetary, and should be treated as such.¹⁵⁶ Second, whether the policy is to protect consumers or to protect both consumers and competitors, lowering the burden of proof will not have any overall positive effect on consumer welfare.¹⁵⁷

152. See *supra* pt. II(D)–(E) (providing legislative history, case holdings, and basic principles that have emerged since the Act).

153. *Infra* pt. IV(B).

154. *Supra* nn. 95–98 and accompanying text (explaining the potential for defendant disparity under the *Balance Dynamics* exception to the actual-damages burden for monetary damages).

155. *Supra* pt. II(D)–(E).

156. *Infra* nn. 158–169 and accompanying text.

157. *Infra* nn. 170–175.

The most obvious argument against the Sixth Circuit's decision is that corrective advertising clearly requires a monetary expense.¹⁵⁸ Therefore, if Congress or other circuits intended to distinguish corrective advertising from the monetary damages category, which the Sixth Circuit found appropriate, a term this general would not accomplish that intent.¹⁵⁹ The *Balance Dynamics* court tried to differentiate between the two remedies by calling one remedy corrective-advertising damages, and the other "marketplace damages," thus renaming and reclassifying the other monetary remedies.¹⁶⁰ However, the inescapable fact is that whether purchasing media or paying damages to a plaintiff, both categories of corrective advertising involve spending money.¹⁶¹

Courts traditionally have held that, under the Lanham Act, monetary damages require proof of actual harm.¹⁶² This precedent is clear and rational because it protects defendants from disparity.¹⁶³ Because corrective-advertising damages are monetary, it is logical that this remedy be held to a similar standard. The Sixth Circuit tried to distinguish corrective-advertising damages from other monetary damages, stating that corrective-advertising damages had never been awarded separate from other forms of monetary damages.¹⁶⁴ The court went further, justifying its position with an argument that other circuits never have expressly held that the actual-damage standard is necessary to award corrective-advertising damages.¹⁶⁵

158. *Supra* nn. 54–56 and accompanying text (describing the two general categories of corrective advertising).

159. *See Balance Dynamics*, 204 F.3d at 692 (rationalizing that "[a]lthough [no] . . . court[] ha[s] awarded [corrective-advertising damages] in the absence of [actual] damage[], none have treated [actual] injury as a prerequisite to recovery of [corrective-advertising damages]"). In contrast to the *Balance Dynamics* court's language, Title 15 United States Code § 1117(a), which provides the Lanham Act remedies, speaks to the award of damages with respect only to actual damage. The statute states that "the plaintiff shall be entitled . . . [to damages] . . . subject to the principles of equity," which is limiting language — the opposite of lowering the burden. 15 U.S.C. § 1117(a).

160. *Balance Dynamics*, 204 F.3d at 691. The *Balance Dynamics* court creates new vernacular not used by other circuits, nor does this term appear in the Lanham Act. 15 U.S.C. §§ 1117(a), 1125(a).

161. *See supra* nn. 54–58 and accompanying text.

162. *Johnson & Johnson*, 631 F.2d at 189; *supra* nn. 69–76 and accompanying text.

163. *Supra* nn. 114–120 and accompanying text (presenting Professor Burns's theory that a higher burden of proof furthers the policy behind the Act).

164. *Balance Dynamics*, 204 F.3d at 693.

165. *Id.* at 690–691.

Conversely, judicial opinions frequently use the terms “damages” and “monetary damages” interchangeably.¹⁶⁶ Until *Balance Dynamics*, the burden of proof for all forms of monetary relief has been distinguished from injunctive relief.¹⁶⁷ No other court has allowed for a lower likelihood-of-damage standard, with two exceptions.¹⁶⁸ Monetary damages, without proof of actual damage, have been allowed only when information is either intentionally or actually false, and only when the likelihood-of-damage standard is arguably rational.¹⁶⁹

The second reason why the court incorrectly decided *Balance Dynamics* is based on public policy, and specifically, the importance of fostering economic growth through small businesses similar to Natural Resources. This is true regardless of whether the Lanham Act has a dual policy to protect both consumers and competitors, and it is especially true if the Act’s main focus is on the consumer.¹⁷⁰ On the surface, while the objective of achieving full truth in advertising seems to give customers the optimal environment in which to make purchasing decisions,¹⁷¹ there is a negative side to lowering the burden of proof.

Although consumers could benefit if Congress and the judiciary ensure that only the full truth is disseminated via corrective advertising, there is a high risk of defendant disparity that may intimidate and discourage advertising altogether.¹⁷² The most likely group of market participants to avoid this risk are the newer, smaller business entrants — such as Jones and his new-concept organic grocery store — who are struggling to get on their feet.¹⁷³ Advertising is a clear and fast way for businesses to draw

166. Compare e.g. *Hot Wax, Inc. v. Turtle Wax, Inc.*, 191 F.3d 813, 819–820 (7th Cir. 1999) (stating that “[monetary] damages under the Act” require proof of actual damage (emphasis added)); with *Badger Meter, Inc. v. Grinnell Corp.*, 13 F.3d 1145, 1156–1158 (7th Cir. 1994) (analyzing the trial court judge’s calculation of “monetary damages” also using the phrase “plaintiff’s damages” (emphasis added)).

167. *Supra* pt. II.

168. *Supra* pt. II(D) (explaining the exceptions created in *U-Haul* and *PPX Enters.*).

169. *Contra supra* nn. 114–120 and accompanying text (presenting Professor Burns’s argument that all Lanham Act remedies should require actual damage).

170. *Supra* pt. II(E).

171. See Lee Goldman, *The World’s Best Article on Competitor Suits for False Advertising*, 45 Fla. L. Rev. 487, 491–492, 508–514 (1993) (contending that truthful advertising has distinct advantages including an improvement in quality decisionmaking).

172. See *id.* at 508–512 (suggesting that a threat of litigation has a chilling effect on truthful advertising, especially in comparative advertising); *supra* pt. II(C).

173. This is especially true if, as in many small businesses, the owner invested his

customers, but an attempt to carve out their niche might be dissuaded if owners think their competitors will scrutinize their ads for a reason to bring a lawsuit.¹⁷⁴ Ultimately, consumers everywhere will feel the effects of a stagnant economy and unemployment if small businesses fail because of lack of advertising.¹⁷⁵

Therefore, the legislative intent of protecting consumers from false advertising is not furthered when awarding corrective-advertising damages on only a likelihood-of-damage, rather than proof-of-actual-damage premise.¹⁷⁶ The court's paternalistic actions actually have created a remedy that results in damage at the expense of an unassuming advertiser.¹⁷⁷ Consumers do not need protection if a plaintiff cannot survey enough consumers who were "actually harmed or deceived."¹⁷⁸ An inability or unwillingness to provide proof of actual damage suggests that an advertisement subject to a suit for corrective-advertising damages was minimally effective.¹⁷⁹ When the *Balance Dynamics* court lowered

personal wealth. Even assuming that small-business owners tend to take more risks, the risk of litigation is an unnecessary addition to the long list of already-existing barriers to market entry. See generally U.S. Bus. Rep., *Specialty Retailing Industry Profile* <http://www.activemedia-guide.com/specialtyretailing_industry.htm> (accessed Apr. 4, 2002). For example, specialty retailers, such as Jones's organic-food store, face "[w]eak or no price flexibility, [l]ittle [c]ustomer [l]oyalty, [u]npredictable [s]ales, [and] [i]ntense [p]rice [c]ompetition." *Id.*

174. Burns, *supra* n. 9, at 808 (calling Lanham Act suits "a proverbial 800-pound gorilla in the legal wars between [competitors]"). Professor Burns's position is that, as the Lanham Act case law stands today, false-advertising litigation has the potential to be a "potent new weapon." *Id.* at 810.

175. See U.S. Small Bus. Administration, *supra* n. 4, at 5 (boasting that small businesses accounted for approximately "three quarters of the employment growth . . . in the 1990s"); *supra* nn. 147-149 (presenting an argument that small business has a positive socio-economic effect as well). Yale Law Professor, Second Circuit Judge, and Economist Guido Calabresi theorizes that

[i]ndustries with more than their share of unforeseeable losses — and, as a result, more than their share of bad years or failures — get reputations for being risky. Fewer firms enter such industries and, over time, higher prices prevail. . . . In such cases undesirable secondary social and economic losses would . . . follow.

Guido Calabresi, *Some Thoughts on Risk Distribution and the Law of Torts*, in *Foundations of the Economic Approach to Law* 42, 49-50 (Avery Wiener Katz ed., Oxford U. Press 1998).

176. Sen. Rpt. 100-515, at 1. "The purpose of the Trademark Law Revision Act of 1988 is to . . . improve the law's protection of the public from counterfeiting, confusion, and deception." *Id.*

177. *Supra* nn. 118-120 and accompanying text.

178. See *supra* nn. 118-120 (stating Professor Burns's theory that a lower burden for injunctive relief does not further the Lanham Act policy because plaintiff-competitor harm should be derived from consumer harm).

179. If false advertising were effective, plaintiff-competitors would have no difficulty

the burden to likelihood of damage, it also made the incorrect assumption that consumers are naive.¹⁸⁰ Furthermore, the *Balance Dynamics* court's concerns would be better served with a hardship exception,¹⁸¹ rather than the court's blanket exception to award corrective-advertising damages after a plaintiff displays only a minimal possibility of harm.

In conclusion, a careful legal analysis reveals that the court's logic is flawed. *Balance Dynamics*' holding, which lowered the burden of proof for corrective advertising, is contrary to existing-case law, legislative intent, and statutory language.¹⁸² Though it believed it was within its limits, the court stepped far outside the historic confines of legal precedent, and it may have caused consumers more harm than good in the long run because this holding may make other small-business owners, like Jones, skeptical of the risks involved with advertising.¹⁸³ We now turn to the law-and-economics analysis.

B. Corrective Advertising Damages under a Law-and-Economics Analysis

Not only does the Sixth Circuit's lowering of the corrective-advertising burden of proof fail traditional legal analysis, but it also fails a law-and-economics examination. Economic analysis differs from traditional analysis in that it is used to predict how specific laws can be used to mold a body of law into a form that produces the most efficient results.¹⁸⁴ As opposed to the usual factual analysis, many of the theorems are "based on simplified and sometimes counterfactual assumptions."¹⁸⁵ The two methods of

surveying and documenting this evidence. Furthermore, the problem of consumers misperceiving the plaintiff's product would greatly outweigh the plaintiff's concern with alienating a sample of its customer base. *Contra Balance Dynamics*, 204 F.3d at 692 (listing fear of client alienation as one of the concerns with the actual-damage burden of proof for corrective advertising).

180. See generally Goldman, *supra* n. 171, at 495–496 (presenting Professor Lillian BeVier's theory "that false advertising does not pose a major threat to consumers," but then offering an alternate hypothesis).

181. This kind of exception would exclude small businesses entirely or offer a less burdensome solution for small businesses.

182. *Supra* pt. IV(A).

183. *Supra* n. 175 and accompanying text (suggesting that the economy's health is in jeopardy).

184. *Foundations of the Economic Approach to Law*, *supra* n. 175, at 5 (providing the editor's introductory remarks).

185. *Id.*

analysis contrast in that “[e]conomics is not an abstract search for truth, . . . but an applied science, a pragmatic endeavor designed to serve human purposes.”¹⁸⁶ Therefore, the resulting prediction is most important to this analysis, not the precision of the facts assumed in achieving this end result.¹⁸⁷

Similar to the dynamic economic model, which favors lower market-entry barriers for new small-business owners, the traditionally applied actual-damages burden of proof for corrective-advertising damages advances consumer protection.¹⁸⁸ In other words, lowering the burden of proof to that of injunctive relief is a law that adds to the proverbial “red tape” that hinders the efficient start and operation of small businesses such as Natural Resources, thereby ultimately giving consumers fewer choices in the marketplace.¹⁸⁹

1. Introduction of Law-and-Economics Theory

When approaching the issue on the propriety of corrective-advertising damages using a lower burden of proof from a law-and-economics standpoint, we must rephrase the issue slightly. First, using economics, one wants to know whether it is efficient to award corrective-advertising damages without proof of actual damages.¹⁹⁰ Second, if the law or standard is efficient, What is the best way to minimize the transactional costs? To resolve these two issues, the pivotal economic focus is on externality: whether legal rules are needed to control resource allocation.¹⁹¹

In theory, competitive markets will assure efficient resource allocation.¹⁹² However, this assumes full information and equal opportunity.¹⁹³ Otherwise, there is market failure — the main category of which is externality.¹⁹⁴ There are two economic theo-

186. *Id.*

187. *Id.*

188. *Supra* nn. 133–146 and accompanying text (defining and describing the reasoning of the dynamic economic model).

189. *Supra* n. 128–129.

190. *See generally Foundations of the Economic Approach to Law, supra* n. 175, at 39 (providing the editor’s commentary and explaining that “[t]he branch of economics dealing with efficient-resource allocation is known as *welfare economics*” (emphasis in original)).

191. *Id.* at 39–40.

192. *Id.*

193. *Id.*

194. *Id.* at 40. “Externality” is described as the social costs of private activity or transactions. Michael J. Swygert & Katherine Earl Yanes, *A Unified Theory of Justice: The*

ries that analyze the best way to “internalize” or fix externality: the Model of Market Failure and the Model of Cooperation.¹⁹⁵

2. *Two Schools of Thought on Public Control over Resource Allocation*

First, consider the Model of Market Failure, which supports the theory that legal rules are the best way to ensure resource allocation and is the traditional view of law and resource allocation.¹⁹⁶ This theory, whose most notable scholar is former Yale Law Professor and Second Circuit Judge Guido Calabresi, views torts as a “regulatory regime for the control of externalities.”¹⁹⁷ Using this approach, by creating damages awards, laws are effective tools to internalize costs.¹⁹⁸ This model, sometimes called the Pigouvian Model, is generally pro-governmental because it advocates state intervention by way of damages alone, not taxes or subsidies.¹⁹⁹

However, Professor Robert Cooter’s theory on the Model of Market Failure states that tort laws that induce mechanisms of precaution for both the injurer and the victim (double responsibility) are the most efficient way to allocate the cost of harm and minimize social costs.²⁰⁰ Therefore, there is an imbalance of precaution when liability is assigned without fault.²⁰¹ For example, when laws impose damages based on strict liability, the victim has no incentive of precaution.²⁰² Similarly, when there is no liability, one who might injure another has no incentive to take precaution against hurting others.²⁰³

Integration of Fairness into Efficiency, 73 Wash. L. Rev. 249, 266 n. 71 (1998).

195. *Foundations of the Economic Approach to Law*, *supra* n. 175, at 40–41 (providing the editor’s comments on competing economic models of law).

196. *Id.* at 39.

197. *Id.* at 40. This model of economic analysis is applicable to the corrective-advertising-damages issue because the Lanham Act has been described as a statutory tort. *Johnson & Johnson*, 631 F.2d at 189.

198. *Foundations of the Economic Approach to Law*, *supra* n. 175, at 40 (providing the editor’s comments on competing economic models of law).

199. *Id.*

200. Robert Cooter, *Unity in Tort, Contract, and Property: The Model of Precaution*, in *Foundations of the Economic Approach to Law*, *supra* n. 175, at 52–59.

201. *Id.* at 53.

202. *Id.* Professor Cooter uses “precaution . . . as a term of art . . . to refer to any action that reduces harm.” *Id.* at 52.

203. *Id.* at 53.

Professor Cooter proposes three common-law mechanisms that provide incentives for efficient precaution by way of damages.²⁰⁴ The first is the “Fault Rule,” which is like negligence in the sense that the “injurer takes efficient precaution to avoid legal responsibility and the victim takes efficient precaution because she bears residual responsibility.”²⁰⁵ The second common-law mechanism is called “Invariant Damages.”²⁰⁶ Like liquidation of damages in contract law, the “promisor balances the cost of precaution against the stipulated damages and the victim balances the benefits of reliance against the potential loss.”²⁰⁷ The third and final mechanism that can ensure efficiency in precaution in tort law is a “Coercive Order” from the court.²⁰⁸ This is an injunction that, when used as a “bargaining chip,” can help victims gain “compensation by private agreement with the injurer,” and thus parties will create efficient allocation of resources.²⁰⁹

The second school of thought on government control over resource allocation is the Model of Cooperation.²¹⁰ This theory’s best-known advocate is Nobel Prize winner and University of Chicago Professor Emeritus Ronald Coase.²¹¹ Professor Coase views the government, the market, and private businesses as alternative entities who can conserve “transactional costs.”²¹² However, despite the method applied to attempt to internalize what the Model of Market Failure calls externality, there will always be some level of transactional cost.²¹³

Externality is not a good enough reason to rely blindly on government laws because there will always be transactional costs.²¹⁴ Sometimes, private entities may be more efficient in solving the externality problem.²¹⁵

204. *Id.* at 59.

205. *Id.*

206. *Id.*

207. *Id.*

208. *Id.*

209. *Id.*

210. See *Foundations of the Economic Approach to Law*, *supra* n. 175, at 41 (providing the editor’s commentary and citing Ronald Coase, *The Problem of Social Cost*, in *Foundations of the Economic Approach to Law*, *supra* n. 175, at 63–72).

211. *Id.*

212. *Id.*

213. Ronald Coase, *supra* n. 210, at 72.

214. *Id.*

215. *Id.*

Professor Coase recommends that, if one truly wants to form the best social policy on handling harmful effects, studies should be conducted to examine how parties handle the harmful behavior.²¹⁶ Moreover, the Model of Cooperation's main theme is that knee-jerk government intervention should not be the norm.²¹⁷ A common problem with governmental regulations is that they are too general, and often they apply to cases for which they were not intended.²¹⁸ Therefore, the government should be viewed as only one of several alternative powers "which might . . . get some things done at a lower cost than could a private organization."²¹⁹

3. Analysis Using Both the Model of Market Failure and the Model of Cooperation

Even under the pro-government regulation standard of the Model of Market Failure, awarding corrective-advertising damages with only a likelihood-of-harm standard is inadequate because potential plaintiffs, such as Michaelson's supermarkets, are not influenced to take precaution against the potential harm of advertising.²²⁰ This standard is similar to strict liability in that Jones or other market competitors bear all the advertising risks because Michaelson's will not make advertising efforts of its own to prevent injury, perhaps by advertising its own organic selection, if it knows that it can recover easily an advertising budget from its competitor.²²¹

Conversely, if Jones had no liability for his advertisements, Michaelson's would bear all responsibility to prevent injury.²²² Under the Model of Market Failure, a standard of actual harm, proven via customer surveys or testimony, is a much more balanced approach.²²³ With this burden, market competitors must use

216. *Id.*

217. *Id.*

218. *Id.*

219. *Id.*

220. See Cooter, *supra* n. 200, at 53 (explaining that the level of liability imposed by the court "will determine [a market competitor's] incentives for precaution. . . . [S]trict liability . . . lack[s] incentives for [a] . . . part[y] to take precaution," and is inefficient.).

221. See *id.* (using a hypothetical of two individuals engaged in harmful activity to show how strict liability reduces the individuals' precaution levels).

222. See *id.* (using a hypothetical to describe how no liability reduces the harming individual's level of precaution).

223. See *id.* at 54 (explaining that fault-based laws achieve the desired objective of "double responsibility").

caution when advertising because if their competitors can show that consumers were misled, they may be liable to pay to correct the misconception.²²⁴ Likewise, because it is not easy to recover corrective-advertising damages, market competitors also must make efforts to keep the public informed about their products so that customers will not be easily persuaded.²²⁵

Therefore, the law as it stood before the Sixth Circuit reinterpreted the Lanham Act is more efficient from the Model of Market Failure standpoint.²²⁶ Professor Cooter's theory supports the idea that an "actual damage[s]" burden of proof for corrective-advertising damages will ensure a balanced precautionary effort between competitors in general.²²⁷

Utilizing the Model of Cooperation, the low burden of proof for corrective-advertising damages also fails. Professor Coase's theory would suggest that a study of retailers, such as Natural Resources and Michaelson's, is appropriate before lowering the burden of proof for corrective advertising.²²⁸ The availability of such damages under the Model of Cooperation analysis may be nonexistent in some instances.²²⁹ The reasons the study is likely to turn out in favor of keeping the old burden of proof are discussed below.

False advertising is a transactional cost of doing business.²³⁰ Both Jones and Michaelson's should expect some false information in the marketplace, and thus, be encouraged to attempt to correct this problem through bargaining and negotiations with one another.²³¹ Although the administration of such negotiations may have transactional costs, this method is potentially much more economically efficient than an automatic award of correc-

224. *See id.* ("Under any fault rule, the injurer can escape responsibility by satisfying the legal standard, so an efficient legal standard will cause his behavior to be efficient.")

225. *See id.* ("[T]he victim's precaution will be efficient because he bears residual responsibility and thus internalizes the cost and benefits of precaution.")

226. *Supra* nn. 220–225 and accompanying text.

227. *Supra* nn. 223–225 and accompanying text.

228. *See Coase, supra* n. 210, at 63–72 ("All solutions have costs, and there is no reason to suppose that governmental regulation is called for simply because the problem is not well handled by the market . . .").

229. *Id.* at 70.

230. *Id.* at 69 (using a hypothetical to explain how private negotiations can have more efficiency in transactional costs).

231. *Id.*

tive-advertising damages.²³² The Model of Market Failure is used to theorize that laws awarding damages totally internalize the false-information transactional cost.²³³ However, government regulation itself is not free from transactional costs.²³⁴

When there is only a likelihood of consumer misconception, bargaining or even publicly broadcasted competition between Jones and Michaelson's will produce the most efficient results, minimizing both Michaelson's and consumer injury.²³⁵ Because the likelihood-of-damage standard warrants only a minimal remedy (injunction) through the court system, the parties would be motivated to remedy the situation themselves, either through negotiations or a more vigorous advertising strategy.²³⁶

This conclusion is further supported by the chance that Jones could be put out of business due to corrective-advertising costs that he may or may not have caused, thus making this level of judicially imposed damages even more costly than necessary.²³⁷ If parties are required to meet a higher burden of proof to recover corrective-advertising damages, they will be encouraged to self-correct the problem of false information before resorting to a suit for these damages.²³⁸ Additionally, because "injured" competitors have adequate remedies already, there is no other justification for a lessened burden of proof on corrective-advertising damages.²³⁹

V. CONCLUSION

After analyzing legislative history, seminal cases in the development of the Lanham Act, and various models of law-and-

232. See *id.* at 72 ("[G]overnment has powers which might enable it to get some things done at a lower cost than could a private organization[,] . . . [b]ut the governmental administrative machine is not itself costless.").

233. *Foundations of the Economic Approach to Law*, *supra* n. 175, at 40 (providing the editor's comments on competing economic models of law).

234. See Goldman, *supra* n. 171, at 512 (listing the expense of time and money in litigation, as well as the possibility of error, as two examples of costs associated with false advertising lawsuits).

235. *Supra* n. 233 and accompanying text.

236. *Balance Dynamics*, 204 F.3d at 696.

237. *Supra* n. 223 and accompanying text.

238. *Supra* n. 233 and accompanying text.

239. Compare Burns, *supra* n. 9, at 874-877 with *Balance Dynamics*, 204 F.3d at 691-692 (disagreeing on whether the consumer or the competitor is the focus of the Lanham Act, thus disagreeing on the appropriate burden for Lanham Act remedies).

economics analysis, judicial application of a lower burden to recover corrective-advertising costs is unsupported.

To better help Jones with his question regarding his liability resulting from his advertising campaign, a preliminary matter must be addressed. Are corrective-advertising damages more akin to injunctive relief or to other, monetary “marketplace” damages?²⁴⁰ Barring the two exceptions for deliberate, false comparative claims and literally false advertisements, courts traditionally have required proof of actual harm.²⁴¹ However, in *Balance Dynamics*, the United States Court of Appeals for the Sixth Circuit required only a “likelihood of damage.”²⁴² If the courts in Jones’s jurisdiction followed the Sixth Circuit’s lead, Jones would be the first of many small-business owners to be exposed to the potentially devastating costs of paying for a competitor’s advertising campaign.

When an entity violates the Lanham Act and promulgates false information about its competitor, the burden for recovery of damage control costs, specifically corrective-advertising damages, should be higher than that of injunctive relief, thus requiring actual confusion rather than a likelihood of confusion. This choice makes more sense because precedent has treated corrective advertising this way, and this choice makes better policy because it provides more economic benefit to consumers.²⁴³ A higher standard promotes a healthy economy, rich with lower market-entry barriers for small businesses like Natural Resources.²⁴⁴

Also, even the more analytic approach of law and economics disfavors the Sixth Circuit’s decision.²⁴⁵ A lower burden is similar to strict liability, which prevents efficient prevention measures and is an economically disfavored form of government regulation.²⁴⁶ Furthermore, neither the government nor the judiciary may be able to reduce transactional costs as efficiently as the parties themselves.²⁴⁷

240. *Supra* pt. II(C).

241. *Supra* pt. II(D).

242. *Supra* nn. 87–94 and accompanying text.

243. *Supra* nn. 150–154 and accompanying text.

244. *Supra* pt. III.

245. *Supra* pt. IV(B).

246. *Supra* nn. 120–121 and accompanying text.

247. *Supra* nn. 228–236 and accompanying text.

Corrective-advertising damages are just one facet of what scholars see as confused jurisprudence in Lanham Act interpretation.²⁴⁸ Had Congress more clearly enunciated the Act's policy, there might not exist as much tension between what is best for consumers and what is best for competitors.²⁴⁹ In any event, Congress should take notice of these problems before small-business owners find themselves winking in the dark, instead of advertising their products and services. But at the very least, courts should be wary when rendering decisions under the Lanham Act, a law that is closely tied to America's economic welfare.

248. *E.g. supra* nn. 114–120 and accompanying text (discussing Professor Burns's perspective on the lack of legislative policy and the resulting confusion).

249. *Supra* nn. 114–120 and accompanying text.