The DIGEST

National Italian American Bar Association Law Journal

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THE DIGEST

The Law Journal of the National Italian American Bar Association

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Two-Thousand and Four

ARTICLES

CASE COMMENT

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THE EDITOR'S NOTE

This volume of *The Digest* marks the 10th year of the partnership between the Syracuse University College of Law and NIABA. It is the tenth year, in which our student editors have worked with NIABA to produce a first-rate professional publication that is respected throughout the legal community. We are proud of our participation in this cooperative effort and we look forward to many more years of working together.

Ten years ago, when we first entered into this partnership, I worked with a hand full of students to help produce *The Digest*. We would meet at my home and have pages spread out all over the floor as we worked on the edit and production process. Now, of course, we have a journal office at the College of Law with multiple computer work stations and a typical student staff of around 20 students.

In all of these years, we have enjoyed the support of NIABA and of the Syracuse University College of Law. For this we are very grateful. There are many people, of course, who make the publication of *The Digest* possible and we could not possibly name all of them. I would like, however, to list below the names of the lead editors of the journal, as identified in each published volume, 1-12. I would also like to recognize the Honorable Anthony J. Cutrona who, as the NIABA Board member charged with directly overseeing *The Digest,* has worked closely with me for most of my years as Editor-in-Chief. Tony has helped me in many ways over these past years and has been instrumental in making this partnership a long-term success.

Below are the names of our distinguished lead editors for Volumes 1-12 of *The Digest.*

Vol. 1. Introduction to the first issue by Michael C. Rainone and Joseph N. Giamboi. Board of Editors: Dan R. Mastromarco, Giovanna M. Cinelli, Ronald A. Cimino, Francis M. Allegra.

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Vol. 12 Editor-in-Chief, Robin Paul Malloy; Managing Editor, Christopher J. Grace; Associate Managing Editor, Elisa Weselis.

With this issue of *The Digest* being the tenth year the journal has been edited by the students at the Syracuse University College of Law, we take honor in listing the lead editors of the journal since its founding. We thank all of them for their leadership and commitment in making *The Digest* possible.

Respectfully,

Robin Paul Malloy
Professor of Law, and Senior Associate Dean for Academic Affairs
Editor-in-Chief of *The Digest*
Member, Board of Directors of NIABA

One Nation under atheism, with liberty and justice for all

KYLE COHEN*

Every morning, before America's children begin a day of learning in public school, the voice of a state employee comes over the loud speaker leading impressionable students in a ritual of indoctrination, suggesting that they profess their belief in a deity. Michael Newdow believes that this type of state establishment of religion occurs every time children recite the words "under God" in the Pledge of Allegiance to the flag. In a stunning decision, the Ninth Circuit agreed with Newdow, holding that the pledge was a violation of the Establishment Clause of the Constitution.[1] The Ninth Circuit has since reaffirmed this conclusion, albeit in a more limited opinion,[2] and the Supreme Court has granted certiorari.[3] This case could force the Supreme Court to address how historical religious expressions fit within its Establishment Clause jurisprudence.

Part I of this paper will look at the history of the pledge and the 1954 addition of the words "under God" to its text. Part II provides analysis of both the majority and dissent in *Newdow v. U.S. Congress*, and compares and contrasts the analysis of the first decision to that of the amended decision. Judge Alfred T. Goodwin's opinion for the majority in *Newdow* will also be compared to that of Judge Frank Easterbrook of the Seventh Circuit, who held that the pledge did not raise any constitutional concerns in *Sherman v. Community Consolidated School District 21 of Wheeling Township*.[4] Part III predicts how the current Supreme Court will decide the case by examining each justice's Establishment Clause jurisprudence and concludes that the *Newdow* decision will likely be reversed. Part IV looks at some theories on how the courts should analyze

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* Kyle Cohen, J.D., 2004, Georgetown University Law Center; B.A., B.S., 2000, University of Florida. Mr. Cohen will be an Associate with the law firm of Howrey Simon Arnold & White, LLP in Washington, D.C. I would like to thank Professors J. Brent Walker and David N. Saperstein for their guidance in developing this article. I would also like to thank my family and my fiancée Rachel for their total support of anything I have accomplished throughout law school. A special thanks to my grandfather, Robert Flato, for his bravery in standing up for his religious freedom at a time when doing so was unpopular. It was his experience as a school board member, fighting to keep denominational prayer out of the school system, that sparked my interest in church/state law.

1. Newdow v. United States Cong., 292 F.3d 597, 612 (9th Cir. 2002) [hereinafter *Newdow I*], *en banc reh'g denied*, 321 F.3d 772 (9th Cir. 2003) (holding that the 1954 Act inserting the words "under God" was a violation of the establishment clause), *cert. granted*, 124 S.Ct. 384 (2003).

2. Newdow v. United States Cong., 328 F.3d 466 (9th Cir. 2003) [hereinafter *Newdow II*] (amending *Newdow I* to hold that the school policy of teacher led recitation of the pledge was unconstitutional).

3. Elk Grove Unified School Dist. v. Newdow, 124 S.Ct. 384 (U.S. Oct. 14, 2003) (No. 02-1624).

4. Sherman v. Cmty. Consol. Sch. Dist. 21 of Wheeling Township, 980 F.2d 437 (7th Cir. 1992) (holding that the school policy of reciting the pledge was constitutional).

symbolic and historical religious practices to determine if they violate the Establishment Clause. Analysis of these theories leads to the conclusion that the endorsement test provides the best way to address historical religious practices. Finally, Part V concludes that while the pledge may not be a violation of the Establishment Clause, it would be in the best interests of this country to remove the phrase from its patriotic affirmation.

I. HISTORY OF THE PLEDGE

The Pledge of Allegiance was written in 1892 by a Baptist Minister and Christian Socialist, Francis Bellamy.[5] This original version of the pledge did not contain any references to God whatsoever.[6] It was not until 1954 that Congress added the words "under God" into the pledge.[7] The stated reason for this addition was to ". . . further acknowledge the dependence of our people and our Government upon the moral directions of the creator."[8] In expressing this purpose Representative Louis Rabaut stated, "[u]nless we are willing to affirm our belief in the existence of God and His creator-creature relationship to man, we drop man himself to the significance of a grain of sand."[9]

The true purpose for the addition of the phrase was the desire of the government during the "red scare" to separate itself from Communism, which was viewed as atheistic. It was believed that a communist could recite the pledge without the reference to God, but once the words "under God" were added, it would be against his or her atheistic nature. Senator Homer Ferguson, who introduced the legislation in the Senate, stated, "[o]ur Nation was founded on a fundamental belief in God. . . communism, on the contrary, rejects the very existence of God."[10] A pledge historian has also cited the Catholic Church's desire for a version of the pledge appropriate for parochial schools as another reason for the addition.[11]

In the legislative history, Congress directly confronted any questions about the Act's constitutionality by pointing out that the new pledge was not an establishment of religion. Congress stated, "[a] distinction must be made between the existence of a religion as an institution and a belief in the sovereignty of God. The phrase 'under God' recognizes only the guidance of God in our national affairs."[12] In essence, Congress reasoned that the phrase was not an es-

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5. 4 U.S.C.A. § 4 (2003); *See* Carol McKay, *The Pledge of Allegiance's Long History of Controversy*, 49 FEDERAL LAWYER 9 (Aug. 2002).

6. *Id.*

7. H.R. REP. No. 83–1693 (1954), *reprinted in* 1954 U.S.C.C.A.N. 2339 (amendment to the pledge o add the words "under God").

8. *Id.* at 2340.

9. *Id.* at 2342.

10. H.R. REP. No. 83–1693, *supra* note 6, at 2342.

11. McKay, *supra* note 5.

12. H.R. REP. No. 83–1693, *supra* note 7, at 2341–42.

tablishment of religion because it simply recognized the historical fact that America was founded on a fundamental belief in God. To prove this point, the legislative history cited historical examples of government recognition of God.[13]

The other major development, in the history of the pledge, came from the Supreme Court. In the 1943 case *West Virginia State Board of Education v. Barnette*,[14] the Court was asked to decide on the constitutionality of a West Virginia statute that made the pledge compulsory and allowed for the state to discipline those students who failed to repeat the pledge.[15] A group of Jehovah's Witnesses brought suit claiming that the statute was a denial of their religious freedom.[16] In an 8–1 decision, the Court found that the statute was unconstitutional, holding that it was a denial of the students' freedoms of speech and worship.[17] *Barnette* did not find that the pledge itself was an unconstitutional establishment of religion. However, the words of the pledge could not have raised any Establishment Clause issue at the time, because the words "under God" had not yet been inserted into the text. *Barnette* is important because it stands for the principle that the government may not employ coercion to force its citizens to recite the pledge. This is a key consideration for some justices on the Supreme Court today, who will be reluctant to find an Establishment Clause violation in *Newdow*, since in *Barnette*, the Court held that the government does not have the power to force anyone to recite the pledge. Without the ability to coerce recitation of the pledge through the force of law, some justices would view that no establishment violation is possible.

II. NEWDOW V. U.S. CONGRESS

Michael Newdow is an atheist whose daughter attends public elementary school in California.[18] In accordance with the California Education Code, teachers must begin every school day with an appropriate patriotic exercise.[19] The school district that Newdow's daughter attends promulgated a policy that it would fulfill the statutory requirement by having the class recite the pledge of

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13. H.R. REP. No. 83-1693, *supra* note 7, at 2340–41. Some examples of the historical references to God cited by Congress include the Mayflower compact in 1620, the Declaration of Independence in 1776, Abraham Lincoln's Gettysburg Address in 1863, and most recently President Dwight Eisenhower's recognition in a commemoration speech for four military chaplains who gave their lives when the troopship Dorchester was sunk in 1943.

14. 319 U.S. 624 (1943).

15. *Id.* at 626 ("refusal to salute the Flag be regarded as an act of insubordination, and shall be dealt with accordingly").

16. *Id.* at 629–30.

17. *Id.* at 642.

18. Newdow I, 292 F.3d at 600.

19. CAL. EDUC. CODE § 52720 (West 1989); The relevant portion of the statute reads:In every public elementary school each day . . . there shall be conducted appropriate patriotic exercises. The giving of the Pledge . . . shall satisfy the requirements of this section.

allegiance once each day.[20] Newdow objected to this, but not because the school district's policy requires his daughter to participate. Rather, he alleges that his daughter is "injured when she is compelled to 'watch and listen as her state-employed teacher in her state-run school leads her classmates in a ritual proclaiming that there is a God.' "[21] The complaint made two basic challenges. First, Newdow argued that the 1954 Act codifying the addition of the words "under God" was an unconstitutional establishment of religion because it did not have a secular purpose.[22] Second, he contends that the school district's policy of requiring teachers to lead willing students in recitation of the pledge is an Establishment Clause violation because its primary effect is to advance religion.[23] District Court Judge Edward Schwartz agreed with the government that neither the 1954 Act nor the school policy were unconstitutional and dismissed the complaint.[24]

A. SHERMAN V. COMMUNITY CONSOLIDATED SCHOOL DISTRICT 21

While the *Newdow* case represents the first time the constitutionality of the 1954 Act was ever questioned, the issue of whether a state statute requiring recitation of the pledge in public schools was an establishment violation had previously been adjudicated by another circuit. In *Sherman*, the parent of a minor challenged an Illinois statute requiring teacher led recitation of the pledge.[25] The District Court ruled in favor of the state, holding that the statute satisfied all three elements of the *Lemon* test because it had a secular purpose, it did not have an effect of advancing religion, and it did not require government entanglement in religion.[26]

On appeal to the Seventh Circuit, Easterbrook stated the issue as whether "ceremonial references in civic life to a deity [are to] be understood as prayer, or support for all monotheistic religions, to the exclusion of atheists and those who worship multiple Gods?"[27] In answering this question, he looked to this country's history to determine whether the founders deemed ceremonial invocations of God as an establishment of religion. Easterbrook found that history shows the founders did not view these practices as violations because of the many occasions where they invoked a reference to God in important government proclamations and documents.[28]

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20. Newdow I, 292 F.3d at 600.
21. *Id.* at 601.
22. *Id.*
23. *Id.*
24. *Id.*
25. Sherman, 980 F.2d at 439.
26. *Id.* at 439–40.
27. *Id.* at 445.
28. Sherman, 980 F.2d at 445–46; The examples mentioned by Easterbrook as demonstrating an acceptance of ceremonial invocations of God by the founding fathers are James Madison's presidential

Easterbrook then cited specific examples of Supreme Court jurisprudence to support his conclusion that references to God in public occasions were not viewed by the Supreme Court "as conveying approval of particular religious beliefs."[29] The first of these examples came from the case *Engel v. Vitale*,[30] which dealt with the constitutionality of prayer in public schools. The Court held that public school prayer was an establishment violation, but was careful to distinguish ceremonial references to God in its reasoning by stating:

> There is of course nothing in the decision reached here that is inconsistent with the fact that school children and others are officially encouraged to express love for our country by reciting historical documents . . . which contain references to the deity OR BY SINGING OFFICIALLY ESPOUSED ANTHEMS WHICH INCLUDE THE COMPOSER'S PROFESSIONS OF FAITH IN A SUPREME BEING, or with the fact that there are many manifestations in our public life of belief in God. Such ***patriotic or ceremonial occasions bear no true resemblance to the unquestioned religious exercise*** that the State of New York has sponsored in this instance (Emphasis added).[31]

This statement is an example of how the Court has distinguished ceremonial references to God from other types of religious activity. Justice William Brennan in *Abington Township School District v. Schempp*,[32] supported this distinction stating,

> [t]he reference to divinity in the revised pledge of allegiance. . .may merely recognize the historical fact that our Nation was believed to have been founded 'under God.' Thus reciting the pledge may be no more of a religious exercise then the reading aloud of Lincoln's Gettysburg Address, which contains an allusion to the same historical fact.[33]

In a later case, Brennan expressed his belief that such practices were consistent with the Establishment Clause because they had lost any true religious significance.[34] Relying on this Supreme Court precedent, Easterbrook found that the pledge was a ceremonial invocation and, therefore, not a violation of the Establishment Clause because it was not a religious activity.[35] In anticipation of the argument that the Supreme Court statements he cited were mere dicta,

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proclamations; Thomas Jefferson's treaties that sent religious ministers to the Indians; George Washington's Thanksgiving day proclamations; and the Declaration of Independence's provision that states, "[A]ll men are created equal, that they are endowed by their Creator with certain unalienable rights."

29. Sherman, 980 F.2d at 447.

30. 370 U.S. 421 (1962).

31. *Id.* at 435.

32. 374 U.S. 203 (1963).

33. *Id.* at 304.

34. Marsh v. Chambers, 463 U.S. 783, 818 (1983) (Brennan, J., dissenting) (holding that Nebraska's practice of opening each legislative session with a prayer by a chaplain was not a violation of the establishment clause).

35. Sherman, 908 F.2d at 447.

Easterbrook said, "[i]f the Court proclaims that a practice is consistent with the establishment clause, we take its assurances seriously. If the Justices are just pulling our leg, let them say so directly."[36]

In concurrence, Justice Daniel Manion agreed that the pledge should not be considered an establishment of religion. However, he disagreed with Easterbrook's analysis of ceremonial deism. Manion argued that the approach taken by Easterbrook implied that the phrase "under God" initially violated the Establishment Clause, but then became constitutional through repetitive use.[37] Manion believed this to be in error because "[a] civic reference to God does not become permissible under the First Amendment only when it has been repeated so often that it is sapped of religious significance."[38] Manion concurred with the result because he believed that the First Amendment was not intended by the Framers to prohibit ceremonial invocations of God. Therefore, Manion argued that the words of the pledge did not have to be described as "meaningless" in order for them to pass constitutional muster.[39]

B. NEWDOW I

In a 2–1 decision the Ninth Circuit held that both the 1954 Act adding the words "under God" in the pledge and the school policy of requiring teacher–led, voluntary recitation of the pledge were impermissible government establishments of religion. In reaching this conclusion, Judge Goodwin analyzed the case using the three different tests enunciated by the Supreme Court: the *Lemon* test, the endorsement test, and the coercion test. Goodwin could have found either the 1954 Act or the school policy unconstitutional if they failed any one of these tests. However, Goodwin attempted to strengthen his opinion by finding that the pledge was unconstitutional under all of these tests.

Goodwin first performed his analysis under the endorsement test, which was first contrived by Justice Sandra Day O'Connor in *Lynch v. Donnelly*.[40] According to the endorsement test, the Establishment Clause is violated whenever the government makes an adherence to religion relevant in any way to a person's standing in the political community.[41] O'Connor stated, "[e]ndorsement sends a message to nonadherents that they are outsiders. . . ."[42] Goodwin found that the pledge runs afoul of the endorsement test because words "under God" infer a government endorsement of monotheism as a favored practice. Goodwin stated:

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36. Sherman, 908 F.2d at 448.
37. *Id.*
38. *Id.*
39. *Id.*
40. Lynch v. Donnelly, 465 U.S. 668, 688 (1984) (O'Connor, J., concurring) (holding that is was not unconstitutional for the city to display a crèche as part of a holiday display).
41. *Id.*
42. *Id.*

> The text of the official Pledge, codified in federal law, impermissibly takes a position with respect to the purely religious question of the existence and identity of God. A profession that we are a nation "under God" is identical, for Establishment Clause purposes, to a profession that we are a nation "under Jesus," a nation "under Vishnu," a nation "under Zeus," or a nation "under no god," because none of these professions can be neutral with respect to religion.[43]

In sum, Goodwin concluded that the pledge is an impermissible endorsement of religion because it sends a message to those who do not believe in a monotheistic religion that they are outsiders.

Next, the Ninth Circuit looked at the practice according to the principles of the coercion test. As the Supreme Court has demonstrated, coercion analysis is relevant even if there is no direct punishment for non-adherence.[44] Coercion can occur when someone is put in the position where they must choose between participating in a religious exercise or protesting. In *Lee v. Weisman*, the Court found the practice of reciting nonsectarian prayers at public graduation ceremonies coercive, because it could be viewed by the minority as "an attempt to employ the machinery of the State to enforce a religious orthodoxy."[45] Goodwin believes that the school policy was coercive because to an atheist, using the words "under God" may reasonably appear to be the State's attempt to enforce the "religious orthodoxy" of monotheism.[46]

In *Weisman*, the Court recognized that, despite the fact, attendance at the graduation ceremony was voluntary, coercion did exist, because in reality the students will participate in this important life event.[47] The Court extended this coercion analysis in *Santa Fe Independent School District v. Doe*,[48] to invalidate a practice of student led prayer before football games. The facts in *Newdow* present an even stronger argument for coercion because in both *Weisman* and *Santa Fe*, the students had a right to choose not to attend the event; a teacher did not lead the recitation; and the practice occurred during special occasions. By contrast, in *Newdow* attendance for the recitation of the pledge is mandatory because it occurs during school hours; the same teachers who indoctrinate the students on different subjects lead in its recitation; and the practice takes place each and every school day. Another key difference is the age of the children. In both *Santa Fe* and *Weisman*,[49] the conduct occurred while the students were in high school or on the verge of entering high school. The audi-

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43. Newdow I, 292 F.3d at 607–08.
44. Lee v. Weisman, 505 U.S. 577, 593 (1992).
45. Weisman, 505 U.S. at 592.
46. Newdow I, 292 F.3d at 609.
47. Weisman, 505 U.S. at 583.
48. 530 U.S. 290 (2000) (holding that the school's policy of student-initiated prayer before football games violated the Establishment Clause).
49. Weisman, 505 U.S. at 581; *Id.* at 294.

ence, in *Newdow,* is not as mature, as plaintiff challenged the school policy on behalf of his elementary school daughter. In an allusion to the particularly vulnerable nature of elementary school children, Goodwin stated, "[t]he coercive effect of this policy is particularly pronounced in the school setting given the age and impressionability of schoolchildren, and their understanding that they are required to adhere to the norms set by their school, their teacher and their fellow students."[50]

Lastly, the majority analyzed the case under the *Lemon* test. According to *Lemon*, in order to survive an Establishment Clause challenge, the government conduct in question, (1) must have a secular purpose, (2) must have a principle or primary effect that neither advances nor inhibits religion, and (3) must not foster "an excessive government entanglement with religion."[51] Goodwin found that both the Act and the school policy violated the *Lemon* test. First, he held that the 1954 Act adding the words "under God" violated the first prong of the *Lemon* test because it had the primary purpose of advancing religion. Second, Goodwin concluded that the school district's policy violated the effects prong of the *Lemon* test.[52]

The government contended that the pledge's acknowledgement of religion did have a secular purpose, which was recognized by the Supreme Court. The government cited Justice O'Connor's reasoning in *Lynch,* that "In God we Trust" and other similar government acknowledgements of religion served the legitimate "purposes of solemnizing public occasions, expressing confidence in the future, and encouraging the recognition of what is worthy of appreciation in society."[53] Goodwin finds this argument unconvincing because even though the pledge as a whole may serve these arguably legitimate secular purposes, the 1954 Act's adding of the words "under God" did not further these functions, and it is the purpose of the 1954 Act that is the issue.[54] In examining the legislative history of the 1954 Act, the majority states, "the Act's sole purpose was to advance religion, in order to differentiate the United States from nations under communist rule."[55] Because the 1954 Act was designed to advance religion by taking a position on the question of theism at the expense of atheism or monotheism, the majority finds that the 1954 Act had a religious purpose and was a violation of *Lemon.* The court was unimpressed by the fact that the 1954 Act expressly disclaimed a religious purpose stating, "[t]he Act's affirmation of 'a belief in the sovereignty of God' and its recognition of 'the guidance of God'

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50. Newdow I, 292 F.3d at 609.

51. Lemon v. Kurtzman, 403 U.S. 602, 612-13 (1971) (holding that two state statutes which authorized state aid to church-related educational institutions were unconstitutional because they involve excessive entanglement between government and religion).

52. Newdow I, 292 F.3d at 609.

53. Lynch, 465 U.S. at 693.

54. Newdow I, 292 F.3d at 610.

55. *Id.*

are endorsements by the government of religious beliefs."[56] Since the majority found that the 1954 Act violated the purpose prong, it did not examine the Act under the other two prongs of *Lemon*.

The plaintiff conceded that the school district policy did not violate the *Lemon* test's purpose prong because fostering patriotism is a legitimate secular purpose.[57] However, the plaintiff argued, and the majority agreed, that the policy violated the effects prong of *Lemon*. The majority restated its endorsement test reasoning that the school policy had an impermissible primary effect of advancing religion. Goodwin concluded that due to the impressionability of elementary school children, the policy was "highly likely to convey an impermissible message of endorsement to some and disapproval to others of their beliefs regarding the existence of a monotheistic God," therefore, it was a violation of the effects prong.[58]

In a footnote at the end of the opinion, the majority addressed the findings of the Seventh Circuit in *Sherman*. Goodwin dismissed the impact of the statements from the Supreme Court cited to by Easterbrook because the Court was not presented with the question of the constitutionality of the pledge directly and did not apply any of its three Establishment Clause tests to the issue.[59] For the same reason, Goodwin attacks the holding of *Sherman* because Easterbrook did not apply the *Lemon*, endorsement, or coercion tests in reaching his result.[60] Goodwin believed that Easterbrook was ignoring Supreme Court precedent by refusing to apply any of these tests, despite the fact that *Sherman's* result rested on statements by the Supreme Court in cases where they did apply the tests. Nevertheless, because Easterbrook did not specifically go through any of the tests in his analysis, Goodwin has little problem in reaching the opposite conclusion.

In dissent, Judge Ferdinand Fernandez argues that the pledge has no tendency to establish religion because "when all is said and done, the danger that 'under God' in our Pledge of Allegiance will tend to bring about a theocracy or suppress somebody's beliefs is so minuscule as to be de minimis."[61] Fernandez is careful not to say that the pledge is a de minimis constitutional violation, rather it is his view that "the de minimis tendency of the Pledge to establish a religion. . .[makes it] no constitutional violation at all."[62] The dissent cites a long list of Supreme Court cases that stand for the proposition that the Pledge of

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56. Newdow I, 292 F.3d at 611.

57. *Id.* at 611.

58. *Id.*

59. *Id.* Goodwin dismisses the Supreme Court's decision in Marsh, upholding legislative prayer because in that case the Court did not apply the Lemon test.

60. *Id.*

61. Newdow I, 292 F.3d at 613.

62. *Id.* at 615.

Allegiance does not constitute an establishment danger.[63] Fernandez does not perform his own analysis of the pledge under any of the tests. Instead he attacks the reasoning of the majority for limiting themselves to the elements of these tests, "while failing to look at the good sense and principles that animated those tests in the first place."[64]

The effect of this opinion was far reaching. Not only did Goodwin's holding force the public schools to cease their policy of reciting the pledge, but because Goodwin found the 1954 Act unconstitutional, anytime any state run institution led a recitation of the pledge it could be an establishment violation. Under *Newdow I*, it may be a violation to recite the current pledge in the schools; in a military ceremony; during oaths of citizenship; or before a legislative session. In short, the majority's reasoning would expel the Pledge of Allegiance from American society as long as it contained the words "under God" because the congressional addition of those words was unconstitutional.

C. NEWDOW II

It did not take long for the decision in *Newdow* to spark both public and legislative reaction.[65] The morning after the decision was announced, members of the House of Representatives, Democrat and Republican, gathered on the steps of the Capital to recite the Pledge of Allegiance. Public sentiment was so outspoken against the opinion that the House voted to deny all federal courts jurisdiction to hear First Amendment challenges to the pledge.[66] In another show of opposition to *Newdow*, Congress passed a law with the purpose of "reaffirm[ing] the reference to one Nation under God in the Pledge of Allegiance" and reaffirming the national motto "In God we trust."[67] Congress cited to many of the same historical references mentioned by Easterbrook in *Sherman*, to show that it was not the intent of the founders, in drafting the Establishment Clause, to have all references to God removed from public life.[68] The legislation also listed Supreme Court jurisprudence that Congress believed was contradictory to the analysis in *Newdow*.[69]

Perhaps in response to this public outcry, or in an effort to narrow the opinion to survive the petition for rehearing en banc, Goodwin wrote an amended opin-

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63. Newdow I, 292 F.3d at 613.

64. *Id.*

65. McKay, *supra* note 5.

66. *See* H.R. 5064, 107th Cong. (2002) (setting forth "[n]o court established by Act of Congress shall have jurisdiction to hear or determine any claim that the recitation of the Pledge of Allegiance . . . violates the first article of amendment to the Constitution of the United States").

67. H.R. REP. NO. 659 (2002), *reprinted in* 2003 U.S.C.C.A.N. 1304.

68. 2003 U.S.C.C.A.N. 1304 *1–2.

69. *Id.* at *2–3.

ion, which was submitted on February 28, 2003.[70] *Newdow II* represents a classic case of addition by subtraction, as Goodwin decided the best way to strengthen the opinion was to narrow its focus. While *Newdow I* made the Pledge of Allegiance unconstitutional in many circumstances, *Newdow II*'s reasoning will only make the pledge unconstitutional when recited in the public schools. Goodwin stated:

> We may assume arguendo that public officials do not unconstitutionally endorse religion when they recite the Pledge, yet it does not follow that schools may coerce impressionable young schoolchildren to recite it, or even to stand mute while it is being recited by their classmates.[71]

Goodwin restricted the effect of the opinion by narrowing the analysis to only the coercion test. Gone was the entire *Lemon* analysis, as the purpose behind the 1954 Act was never made an issue. Also notably absent was the previous critique of the pledge as a violation of the endorsement test. Based solely on its failure of the coercion test, the majority held that the school policy requiring the recitation of the pledge was an unconstitutional establishment of religion. The court stated, "[b]ecause we conclude that the school district policy impermissibly coerces a religious act and accordingly hold the policy unconstitutional, we need not consider whether the policy fails the endorsement test or the *Lemon* test as well." (Emphasis added).[72] In his coercion analysis, Goodwin paralleled this case with *Weisman*, because the Supreme Court made its finding of coercion in that case by relying heavily on the fact that the conduct occurred in a public school.[73] The Ninth Circuit argued that similar to *Weisman*, the school's action forced the student to decide between participating in the religious exercise or protesting.[74]

Goodwin distinguishes the pledge from the historical examples used by the dissent. Goodwin views the references to God in such writings as the Declaration of Independence and the National Anthem as fundamentally different from the pledge, because in those documents the references to God are "merely a reflection of the author's profession of faith."[75] By contrast, the Pledge of Allegiance is an affirmation by the person reciting it. The court states, "[t]o pledge allegiance to something is to alter one's moral relationship to it, and not merely to repeat the words of an historical document or anthem."[76] In sum, the majority believes that because the pledge has a personal component to it, as it is an

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70. It is not unusual for a panel to amend one of its opinions. *See* David L. Hudson Jr., *Pledge Plaintiff Hopes for High Court Review: New Narrow Ruling May Stand Better Chance of Winning Affirmance*, 2 No. 9 A.B.A. J. E-REPORT 6 (March 7, 2003).

71. Newdow II, 328 F.3d 466, 489 (9th Cir. 2003).

72. *Id.* at 487.

73. Weisman, 505 U.S. at 593.

74. Newdow II, 328 F.3d at 488.

75. *Id.*

76. Newdow II, 328 F.3d at 489.

affirmation by the speaker of his beliefs, it is fundamentally different from the references to God found in many of America's historical documents. This argument represents a frontal assault on the reasoning of Easterbrook, whose analysis in *Sherman* centered on how the words of the pledge were no different than other historical references to God by America's founders.

Judge Diarmuid O'Scannlain wrote a long dissent from the Circuit's decision to deny rehearing the case en banc, which was joined by five other judges.[77] It argues that the pledge is not an Establishment Clause violation because it is not a religious act; rather it is a patriotic act. The dissent from the denial of rehearing states, "[w]e should have reheard *Newdow I* en banc . . . because it was wrong, very wrong—wrong because reciting the Pledge of Allegiance is simply not 'a religious act.'"[78] O'Scannlain supports this view by pointing to Supreme Court statements that make this distinction. *Engel*,[79] *Schempp*,[80] *Wallace v. Jaffree*,[81] and *Weisman*[82] stand for two fundamental principles according to O'Scannlain. First, formal religious observances are prohibited in public schools because of the possibility that they may be viewed as an establishment of religion.[83] Second, not every reference to God in the public schools was prohibited, because, in each case, the Court confined its holding to instances of explicit religious exercise rather than making a blanket prohibition of all things religious.[84] The mistake made by the majority, according to the en banc dissent, is that the coercion analysis should not apply, in this case, because no formal religious exercise takes place.

The dissent from the denial of rehearing also believes that the majority's reasoning is flawed because it demonstrates hostility toward religion. O'Scannlain worries that as a result of *Newdow*, atheism has been given a favored status.[85] The en banc dissent states, "[t]he absolute prohibition on any mention of God in our schools creates a bias *against* religion." (Emphasis supplied).[86] In sum, O'Scannlian charges that the majority's reasoning affirmatively favors non-belief over belief. Therefore, he argues that the majority's

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77. The Ninth Circuit voted 15–9 against en banc review; *See* Newdow v. United States Cong., 321 F.3d 772, 776 (9th Cir. 2003) (denied rehearing en banc) (Scannlain J., dissenting).

78. *Id.*

79. Engel v. Vitale, 370 U.S. 421, 435 (1962) (holding that it was an Establishment Clause violation for the school to begin each day with a formal prayer acknowledging and giving thanks to God).

80. Abington Sch. Dist., 374 U.S. at 203 (holding that beginning each day in the public schools with Bible reading is unconstitutional under the Establishment Clause).

81. 472 U.S. 38 (1985) (holding that an Alabama statute authorizing a one-minute period of silence was an impermissible government endorsement of religion because the law was passed with the purpose of endorsing prayer activities).

82. Weisman, 505 U.S. at 577 (holding that it was an unconstitutional endorsement of religion to have nonsectarian prayer at official school graduation ceremonies).

83. Newdow, 321 F.3d at 781 (denied rehearing en banc) (O'Scannlain J., dissenting).

84. *Id.*

85. *Id.* at 786.

86. *Id.*

interpretation of the Establishment Clause is not consistent with the purposes and evils the clause was designed to guard against.

III. PREDICTING THE SUPREME COURT'S RULING

The Supreme Court has granted certiorari on the question of "Whether a public school district policy that requires teachers to lead willing students in reciting the Pledge of Allegiance, which includes the words 'under God,' violates the Establishment Clause of the First Amendment, as applicable through the Fourteenth Amendment."[87] Under the Court's current composition, there are two distinct groups who are likely to be on opposite sides of the issue. Justices John Stevens, Ruth Bader Ginsburg, and David Souter form the separationalist block, and would likely vote to affirm the *Newdow* decision because they view that the Establishment Clause creates a wall between church and state. On the opposite extreme, the accommodationalist group consisting of Chief Justice William Rehnquist, along with Justices Antonin Scalia and Clarence Thomas, favor a narrow view of the scope of the Establishment Clause and would likely vote to reverse. Therefore, the case will likely be decided by the three swing voters, Justices Stephen Breyer, Anthony Kennedy, and O'Connor.

A. THE SEPARATIONALIST BLOCK

Justices Stevens, Ginsburg, and Souter are the Supreme Court members who are most likely to agree that the recitation of the pledge in public schools is an impermissible establishment of religion. They believe the Establishment Clause was designed to protect against government establishment of religion in general, rather than only protecting from establishment of one particular religious sect.[88] The separationalists have found support in the history of the clause itself for their theory that it was designed to forbid the government from favoring religion over non-religion. In *Allegheny v. ACLU*,[89] Stevens noted that because subsequent drafts of the Establishment Clause broadened the scope of the clause from "any national religion" to simply "religion . . . the clause as ratified proscribes federal legislation establishing a number of religions as well as a single national church."[90] In *Weisman*, Souter concurred in this belief stating that the Establishment Clause was no less applicable to "government acts favoring religion generally than to acts favoring one religion over others."[91] Souter goes on

87. Elk Grove Unified School Dist. v. Newdow, 124 S.Ct. 384 (2003).

88. Wallace, 472 U.S. at 54 (stating that "the political interest in forestalling intolerance extends beyond intolerance among Christian sects–or even intolerance among 'religions'—to encompass intolerance of the disbeliever and the uncertain").

89. Allegheny v. ACLU, 492 U.S. 573 (1989) (holding that the crèche placed on the grand staircase of the courthouse was an impermissible government establishment of religion).

90. *Id.* at 648.

91. Weisman, 505 U.S. at 610.

to explain that since the government cannot favor religion over non-religion, it similarly cannot favor theism over non-theism.[92] This argument is exactly the point made by the majority in *Newdow* in stating that the phrase "under God" is the same for establishment purposes as saying we are a nation under Jesus, Vishnu, or Zeus.[93]

Unlike Goodwin in *Newdow II*, the separationalists would not have analyzed the case solely under the coercion test. This group believes that coercion is not a necessary element in finding an establishment violation because reading the clause as requiring coercion would make it redundant with the Free Exercise Clause, therefore, rendering the Establishment Clause meaningless.[94] Rather then being a necessary factor, the separationalists have looked to coercion as one factor to take into account when determining whether a practice has a primary effect of advancing religion.[95] In fact, the separationalists have utilized both coercion and endorsement as factors in determining violations of *Lemon's* effects prong. For example, in *Santa Fe*, Stevens, writing for the majority, used both coercion and endorsement analysis in holding that student led prayer at high school football games violated the Establishment Clause.[96] He stated that in cases involving state participation in a religious activity, one of the relevant questions is "whether an objective observer. . .would perceive it as a state endorsement of prayer in the public schools."[97] The opinion also relies on the coercive nature of the public school context.[98] Therefore, it is likely that the separationalists would find the school policy in *Newdow* violates the effects prong of *Lemon* because of the coercive public school environment along with the endorsement of monotheism over atheism as a favored practice.

The separationalists would refuse to dismiss the pledge as mere ceremonial deism. In *Allegheny*, Stevens noted that symbolic government speech respecting religion might violate the constitution.[99] Stevens also attacked the notion of ceremonial deism because he believes that it does a disservice to religion by stripping such practices of meaning.[100] The separationalists have also con-

92. Weisman, 505 U.S. at 617.

93. Newdow II, 328 F.3d 466, 487 (9th Cir. 2003).

94. Weisman, 505 U.S. at 621; "a violation of the Free Exercise Clause is predicated on coercion while the Establishment Clause violation need not be so attended.. . . If coercion is an element of the establishment clause, establishment adds nothing to free exercise."

95. The second and third prong of Lemon have been combined by the Supreme Court, as entanglement has become a factor in determining whether there was a violation of the effects prong. *See Agostini v. Felton*, 521 U.S. 203, 205 (1997) (holding that a federally funded program providing supplemental education to disadvantaged children on a neutral basis was not invalid where the instruction was given on the grounds of sectarian schools).

96. Santa Fe, 530 U.S. at 312.

97. *Id.* at 308.

98. *Id.* at 312.

99. Allegheny, 492 U.S. at 650.

100. Lynch, 465 U.S. at 726-27.

fronted the analysis in *Marsh v. Chambers*, which held that prayer before a legislative session offered by chaplains was not unconstitutional, because the practice is rooted in history and shows that the framers could not have possibly understood it to be an establishment violation.[101] In *Weisman*, Souter stated, "those [historical] practices prove, at best, that the Framers simply did not share a common understanding of the Establishment Clause, and, at worst, that they, like other politicians, could raise constitutional ideals one day and turn their backs on them the next."[102] This demonstrates that the separationalists will not put too much emphasis in the ceremonial history of the activity in determining whether it is an establishment of religion.

Though she has not yet written much on the topic, Justice Ginsburg should be included among the separationalists because she has agreed with Stevens on every major Establishment Clause case coming to the Court during her tenure. She only disagreed with Souter on Establishment issues twice, but in both of those disagreements the issue was unique. In *City of Boerne v. Flores*,[103] she agreed with the majority and not Souter that the Religious Freedom Restoration Act exceeded Congress' § 5 enforcement powers. She also dissented along with Stevens in *Capitol Square Review and Advisory Board v. Pinette*,[104] where the Court majority, including Souter, held that the display of a Latin cross on public property by the Ku Klux Klan did not violate the Establishment Clause. Ginsburg departed from the majority's reasoning because she believed that a reasonable observer would view this as a government endorsement of religion because the observer would not be able to tell that it was an endorsement by a private party rather than the government.[105] In her dissent, she stated that the Establishment Clause required an uncoupling of the government from the church, and that requirement was not met in this case because:

> [n]ear the stationary cross were the government's flags and the government's statues. No human speaker was present to disassociate the religious symbol from the State.
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> No other private display was in sight. No plainly visible sign informed the public that the cross belonged to the Klan and that Ohio's government did not endorse the display's message.[106]

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101. Marsh, 463 U.S. at 792; "In light of the unambiguous and unbroken history of more than 200 years, there can be no doubt that the practice of opening legislative sessions with prayer has become a part of the fabric of our society." In *Newdow I*, Goodwin did not directly address Marsh in his analysis. Goodwin dismisses the case as an aberration in his background discussion of the Establishment Clause because it did not apply the *Lemon* test; *See* Newdow I, 292 F.3d at 607. "The Supreme Court applied the *Lemon* test to every Establishment case it decided between 1971 and 1984, with the exception of *Marsh v. Chambers*."

102. Weisman, 505 U.S. at 626.

103. 521 U.S. 507 (1997).

104. 515 U.S. 753 (1995).

105. *Id.* at 2474–75.

106. Pinette, 515 U.S. at 2474.

If anything, parting ways with Souter in this case could show that Ginsburg has an even stronger commitment to the wall of separation then does Souter. Therefore, she is solidly within this separationalist block.

In sum, because the separationalists believe the Establishment Clause is violated anytime the government favors religion in general over non-religion, they will most likely agree that the school policy failed the effects prong of the *Lemon* test as it established theism as a favored practice and the school context made the practice extremely coercive.

B. THE ACCOMMODATIONALIST BLOCK

Chief Justice Rehnquist, and Justices Scalia, and Thomas all take a narrow view of the Establishment Clause's protections. That view was expressed by Rehnquist in *Wallace*, when he stated that the Establishment Clause was only meant to prohibit the designation of a national church and to prevent the government from asserting preference for one religious sect over another.[107] Because neither one of these protections are threatened by the Pledge of Allegiance, it is virtually guaranteed that this group will vote to reverse the decision in *Newdow*. In dicta, they have already expressed a belief that not only is the pledge constitutional, a decision to the contrary is ridiculous. In *Weisman*, Scalia, speaking for all three members of this group, stated sarcastically, "[I]n *Barnette* we held that a public-school student could not be compelled to *recite* the Pledge; we did not even hint that she could not be compelled to observe respectful silence. . .. Logically, that ought to be the next project for the Court's bulldozer."[108] Even if we were to disregard this dicta, the accommodationalist segment of the Court would almost assuredly vote in favor of reversal because the pledge is nonsectarian, the statute was not coercive on its face, and removal of the words "under God" would show a hostility toward religion.

The first reason why the accommodationalists would reverse the decision of the Ninth Circuit is because they believe that the clause only requires government neutrality between religious sects. For example, the government cannot favor Catholicism over Protestantism. However, they view nothing in the clause requiring neutrality on the part of the government between religion and non-religion. In *Newdow II*, Goodwin expressed his view that by including the words "under God" the pledge made monotheism a preferred practice over atheism.[109] In *Weisman*, the trio argued that the nonsectarian nature of the prayer should save it from Establishment Clause scrutiny.[110] As a result, Scalia, listed historical documents and speeches, in which public officials offered thanks to

107. Wallace, 472 U.S. at 99 (holding that an Alabama statute authorizing a daily period of silence in public schools for mediation and voluntary prayer was an endorsement of religion).

108. Weisman, 505 U.S. at 639.

109. Newdow II, 328 F.3d 466, 487 (9th Cir. 2003).

110. Weisman, 505 U.S. at 631.

God, to support his proposition that a nondenominational prayer was never understood to be an Establishment Clause violation.[111] At the end of this opinion, Scalia stated, "nothing, absolutely nothing, is so inclined to foster among religious believers of various faiths, a toleration—no, an affection—for one another than voluntarily joining in prayer together, to the God whom they all worship and seek."[112] This statement reveals that Scalia's jurisprudence favors monotheism, as he does not take into account that the students may not worship "the God." While Rehnquist and Thomas do not speak in such bold terms as Scalia, it is clear that they too believe that the government can prefer religion over nonreligion.[113] Since the pledge does not favor a specific religious sect, the accommodationalists would find it is beyond the scope of the Establishment Clause. Another key difference between the accommodationalists and the majority in *Newdow II,* is very different requirements for coercion. Unlike Justice Kennedy, who has a broader concept of coercion, the accommodationalists would require direct coercion in order to find a violation. In *Weisman*, Scalia made clear in his dissent that the coercion had to be by "force of law and threat of penalty," which would require the students to attend a graduation ceremony where the nonsectarian prayer was offered[114] The coercion required by the accommodationalists is akin to the coercion that occurred in *Barnette*, where the students were threatened with discipline if they did not recite the pledge.[115] Because the majority's analysis in *Newdow* relies on psychological coercion, the accommodationalists would likely vote for reversal as the policy was not implemented under the threat of discipline.

However, there are signs that the coercion in *Newdow II* may be unacceptable even to the accommodationalist block. In distinguishing *Weisman* from the previous Supreme Court cases, which found school prayer unconstitutional, this group stated that in those cases "school prayer occurs within a framework in which legal coercion to attend school (i.e., coercion under threat of penalty) provides the ultimate backdrop."[116] Like the school prayer cases, the statute in *Newdow II* calls for the pledge to be read every morning, during time when the students are required by law to attend school. Because of this backdrop of legal coercion, the pledge may involve coercive pressure that meets the accommodationalists' requirement of force of law and threat of penalty. Another key difference that may change the accommodationalists' coercion analysis is the fact that unlike *Weisman*, the pledge was offered and repeated every day, without

111. Weisman, 505 U.S. at 633–36.

112. *Id.* at 646.

113. *See* Wallace, 472 U.S. at 99 (Rehinquist, J., dissenting); "The Establishment Clause did not require government neutrality between religion and irreligion."

114. Weisman, 505 U.S. at 640.

115. West Virginia State Bd. of Educ. v. Barnette, 319 U.S. 624 (1943).

116. Weisman, 505 U.S. at 643.

the presence of the students' parents.[117] Scalia noted in *Weisman*, "[v]oluntary prayer at graduation—a one-time ceremony at which parents, friends and relatives are present" would not raise concerns that the classrooms were being used to advance religious views that conflict with the beliefs of the student and his family.[118] The accommodationalist block may have to admit that coercive pressure is present because the statute requires the recitation of the pledge during school time; when there is legal duty of the students to attend; as well as it takes place every day without the presence of the parents.

Finally, this group is likely to vote for reversal because they will view the *Newdow II* decision as hostile to all things religious in public life. As Rehnquist stated, "[t]he Establishment clause does not require that the public sector be insulated from all things which may have a religious significance or origin."[119] The accommodationalists will view the *Newdow II* opinion as an attempt to further push religion to the outskirts of public life. This group would agree with the Sixth Circuit's statement that stripping "from public ceremonies all vestiges of the religious acknowledgements that have been customary at civic affairs in this country since well before the founding of the Republic" amounts to an unconstitutional hostility toward religion.[120] This is especially evident because the effect of the *Newdow II* decision will be much more noticeable to the children than what occurred after the *Stone v. Graham* decision, where the school simply had to remove the postings of the Ten Commandments.[121] Although removal of the Ten Commandments would occur with little fanfare, as the students probably would have never noticed them in the first place, since the students have repeated the words "under God" in the Pledge of Allegiance from their first day of school, removal of the phrase could serve as a daily reminder that religion is incompatible with the public sphere. Because the decision would force removal of a phrase that students have already become accustomed to, the accommodationalists would view this decision as especially hostile toward religion.[122]

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117. Weisman, 505 U.S. at 644.

118. *Id.*

119. Stone v. Graham, 449 U.S. 39, 45-6 (1980) (Rehnquist, J., dissenting) (holding that a Kentucky statute requiring the posting of the Ten Commandments in public schoolrooms had no secular purpose, and was therefore unconstitutional).

120. Chaudhuri v. Tennessee, 130 F.3d 232, 236 (6th Cir. 1997) (affirming the constitutionality of a nonsectarian prayer or moment of silence at a public university function); *See* Andrew Cogar, *Government Hostility to Religion: How Misconstruction of the Establishment Clause Stifles Religious Freedom*, 105 W. VA. L. REV. 279, 293 (2002) (arguing that the *Lemon* test is an inappropriate Establishment Clause test because it validates government hostility toward religion).

121. Stone, 449 U.S. at 41.

122. In *Engel*, the Court struck down the school prayer despite the fact that its absence would be noticeable to the students. Engel, 370 U.S. at 436. However, in *Engel*, the school policy was challenged immediately upon the practice's adoption. *Id.* at 423. The removal of a prayer that was employed for a few years in U.S. schools would not have the same affect on students, as the removal of the pledge that has been applied in the schools with the phrase "under God" for the past 50 years. Unlike

The accommodationalist block will almost assuredly vote for a reversal of the Ninth Circuit, as they would view Goodwin's analysis as hostile toward religion. This conclusion is buttressed, by the fact, that the group has manifested its belief that nonsectarian prayer is not a violation and there must be legal coercion, like the coercion that was present in *Barnette*, in order to find a violation.[123]

The impact that accomodationalist block will have on the outcome of the case was lessened by the announcement that Justice Scalia that he will not take part in the decision.[124] Scalia had reportedly stated at a Religious Freedom Day rally in January 2003 that removing references to God from public forums would be "contrary to our whole tradition."[125] Scalia's recusal means that the accommodationalists will only have two votes. This makes the swing voters even more critical for the accommodationalists because a 4-4 split would have the affect of upholding the pledge ban in the schools of the Ninth Circuit.

C. THE SWING VOTES

With the accommodationalist and the separationalist blocks' stances reasonably clear, Justices O'Connor, Kennedy, and Breyer will likely be the deciding votes on the fate of the pledge. O'Connor and Kennedy have often been the swing votes on Establishment Clause issues, but it is not because they have similar philosophies. O'Connor will analyze the case according to the endorsement test she laid down in *Lynch*.[126] Kennedy, on the other hand, will perform coercion analysis. The *Newdow II* decision was based entirely on coercion and could have been a direct attempt by Goodwin to use Kennedy's own analysis in order to win his vote. Breyer's position is a little harder to track, as he has sided with the separationalists on some issues and with the accommodationalists on others. However, his past voting record and use of the endorsement test make it likely that he will side with O'Connor.

1. *Justice O'Connor*

As the founder and chief supporter of the endorsement test, Justice O'Connor is likely to ask one essential question: What is the message conveyed to a reasonable observer by the recitation of the pledge containing the reference to God? In the past, O'Connor has written dicta expressing a position that the pledge is not a government endorsement of religion. In *Lynch*, she stated that

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the prayer in *Engel*, the pledge has become part of the students' daily routine and its absence would represent a noticeable break from that routine.

123. Barnette, 319 U.S. at 626.

124. Bill Mears, Supreme Court Accepts Pledge of Allegiance Case, CNN, *available at* http://www.cnn.com/2003/LAW/10/14/scotus.pledge.of.allegiance/ (last visited March 29, 2004).

125. *Id.*

126. Lynch, 465 U.S. at 688.

"In God we Trust" and other government acknowledgements of religion serve "the legitimate secular purposes of solemnizing public occasions, expressing confidence in the future, and encouraging the recognition of what is worthy of appreciation in society. For that reason, and because of their history and ubiquity, those practices are not understood as conveying government approval of particular religious beliefs."[127] Goodwin dismissed this statement and others like it as mere dicta.[128] Even if one was to dismiss this statement as irrelevant, O'Connor would still likely vote for a reversal of the decision in *Newdow II*. This is because O'Connor may limit her endorsement analysis to instances of inherently religious exercises and, even if she did consider the pledge to be a religious exercise, its history and nonsectarian nature would lead her to conclude it does not convey a message of endorsement.

O'Connor would probably find compelling the dissent written by Judge O'Scannlain, in which he argues that the pledge is not a religious exercise. In her concurring opinion in *Wallace*, O'Connor stated that the previous school prayer decisions, "expressly turned on the fact that the government was sponsoring a manifestly religious exercise."[129] In that case, she contrasted a moment of silence from state-sponsored bible reading or prayer. In making this distinction she states, "[s]ilence, unlike prayer or Bible reading, need not be associated with a religious exercise."[130] Similarly, the argument is strong that the pledge, unlike prayer, is associated with patriotism and not religious exercise. Although the reference to God does have religious connotations, first and foremost, the main purpose of the pledge in the schools is to instill in children values of civic pride and patriotism. Because the practice is not inherently religious, O'Connor would likely view the pledge as not an explicit religious exercise subject to Establishment Clause scrutiny.

There is, however, a key distinction between a moment of silence and the pledge that may change the analysis. In *Wallace*, O'Connor points to the fact that during a moment of silence, the student does not have to compromise his or her own beliefs, as nothing is stated out loud, and the student is "not compelled to listen to the prayers or thoughts of others."[131] This is not the case with the pledge, as a student who does not believe in God, or believes in many Gods, is still compelled to hear the thoughts of others on the subject because the pledge is recited aloud. However, the thoughts that the student is compelled to hear are not devotional prayers. Because O'Connor would likely not view the pledge as inherently religious, she may not be bothered by the fact that all students are compelled to hear it.

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127. Lynch, 465 U.S. at 693.
128. Newdow I, 292 F.3d at 611.
129. Wallace, 472 U.S. at 72.
130. *Id.*
131. *Id.*

Even if it was found that the pledge was a religious activity, O'Connor may find it to be a permissible exercise of ceremonial deism. O'Connor has shown a reluctance to find a long-standing historical practice an establishment violation. In fact, the only instance where she abandoned her endorsement test was in *Marsh*, where she voted along with the majority to preserve the right to open legislative sessions with prayer because the practice's long history made it part of the "fabric of our society."[132] However, unlike the practice in *Marsh*, it was not until 1954 that the offending words "under God" were inserted into the pledge.[133] Fifty years of practice is probably not a lengthy history to justify abandoning endorsement analysis in this case. In *Lynch*, O'Connor stated that ceremonial deism would only serve as an exception when the practice has a long historical tradition of intermingling religion and government.[134] Therefore, O'Connor probably will analyze the case under her endorsement test.

The pledge would probably withstand scrutiny under endorsement because the history of the pledge and its nonsectarian nature would preclude a finding that a reasonable observer would view it as an endorsement of religion. In *Allegheny*, O'Connor framed the endorsement test as "whether a reasonable observer would view such longstanding practices as a disapproval of their particular religious choices, in light of the fact that they serve a secular purpose rather than a sectarian one and have largely lost their religious significance over time."[135] O'Connor has made it clear that the history of the practice alone is not enough to validate it under the Establishment Clause. Rather the history is relevant because "it provides part of the context in which a reasonable observer evaluates whether a challenged governmental practice conveys a message of endorsement of religion."[136] In perhaps the clearest statement on how O'Connor would come out on the pledge issue, she states:

> [t]he combination of the longstanding existence of practices such as opening legislative sessions with legislative prayers or opening Court sessions with 'God save the United States and this Honorable Court' as well as their nonsectarian nature, that lead me to the conclusion that those particular practices, despite their religious roots, do not convey the message of endorsement of particular religious beliefs.[137]

This is a key statement for many reasons. First, it reflects a definition of nonsectarian that is inapposite from the one expressed by the majority in *Newdow II*. In *Newdow II*, Goodwin stated that the phrase "under God" was identical for

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132. Marsh, 463 U.S. at 792.

133. H.R. 83-1693, 83rd Cong, (1954), reprinted in 1954 U.S.C.C.A.N. 2339.

134. Lynch, 465 U.S. at 693 (O'Connor, J., concurring) (citing legislative prayers, government declaration of Thanksgiving as a public holiday, the national motto, and the phrase "God save the United States and this honorable court" as examples that would fall under the ceremonial deism exception).

135. Allegheny, 492 U.S. at 631.

136. *Id.* at 630.

137. Allegheny, 492 U.S. at 630–31.

Establishment Clause purposes as "under Jesus."[138] By saying that "God save the United States and this Honorable Court" is nonsectarian in nature, O'Connor is expressing a belief that references to a divine creator generally are nonsectarian and, therefore, the phrase "under God" in the pledge would also be considered nonsectarian. Second, it shows that the history and a popular understanding that something is not meant to convey an endorsement of religion, will serve to excuse de minimus references from violating the Establishment Clause. Because of the numerous historical examples of general references to God, O'Connor could infer that the phrase "under God" has gained historical acceptance despite the fact that it has only been a part of the Pledge of Allegiance for the past fifty years. Therefore, a reasonable observer viewing this phrase in the context of history would not view these words as a state endorsement of religion.

In sum, since the pledge is consistent with O'Connor's view of what is nonsectarian and the use of words such as "under God" has gained historical acceptance, O'Connor would likely find that a reasonable observer would understand the purpose of the pledge to be patriotic and not an attempt to use the machinery of the state to proscribe religious orthodoxy. Therefore, she is likely to vote to reverse the decision in *Newdow*.

2. *Justice Kennedy*

The decision in *Newdow II* rested entirely on coercion analysis, meaning that it is solidly within Justice Kennedy's area of expertise. Unlike the accommodationalists, Kennedy is more open to the possibility of psychological coercion because he believes that there does not have to be an actual government enforced penalty for the conduct to be coercive. Writing for the majority in *Weisman*, Kennedy found that State practice of prayer, at a graduation ceremony, was coercive despite the fact that attendance was not mandatory.[139] Since Kennedy found that the prayer in the context of the public school graduation was coercive, it is likely that he would find the conduct in *Newdow II* coercive as well. In fact, there is a stronger case for coercion in *Newdow II* then there was in *Weisman*. First, the conduct in *Weisman* was a one-time event, while in *Newdow II* it is something that occurs every day.[140] Secondly, the conduct in *Weisman* occurred during a graduation ceremony, which is removed from the classroom.[141] In contrast, the pledge is recited while the students are in class and during regular school time. Third, though attendance was not required at the graduation ceremony, Kennedy understood that the students would not miss

138. Newdow I, 292 F.3d at 607.
139. Lee, 505 U.S. at 586.
140. *Id.* at 583.
141. *Id.*

an important life event to protest hearing a prayer they did not believe.[142] Contrast this with *Newdow II*, where attendance is legally required because it takes place during the actual school day and the students, who are elementary school age, are not free to enter and leave the room. For these reasons, Kennedy would most assuredly find that the recitation of the pledge in school is a coercive practice.

Despite Kennedy's probable agreement with the Ninth Circuit's conclusion that the practice is coercive, it is still likely that Kennedy will vote to reverse *Newdow II*. Kennedy has stated that even though "[s]peech may coerce in some circumstances . . . [it] does not justify a ban on all government recognition of religion."[143] In dicta, Kennedy has expressed a belief that the pledge is constitutionally permissible in stating:

> [B]y statute, the Pledge of Allegiance to the Flag describes the United States as "one Nation under God." (citation omitted) To be sure, no one is obligated to recite this phrase [see Barnette] . . . but it borders on sophistry to suggest that the " 'reasonable' " atheist would not feel less than a "full membe[r] of the political community' " every time his fellow Americans recited, as part of their expression of patriotism and love for country, a phrase believed to be false.[144]

Kennedy used this statement to explain how application of the endorsement doctrine would cause many religious references to be deemed unconstitutional. Ironically, this statement, used to show why the endorsement test is unworkable, and is the exact same analysis employed by the majority in *Newdow I* to justify finding the pledge unconstitutional. Regardless, this dicta shows that Kennedy believes the pledge as currently codified is not an Establishment Clause violation. Even if this statement can be dismissed as dicta, Kennedy would still probably vote for reversal because he will not view the recitation of the pledge as a religious exercise, because he believes that symbolic, ceremonial references to God survive Establishment Clause scrutiny.

Similar to Justice O'Connor, Kennedy will also likely question whether the pledge is a religious activity. In his decision in *Weisman*, Kennedy states that the prayer, in this case, was unconstitutional because the State compelled attendance and participation in what is "an explicit religious exercise."[145] Kennedy's decisions have distinguished between prayer and other activities. He agreed with the majority and found establishment violations in *Weisman*[146] (dealing with prayer at a graduation ceremony) and *Santa Fe*[147] (concerning

142. Lee, 505 U.S. at 595.
143. Allegheny, 492 U.S. at 661.
144. *Id.* at 672–73.
145. Weisman, 505 U.S. at 598.
146. *Id.* at 599.
147. Santa Fe Indep. Sch. Dist., 530 U.S. at 290.

student led prayer at football games). However, he authored the dissent in *Allegheny*, a case in which the majority held that the displaying of a crèche violated the Establishment Clause.[148] The question becomes, is the pledge more like a prayer or more like a display? It seems that Kennedy would require the practice to be an explicit religious exercise. The main purpose of prayer is religious, even if that prayer is nonsectarian. In *Allegheny*, Kennedy found that the main purpose of displaying the crèche was to celebrate the season and to recognize its historical background.[149] Since the main purpose of the pledge is patriotic, there is a strong argument that Kennedy would not find it to be a violation because it is not an explicit religious exercise.

Kennedy would also likely find that the pledge is a symbolic act, and therefore would not violate the clause. In *Allegheny*, Kennedy states, "[t]he Establishment Clause permits government some latitude in recognizing and accommodating the central role that religion plays in our society. (Citations omitted). Any approach less sensitive to our heritage would border on latent hostility toward religion. . . ."[150] In his analysis, he quotes a line from Justice Goldberg stating:

> Neither government nor this Court can or should ignore the significance of the fact that a vast portion of our people believe in and worship God and that many of our, legal, political and personal values derive historically from religious teachings. Government must inevitably take cognizance of the existence of religion.[151]

Thus, it is clear that Kennedy does see a place for symbolic recognition of religion by our government. However, he also stated that "[s]ymbolic recognition . . . of religious faith may violate the Clause in an extreme case."[152] The example he uses to describe an "extreme case" is the erection of a large Latin cross.[153] This choice of examples is important because it is sectarian, while the pledge is nondenominational. Under Kennedy's reasoning, nondenominational, symbolic recognition would probably not be an Establishment Clause violation.

Even though Goodwin's coercion analysis does comport with Justice Kennedy's understanding of coercion, expect Kennedy to vote to reverse *Newdow II* for other reasons. First, Kennedy appears to make a distinction between an explicit religious exercise and other practices. Secondly, Kennedy has shown an inclination to give wide latitude to the government in instances of nondenominational, symbolic recognition of religion. For these reasons, it seems more likely then not that Kennedy will vote to reverse *Newdow II*.

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148. Allegheny, 492 U.S. at 621.
149. *Id.* at 662.
150. *Id.* at 657.
151. *Id.* at 659.
152. *Id.* at 661.
153. Allegheny, 492 U.S. at 661.

3. *Justice Breyer*

Much like Justice Ginsburg, Justice Breyer has not written much on the Establishment Clause during his tenure. However, while Ginsburg has clearly sided with the separationalist block, Breyer's record does not reveal where along the spectrum from separationalist to accommodationalist his allegiance lies. He sided with the separationalists in *Santa Fe*,[154] *Agostini v. Felton*,[155] *Zelman v. Simmons-Harris*,[156] and *Rosenberger v. Rector* and *Visitors of University of Virginia*.[157] However, he agreed with the accommodationalists in *Good News Club v. Milford*,[158] *Mitchell v. Helms*,[159] and *Pinette*.[160] Breyer's most consistent trend in his Establishment Clause cases is that he has sided with O'Connor on issues of government speech on religious topics. One reason that Breyer has sided so often with O'Connor is because it seems that they share a similar belief that endorsement is the proper test to determine an establishment violation. For that reason, Breyer will probably vote in accordance with O'Connor on this issue, and since it is likely that O'Connor would not hold the pledge to be a violation, Breyer may very well follow suit.

There is evidence that Breyer has adopted the endorsement test. In his concurrence in *Good News Club*, Breyer framed the issue as "whether a child, participating in the Good News Club's activities, could reasonably perceive the school's permission for the club to use its facilities as an endorsement of religion."[161] In stating the issue this way, it appears, at least in cases of governmental speech on religion, that Breyer has supported endorsement analysis. In *Good News Club*, Breyer listed some factors the Court should use in deciding the endorsement issue, stating, "[t]he time of day, the age of the children, the nature of the meetings, and other specific circumstances are relevant in helping determine whether,. . .in the children's minds, 'a formal policy of equal access is transformed into a demonstration of approval."[162] Using these factors,

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154. Santa Fe Indep. Sch. Dist., 530 U.S. at 290.

155. Agostini, 521 U.S. at 203 (holding program which sent public school teachers into parochial schools to provide remedial education to disadvantaged kids did not violate the Establishment Clause).

156. Zelman v. Simmons-Harris, 536 U.S. 639 (2002) (holding that a school voucher program did not violate the Establishment Clause).

157. Rosenberger v. Univ. of Virginia, 515 U.S. 819 (1995) (holding that the use of university funds for printing costs on student publications did not violate the Establishment Clause because the program was neutral toward religion).

158. Good News Club v. Milford Central Sch., 533 U.S. 98 (2001) (holding that a school's viewpoint discrimination, in refusing to allow a religious club to use school facilities, was not required to avoid violating the Establishment clause).

159. Mitchell v. Helms, 530 U.S. 793 (2000) (held that a government program which distributed funds to state and local governmental agencies, which in turn lend educational materials and equipment to public and private schools, does not violate Establishment Clause).

160. Capitol Square Review and Advisory Bd., 515 U.S. at 753 (holding that state did not violate Establishment Clause by permitting Klu Klux Klan to display cross on grounds of state capitol).

161. Good News Club, 533 U.S. at 128–29.

162. *Id.*

Breyer may find that the school policy in *Newdow II* was a violation. First, the time of day was during school hours, making the chances that the students will believe the school is endorsing the speech much greater. Secondly, Newdow's daughter was an elementary school student, which is an age especially susceptible to indoctrination. Finally, the fact that the recitation was teacher-led cuts toward a finding that the practice was an establishment violation.

Even though Breyer's, has exhibited a closer identification with the separationalists then the accommodationalists on Establishment Clause issues, he may very well vote in favor of reversal of the Ninth Circuit's decision. Breyer's past voting record on issues involving governmental speech on religious subjects and belief in the endorsement test suggest strongly that he will vote alongside O'Connor. However, Breyer could easily vote to affirm because the California school board policy may be particularly troublesome due to the context in which the pledge is recited. Because O'Conner and Kennedy should side with the two accommodationalists, Breyer may very well hold the fate of the pledge in his hands. Due to the fact that Scalia has recused himself from the decision, if Breyer votes to affirm *Newdow II*, the Court will likely have a 4-4 split.

IV. THEORIES ON THE INTERACTION OF ESTABLISHMENT AND CEREMONIAL DEISM

Overall, the Supreme Court's Establishment Clause jurisprudence can only be described as inconsistent. Sometimes the justices would apply *Lemon* with great particularity, and other times the *Lemon* test is absent from the analysis. Justice O'Connor believes that a reason for this inconsistency is Establishment Clause issues are not subjectable to a one size fits all test. In *Kiryas Joel v. Grumet*, O'Connor stated that "[e]xperience proves that the Establishment Clause, like the Free Speech Clause, cannot easily be reduced to a single test. There are different categories of Establishment Clause cases, which may call for different approaches."[163] The different categories she mentions are cases in which a specific group is targeted by the government for either special benefits or burdens, cases in which the government must make decisions about matters of religious doctrine, cases involving government delegations of power to religious bodies, and cases involving government speech on religious topics.[164]

This case fits into the last category of cases involving government speech on religious topics. However, there should be a subcategory within this group dedicated to symbolic and historical religious expressions. The Court has already recognized that because the *Lemon* test fails to take into account the his-

163. Bd. of Educ. of Kiryas Joel Vill. Sch. Dist. v. Grumet, 512 U.S. 687, 720 (1994) (holding statute creating special school district following village lines for religious enclave incorporated as village to exclude all but its practitioners violated Establishment Clause).

164. Grumet, 512 U.S. at 720.

tory of a practice, it should not be used in all cases.[165] In *Marsh*, the appeals court found that Nebraska's practice of employing legislative chaplains to open up each legislative session with a nondenominational prayer violated all three prongs of the *Lemon* test.[166] The Supreme Court reversed this decision primarily because of historical evidence that the framers had themselves employed such legislative chaplains.[167] Thus, the Court's decision turned, on the fact, that the practice was one, which was rooted in historical tradition.

Many scholars have tried to formulate a new, single test that would allow the courts to take into account the history of a particular practice in determining whether it was a violation. In order to gain acceptance across the political spectrum, any new theory to deal with this issue must allow the courts to do two fundamental things. First, the theory should allow for at least some of these ceremonial references to continue because the courts do not want to drive a steamroller over all instances of religion in the public sphere. Second, the test needs to be able to prevent the creation of new practices under the guise of ceremonial deism, because this could have the dangerous effect of bringing the public and religious realm impermissibly closer together.

The first of the theories is the unbroken practice justification. Under this test, a religious practice may be justified because it has existed for a long time and has traditionally not been found to violate the Constitution.[168] Examples of such practices are the national motto, "In God We Trust," which dates back to 1864 and the National Day of Prayer, which began in 1775.[169] In *ACLU v. Capitol Square Review and Advisory Board*, the Sixth Circuit relied on the unbroken practice theory in finding that the Ohio motto, "With God, All Things Are Possible," does not violate the Establishment Clause.[170] Despite the fact that the motto was adopted in 1959, the *Capitol Square* majority viewed its use in the context of a long tradition of government acknowledgement of religion.[171]

Several problems have been identified with the use of the unbroken practice theory. First, looking to history to justify a practice as constitutional can be

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165. Marsh v. Chambers, 463 U.S. 783, 786 (1983).

166. *Id.*

167. *Id.* at 786–89.

168. *See* Benjamin S. Genshaft, *With History, All Things are Secular: The Establishment Clause and the Use of History*, 52 CASE W. RES. L. REV. 573 (2001) (arguing that the endorsement test provides the best framework to analyze Establishment Clause issues because it allows the court to take the history of a practice into account).

169. *See* Ashley Bell, *"God Save this Honorable Court": How Current Establishment Clause Jurisprudence can be Reconciled with the Secularization of Historical Religious Expressions*, 50 AM. U. L. REV. 1273, 1314 (2001) (arguing that for nonpreferentialist analysis with a historical inquiry as the best approach for Establishment Clause determinations).

170. ACLU v. Capitol Square Review and Advisory Bd., 243 F.3d 289, 305 (6th Cir. 2001) (en banc).

171. *Id.* at 299.

misleading because, as Souter argued, the framers were, after all, politicians who could have turned their backs on the establishment ideals to please a more religious constituency.[172] Second, the courts have not drawn a distinction between specific and general history.[173] In *Capitol Square*, the Sixth Circuit court looked to the general history of religion in this country rather then the specific history of the motto in question in finding that it was not an establishment violation.[174] Such a use of general history could allow the unbroken practice theory to act as a loophole to justify every ceremonial religious practice, no matter how recently that practice was implemented. Lastly, the test does nothing to obviate the concerns about subjectivity on the part of judges because the courts can engage in a selective reading of history.[175] Therefore, adoption of the unbroken practice test would not lead to consistent results among the courts.

The inconsistency of this test is evident by applying it to the facts in *Newdow*. Whether or not the pledge is determined to be constitutional under this test would depend on the particular judge. If the judge used general history (which is what the accommodationalists would do under this test) the pledge would be constitutional because, as the Sixth Circuit expressed in *Capitol Square*, there has been a long history government acknowledgement of religion generally.[176] However, if the court looked to specific history of the pledge it would have difficulty getting around the fact that the words "under God" did not appear until fifty years ago. Thus, the resolution of the issue would depend on how the court used the history.

Another theory on how to deal with traditional, symbolic religious expressions is the secularization rational.[177] Under this test, practices that would have at the time of their creation failed any one of the three Establishment Clause tests may still be found constitutional through repetitive use. This approach is consistent with the views of some members of the Court. However, this secularization rational has also been attacked as inconsistent. For example, the Court has found that a crèche was sufficiently secularized in one circumstance,[178] but that same crèche was not in another,[179] because of the surrounding context. Another argument against secularization analysis is the belief that it does a disservice to religion by taking away the religious meaning of such symbols and requiring them to be a generic, water-down version of the relig-

172. Lee, 505 U.S. at 626; "those practices prove, at best, that the Framers simply did not share a common understanding of the Establishment Clause, and, at worst, that they, like other politicians, could raise constitutional ideals one day and turn their backs on them the next".

173. Genshaft, *supra* note 168, at 585.

174. Capitol Square, 243 F. 3d at 296–99.

175. Genshaft, *supra* note 168, at 585.

176. Capitol Square, 243 F. 3d at 296–99.

177. Bell, *supra* note 169, at 1294-95 (arguing that for nonpreferentialist analysis with a historical inquiry as the best approach for Establishment Clause determinations).

178. Lynch, 465 U.S. at 694.

179. Allegheny, 492 U.S. at 637.

ion.[180] In *Lynch*, the crèche was described by the Court as "engender[ing] a friendly community spirit of good will in keeping with the season."[181] Finally, the secularization analysis does not seem to take into account whether the practice prefers a particular religious sect. One scholar has even suggested that the courts are more likely to secularize practices derived from Christianity then other minority religions.[182]

Yet another suggested test would combine the requirement of nonpreferentialism with an inquiry into the historical basis of the practice.[183] In effect, under this analysis, the practice would have to pass two tests. First, the practice must be nonpreferential on its face.[184] Second, the practice would have to be deeply rooted in history.[185]

The pledge would likely pass the first prong of this test, which asks whether the practice is nonpreferential, as it contains only a general reference to God and does not use any words that are inherent to one particular faith. The Ninth Circuit would not view the pledge as nonpreferential because the phrase "under God" shows a preference for theism.[186] However, if use of the word "God" is deemed preferential, all public references to God may be eliminated. The result would be to greatly broaden the scope of the Establishment Clause and force the Court to revisit many past decisions. Also, the fact that the phrase "under God" did not originate in any religious book or passage supports a finding that it is nonpreferential.[187] Some commentators have disagreed that the expression should be required to be nonpreferential in its origin, fearing that due to the growing number of religions the government will run the risk of violating the Establishment Clause anytime it speaks because the words may be contained in some religious text.[188] In short, resolution of this issue depends on whether the government practice can take a position on theism and still be considered nonpreferential.

The second part of this proposed test asks whether the practice in question is one deeply rooted in this country's history. Whether the pledge is deeply rooted

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180. Bell, *supra* note 169, at 1305–06.

181. Lynch, 492 U.S. at 685.

182. Alexandra D. Furth, Comment, *Secular Idolatry and Sacred Traditions: A Critique of the Supreme Court's Secularization Analysis*, 146 U. PA. L. REV. 579, 604 (1998) (arguing that because secularized practices are most frequently derived from Christianity, the Court is not only choosing religion over no religion but also Christianity over all).

183. Bell, *supra* note 169, at 1312; "this new approach would look to whether practices are deeply rooted in history and whether they are historically nonpreferentialist."

184. *Id.*

185. *Id.*

186. Newdow I, 292 F.3d 597, 607 (9th Cir. 2002).

187. *See contra* ACLU, 243 F.3d at 289 (en banc) (holding that the Ohio state motto does not violate the Establishment Clause despite the fact that the phrase was taken directly from the New Testament).

188. Theologos Verginis, *ACLU v. Capital Square Review and Advisory Board: Is There Salvation for the Establishment Clause? "With God All Things are Possible."* 34 AKRON L. REV. 741, 764 (2001) (expressing concern over the further complication of Establishment clause analysis).

in history is a tough question because the offending words were added only fifty years ago. Is a fifty-year period enough to justify calling it a historical practice under this prong? Should the courts be allowed to look to the history of references to God generally or should they be regulated to the specific history of the phrase in the pledge? If courts look to history of general references to God, they will probably not find the phrase objectionable because there are many other historical practices that have the same reference to God, which do posses the required longevity.

While this test is better then the unbroken practice theory and secularization theory because it takes into account the nonpreferentiality of the practice, it is not immune from criticism. First, the historical prong is similarly susceptible to judicial manipulation, as the courts could choose to cite either general history or specific history in formulating its historical analysis. Second, the nonpreferential view fails to address the argument that the government may not favor religion over non-religion generally. Only the accommodationalists on the Court take the view that the Establishment Clause was only intended to prevent discrimination between religious sects. However, this may not be a problem for those who ascribe to the theory that the word "religion" in the First Amendment context describes only theistic belief systems.[189]

A more simplistic and probably the best solution, is to adopt Justice O'Connor's endorsement test in all cases dealing with government speech on religious subjects. This is because endorsement analysis allows the courts to factor in historically based arguments. Endorsement asks whether a reasonable observer would regard the practice as an endorsement of religion. In *Pinette*, O'Connor stated that this reasonable observer is "aware of. . . history."[190] In analyzing the history under the endorsement test, the courts should take into account such factors as the longevity of the historical practice; the existence of other similar historical practices; the primary purpose of the practice (patriotic, ceremonial, etc.); whether it is nonsectarian; and whether the practice has religious origins. Because endorsement allows the Court to take all of these historical factors into account, it is the proper test to use when analyzing these historical and ceremonial practices.

The best argument against using the endorsement test in dealing with historical practices is that the test is very subjective and, therefore, has produced unpredictable results. To lessen the impact of this subjectivity, there should exist some limitations on how the courts may use history in its analysis. First, the courts should never use tradition as the sole reason to justify a decision.[191] This

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189. Lee J. Strang, *The Meaning of "Religion" in the First Amendment*, 40 DUQ. L. REV. 181 (2002) (arguing that the Establishment Clause was not intended to protect atheism or monotheistic beliefs).

190. Capitol Square Review and Advisory Bd., 515 U.S. at 781 (O'Connor, J., concurring).

191. *See* Genshaft, *supra* note 168, at 573 (2001) (arguing for a more appropriate way for the courts to use the history of a practice in its Establishment Clause security).

limitation was recognized in *Marsh*, where the Court stated "[s]tanding alone, historical patterns cannot justify contemporary violations of constitutional guarantees."[192] Second, "the tradition used must be the specific tradition and history of the practice, not merely a reference to a general history of government involvement in religion."[193] This requirement of specificity will keep the courts from using general theories of the mingling of government and religion to justify a conclusion. Further, this will protect against the courts using general history to totally swallow Establishment Clause jurisprudence. In adhering to this limitation, the courts should not look to other unrelated practices that are rooted in tradition and decide that the practice in question is not more dangerous than an unrelated one. These two limitations will keep the courts from overly relying on history in determining whether a religious practice is constitutional.

The result of endorsement analysis in this case will be a finding that the Pledge of Allegiance does not violate the Establishment Clause because a reasonable observer would not view the pledge as an attempt by the state to enforce a religious orthodoxy. The pledge is nonsectarian and does not owe its origin to any religious canon. There are many specific examples of longstanding historical practices that use the exact phrase "under God" or have a very similar reference to God. Finally, when viewed in context, the overall message of the pledge is patriotic, rather then religious. All of these factors point to the conclusion that a reasonable observer would not view the pledge as a government endorsement of religion.

V. CONCLUSION

The Pledge of Allegiance is not a violation of the Establishment Clause because any reasonable observer would not view this predominately patriotic exercise to be a government endorsement of religion. However, while the *Newdow II* decision may have been legally wrong, as a matter of policy, inclusion of the words "under God" may only take away from the true purpose of the Pledge of Allegiance. The fact that inclusion of this reference to God may cause people to choose not to repeat the affirmation is unacceptable because it is in this country's interest to have an affirmation of pride, which every citizen can repeat without feeling conflicted. As more children are brought up repeating the pledge, the better off this country is from a patriotic standpoint. Why would we not want every child, not just those who believe in monotheism, to remember every morning that we are a republic, by the people, dedicated to bringing justice for all people.

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192. Marsh, 463 U.S. at 790.

193. Genshaft, *supra* note 168, at 597.

However, it is for Congress and not the courts to make this change. In 1954 the words "under God" were inserted into the pledge for the arguably secular purpose of distinguishing the American people from the communists who had removed religion from their society. Communism is no longer our enemy, so the secular purpose of this Act is no longer valid.[194] Now, the chief threat to this country comes not from the "Godless" communists, but rather from terrorist empires acting on what they believe is God's behalf. If it is the desire of Congress to use the Pledge of Allegiance to distinguish America from her enemies, the same rational, which formed the impetus for the decision to insert the words "under God" should be utilized in its removal. As Americans are growing increasingly irreligious, these words of exclusion can only take away from the true ideal, which this country stands for. Our message should be clear: America stands for justice for all, regardless of whether one believes in one God, no God, or many Gods.

194. The fact that an important purpose of the 1954 Act is no longer valid might change the Lemon analysis if the Court was deciding on the constitutionality of the 1954 Act. However, because there were other arguably legitimate secular purposes in amending the pledge, it would probably not be enough for a majority of the Court to find the 1954 Act unconstitutional.

"One way to hide a log is to put it in the woods . . ."[1] CEO/CFO responsibility after the "Sarbanes-Oxley Act": Drowning the "reasonable investor" in details to escape civil liability

TIMOTHY J. WELSH*

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* Timothy J. Welsh, J.D., 2004, Syracuse University College of Law, B.A., 1999, Fairfield University. Mr. Welsh will be working for the United States' Securities and Exchange Commission after graduation.

1. Bethany McLean, *Why Enron Went Bust*, FORTUNE, Dec. 24, 2001, at 58 (quoting Congressman John Dingell's call for an investigation into Enron).

INTRODUCTION

A. AN "ENDRUN" AROUND THE SECURITIES AND EXCHANGE COMMISSION'S DEFENSE: A HYPOTHETICAL.[2]

In the wake of a number of large financial scandals Congress passed the "Sarbanes-Oxley Act of 2002," (hereinafter Act) in order "to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws."[3] A committee report, presented by Representative Oxley, stated the need for legislation as concern "about the adequacy of the current disclosure regime for public companies" after "the bankruptcies of Enron Corporation and Global Crossing LLC, and restatements of earnings by several prominent market participants."[4] The key to the future adequate disclosure is the requirement that CEOs certify all company periodic reports, required under section 13(a) or 15(d) of the Securities Exchange Act of 1934, which did not "contain any untrue statement of material fact or omit to state a material fact."[5] At the time of the Act's passing, the accepted standard for what was "material" depended on "the significance the reasonable investor would place on the withheld or misrepresented information."[6] What the report, and the Sarbanes-Oxley Act, seem to fail to consider, are situations where a public company does provide "full and accurate disclosure of the true condition of the company" but that "material" information is incomprehensible to the "reasonable investor" because they lacked the sophistication to understand it.[7]

Imagine a situation where a company, we will call "Endrun," whose core business was originally the distribution of a energy products, began to take advantage of deregulation and starts to trade energy and natural gas futures.[8]

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2. This hypothetical is based very closely on what has become known as the "Enron Scandal," which has been widely discussed throughout various media; the key distinction being that unlike the real Enron collapse, in this hypothetical "Endrun" fully discloses its use of legal "off-balance sheet" risk hedging transactions to the securities markets; McLean, *supra* note 1; The Daily Enron, *Enron: a General Overview*, Enron 101, *available at* http://www.thedailyenron.com/enron101/overview.asp (last accessed on Jan. 26, 2003 and on file with author). This website was run by American Family Voices "to be a strong voice for middle and low income families on economic, health care, and consumer issues."

3. Public Company Accounting Reform and Investor Protection Act, Pub. L. 107–204 (H.R. 3763), 107th Cong., preamble (2002) [hereinafter Sarbanes–Oxley Act of 2002].

4. H.R. REP. NO. 107–414, at *18 (2002), *reprinted in* 2002 U.S.C.C.A.N. 542, 2002 WL 661614 (Report of the Committee on Financial Services).

5. 15 U.S.C.A. § 7241 (a)(2) (2002); Sarbanes–Oxley Act Sec. 302 (a)(2); "Corporate Responsibility For Financial Reports."

6. Basic, Inc. v. Levinson, 485 U.S. 224 at 240 (1998).

7. H.R. REP. NO. 107–414, at *18 (2002), *reprinted in* 2002 U.S.C.C.A.N. 542, 2002 WL 661614.

8. Michael Schroeder, *Building the House of Enron*, WALL ST. J., Jan. 28, 2002, at C1; *See also*, A "future" of "futures contract," which is "An agreement to buy of sell a standardized asset (such as a commodity, stock, or foreign currency) at a fixed price for a future time, usually during a particular time of a month." BLACK'S LAW DICTIONARY 685 (7th ed. 1999). The future operates "to sell goods or commodities at a future time at a specified price. The buyer agrees to pay that fixed price and the seller

Eventually the largest part of Endrun's profits began to flow from its trading of an unregulated financial product known as "derivatives," which "derive their value from an underlying commodity or wager on the future."[9] If Endrun had been a bank, its trading would have made it one of the ten largest derivatives dealers in the world, but it still would not be required to provide the Securities and Exchange Commission (SEC) with any "agency detailed information about its over-the-counter trading activities" due to an exemption from such regulation that had been passed by Congress in late 2000.[10]

Endrun had great success in trading derivatives and quickly began to have sizable consistent earnings, which caught the securities market's attention, and helped it become one of the ten largest companies on the FORTUNE 500.[11] In order to protect itself from the inherent risk of trading such exotic derivative products, and to continue to report consistent earnings, Endrun set up a number of partnerships, to be managed by Endrun directors, which it used to protect itself from the losses in the futures derivative markets it participated in.[12] In

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agrees to deliver the goods although the parties do not actually contemplate delivery, but rather that the contract calls for a settlement between the parties according to market prices. If the value of the commodity has risen, the seller pays the buyer the amount of the increase; if the value of the commodity falls, the buyer pays the seller the decrease." GILBERT LAW DICTIONARY 127 (Pocket ed. 1997).

9. Schroeder, *supra* note 8, at C1; *See also,* "derivative," which is "A volatile financial instrument whose value depends on or is derived from the performance of a secondary source such as an underlying bond, currency, or commodity. . .Within the broad panoply of derivatives transactions are numerous innovative financial instruments whose objectives may include a hedge against market risks, management of assets and liabilities, or lowering of funding costs; derivatives may also be used as speculation for profit." BLACK'S LAW DICTIONARY 454 (7th ed. 1999) (quoting Procter & Gamble Co. v. Bankers Trust Co., [1996-1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) P99, 229, at 95, 238 (S.D. Ohio 1996)).

10. *See* Schroeder, *supra* note 8, at C1; *see also,* "over-the-counter" or "over-the-counter-market" describing securities that are "not listed or traded on an organized securities exchange; traded between buyers and sellers who negotiate directly." BLACK'S LAW DICTIONARY 1130 (7th ed. 1999).

> "Innovations in technology and finance have helped obliterate clear distinctions between banks, brokerage firms and newer hybrids, such as Enron. But financial regulators hew to decades-old divisions of authority, continuing to keep a close watch on banks, brokerage firms and conventional exchanges, while leaving new entrants such as Enron to police themselves. In late 2000, Congress passed legislation that exempted from regulation over-the-counter derivatives, which are contracts arranged among *sophisticated* buyers and sellers such as banks, Wall Street firms and public companies. The measure had support from both parties, as well as the Federal Reserve and the Clinton administration."

Schroeder, *supra* note 8 (emphasis added). The question of whether and how the government should have regulated over-the-counter securities, while related to the Enron collapse, will not be directly discussed in this note.

11. *See e.g.*, McLean, *supra* note 1, at 58 (reporting on Enron's "Culture of Arrogance" the article recounts how Enron was created by the merger of two gas pipelines, began to trade all manner of futures, and from 1998 to 2000 saw revenue growth from $31 billion to over $100 billion, "making it the seventh-largest company on the FORTUNE 500.").

12. *See e.g.*, Jeanne Cummings et al., *Law Firm Reassured Enron on Accounting*, WALL ST. J., Jan. 16, 2002, at A18. (describing how Enron would create special purpose partnerships in order to manage their risk). *See, also,* SEC Integrated Disclosure System For Small Business Issuers, 17 C.F.R. §§ 228,

effect the partnerships, which were to be run by a senior Endrun officer, and have to pay Endrun, if the price of Endrun's commodities fell.[13] At the same time, while these partnerships took the risk for Endrun's potential losses, Endrun would prop up the partnerships with shares of its stock, which was constantly rising due to its tremendous earnings.[14]

Because of the tremendously consistent earnings growth that Endrun was able to produce, the securities market rewarded Endrun with a very high stock price.[15] Endrun's high stock price continued to prop up its off balance sheet partnerships, which in turn allowed Endrun to keep more bad derivatives trades off its books through "mark-to-market" accounting.[16] Endrun's accounting resulted in higher reported earnings, which raised its overall stock price.[17] To some this sounds remarkably like a "Ponzi scheme."[18] Eventually the market called Endrun's mark-to-market accounting into question and many began to pull their investments from the stock.[19] This led to Endrun's inability to keep bad debt off their books, and the stock price's eventual collapse, taking thousands of investors' total equity portfolios with it.[20] And the question on everyone's lips was "where were the regulators who were supposed to stop this?"

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229. 249 (2003). The SEC has issued rules on disclosure of off-balance sheet transactions contained in: Final Rule: Disclosure in Management's Discussion and Analysis about Off-Balance Sheet Arrangements and Aggregate Contractual Obligations, Release No. 33–8182, 34–47264 (Jan. 27, 2003). In summary the new regulations require a separate section in the Management's Discussion and Analysis of the issuer's use of off-balance sheet transactions. For the purposes of this note the use and regulation of off-balance sheet transactions will not be discussed in depth. Any mention of off-balance sheet transactions in this note's hypothetical is assumed to comport with the disclosure laws for such transactions.

13. *See,* McLean, *supra* note 1, at 58; *see also,* "exposure" "The amount of liability or other risk to which a person is subject. . .[for instance] the client wanted to know its exposure before it made a settlement offer." BLACK'S LAW DICTIONARY 601 (7th ed. 1999).

14. *See, e.g.,* McLean, *supra* note 1, at 58; Jeanne Cummings et al., *supra* note 11, at A18.

15. *See* McLean, *supra* note 1, at 58.

16. *Id.*

17. *Id.* (noting that Enron's use of such accounting had the same result on its stock price); *see also,* "fair-value accounting method" "The valuation of assets at present actual or market value." BLACK'S LAW DICTIONARY 20 (7th ed. 1999).

18. *See,* "Ponzi scheme," which is "A fraudulent investment scheme in which money contributed by later investors generates artificially high dividends for the original investors, whose example attracts even larger investments. Money from the new investors is used directly to repay or pay interest to old investors, usually without any operating or revenue-producing activity other than the continual raising of new funds. The scheme takes its name form Charles Ponzi, who in the late 1920s was convicted for fraudulent schemes he conducted in Boston." BLACK'S LAW DICTIONARY 1180 (7th ed. 1999).

19. *See,* McLean, *supra* note 1, at 58.

20. *Id.*

B. BACKDROP

> "Why aren't all of you in jail? And not like white-guy jail - - jail jail. With people by the weight room going, 'Mmmm.'"[21]

That was the question that Jon Stewart, host of "The Daily Show," a satirical news broadcast, shouted in early 2002, after the faces of executives from Enron and Arthur Anderson flashed across the screen.[22] By early 2002 the news had been full of a wave of white-collar crimes.[23] From an alleged "pervasive scheme" demanding excessive trading fees from customers at Credit Suisse First Boston, to Waste Management's overstatement of some $1.4 billion dollars income under Arthur Anderson's supervision, the country had seen a great deal of what was wrong with corporate America.[24] It is not surprising then, that when the news Enron's scandal broke that "political rehabilitationists" were hoping that the fallout would bring reform to everything from accountancy to corporate governance,[25] and would answer why with so many white-collar crimes "hardly anyone ever went to prison."[26]

By the time it had began to debate the final version of the Sarbanes-Oxley Act (the "Act"), Congress had seen the country hit with many more corporate scandals. Thus, Congress sought to "protect investors by improving the accuracy and reliability of corporate disclosures."[27] When the Sarbanes-Oxley Act was passed on July 23, 2002 the nation was in the midst of a surge of reform, which had been set-off by scandals at Enron,[28] Tyco,[29] Worldcom,[30] Global Crossing,[31] and Adelphia,[32] which fueled Congress' zeal to reform. As part of the final Act, Congress greatly increased the penalties for corporate fraud by

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21. Clifton Leaf, *Enough Is Enough*, FORTUNE, Mar. 18, 2002, at 60 (*quoting* Jon Stewart).

22. *Id.*

23. *Id.*

24. *Id.*

25. Daniel Henninger, *Wonder Land: Take It to the Limit Is National Anthem of America's Pols*, WALL ST. J., Feb. 15, 2002, at A16.

26. *See* Leaf, *supra* note 19, at 60.

27. Sarbanes-Oxley Act of 2002, *supra* note 3.

28. *See* McLean, *supra* note 1, at 58. (noting Enron's management is accused of using off-balance sheet transactions to hide upwards of $4 billion in debt).

29. Nicholas Varchaver, *Fall From Grace*, FORTUNE, Oct. 28, 2002, at 112 (reporting that Tyco's former CEO, CFO, and Chief Corporate Counsel have all been charged with grand larceny, conspiracy, and falsifying business records, and taking over $600 million from the company for personal gain).

30. Alfred Rappaport, *Show Me the Cash Flow!*, FORTUNE, Sept. 16, 2002, at 192 (reporting that WorldCom "buried uncollectable customer receivables, write-offs of investments, and restructuring charges").

31. *Id.* (noting that Global Crossing fictitiously reported future earnings as revenues).

32. Devin Leonard, *The Adelphia Story*, FORTUNE, Aug. 12, 2002, at 136 (noting that Adelphia had $2.3 billion in off balance sheet loans to CEO John Rigas and his family).

corporate executives, the people that average Americans most associated with the scandals.[33]

Unfortunately, in Congress' rush to legislate in response to the scandals, they were "sloppy in its effort to hold senior executives feet closer to the fire,"[34] by continuing to define the standard for what "material" information must be included in financial reports in terms of what a "reasonable investor" would find significant.[35] This article proposes that without a new definition of what constitutes a "material" fact, which would need to be disclosed as part of the new financial certification requirements, corporate CEOs and CFOs will have no incentive to make their statements clear enough for investors to avoid another Enron.

C. OVERVIEW OF NOTE

In proposing a new standard for what is a "material" fact for the purposes of inclusion in SEC reporting of issuer's financial statements, this article will first review the adoption of the Sarbanes-Oxley Act of 2002 in section one. Section two will address the Commission's final rule for "Certification of Disclosure in Companies' Quarterly and Annual Reports" as authorized under the Act.[36] Specifically, section two will address two cases, cited by the SEC to describe the statutory disclosure standards for material accuracy.[37] The cases on which the SEC relies suggest, "Materiality depends on the significance the reasonable investor would place on [any] withheld or misrepresented information."[38] In clarifying the materiality standard the court in Basic, Inc. v. Levinson,[39] and the SEC, in its final rule,[40] made reference to the scienter and reliance elements in § 10(b)[41] and Rule 10b–5[42] of the Securities Exchange Act of 1934. Section three will return to the hypothetical at the start of the note, and demonstrate how an issuer could be compliant with the standards for material disclosures as understood after the adoption of the Sarbanes-Oxley Act and still fail in preventing an Enron-like collapse. Section four will propose a change in the

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33. 18 U.S.C.A. § 1350 (c)(2); Sarbanes-Oxley Act of 2002, § 906(c)(2) (setting the maximum criminal penalties for failure to certify financial reports at a fine of $5,000,000 and imprisonment for 20 years).

34. Paul Beckett, *Executives Face Harsh Sanctions In Corporate-Governance Law*, WALL ST. J., July, 31, 2002, at C7 (reporting that some lawyers felt that Congress was in a rush to legislate).

35. Basic, Inc. v. Levinson, 485 U.S. 224, 240 (1998).

36. SEC Integrated Disclosure System For Small Business Issuers, 17 C.F.R. §§ 228, 229, 232, 240, 249, 270, 274 (2003). Final Rule: Certification of Disclosures in Companies' Quarterly and Annual Reports, S.E.C. Rel. No. 33-8124, 34–46427 (Aug. 29, 2002).

37. *Id.* (citing TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976); and *Basic, Inc.*, 485 U.S. at 224 (1988)).

38. Basic, 485 U.S. at 240.

39. *Id.* at 243.

40. S.E.C. Rel. No. 33–8124, 34–46427.

41. 15 U.S.C.A. § 78j (West 1997 & Supp. 2003).

42. 17 C.F.R. § 240.10b–5 (2003).

interpretation of what is a material fact that should be included in corporate financial reports, which could prevent future collapses of reporting companies.

I. ADOPTION OF THE SARBANES-OXLEY ACT OF 2002 AND ITS BURDEN ON CEO/CFOs.

When the Sarbanes-Oxley Act of 2002 was passed its purpose was "to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws."[43] The Act set out to strengthen the financial markets by creating the Public Company Accounting Oversight Board,[44] which demanded auditor independence,[45] and required enhanced financial disclosures.[46] Partially in response to the wave of corporate fraud committed by company executives,[47] Congress included a section on CEO/CFO liability for any misleading information included in the companies' filing of periodic reports.[48]

In legislating the "Corporate Responsibility For Financial Reports" in section 302 of the Act,[49] Congress amended the existing securities laws, codified in the Securities Act of 1933,[50] and the Securities Exchange Act of 1934,[51] and hoped to improve the quality of the information included in required financial reports.[52] Among the provisions of section 302 Congress required that "for each company filing periodic reports under §§ 13(a)[53] or 15(d)[54] of the Securities Exchange Act of 1934" the CEO or CFO or "persons performing similar functions," must certify "in each annual or quarterly report filed or submitted under either section of such Act that":[55]

> (1) The signing officer has reviewed the report; (2) Based on the officer's knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading; (3) Based on such officer's knowledge, the financial statements, and other financial information included in the report, fairly present in

43. Sarbanes-Oxley Act of 2002, *supra* note 3.
44. H.R. 3763, § 101, 107th Cong. (2d Sess. 2000).
45. H.R. 3763, title II, 107th Cong. (2d Sess. 2000).
46. H.R. 3763, title III, 107th Cong. (2d Sess. 2000).
47. *See*, Beckett, *supra* note 14.
48. H.R. 3763-62 § 1350 (c)(1), 107th Cong. (2d Sess. 2000).
49. 15 U.S.C.A. § 7241(a) (2002).
50. 15 U.S.C.A. § 77a (West 1997 & Supp. 2003).
51. 15 U.S.C.A. § 78a (West 1997 & Supp. 2003).
52. H.R. 3763, preamble, 107th Cong. (2d Sess. 2000).
53. 15 U.S.C. § 78m (West 1997 & Supp. 2003).
54. 15 U.S.C. § 78o(d) (West 1997 & Supp. 2003).
55. 15 U.S.C.A. § 7241(a) (2002).

> all material respects the financial condition and results of operations of the issuer as of, and for, the periods presented in the report.[56]

Failure to certify such reports brought with it criminal penalties of a fine of up to "$1,000,000 or imprison[ment] not more than 10 years, or both" for "knowing" certification of reports that do not comport with the requirements of §§ 13(a) and 15(d) of the 1934 Act.[57] "Willful" certification of any statement which did not fully comply with §§ 13(a) and 15(d), or did not "fairly present" information "in all material respects," could carry a criminal penalty of up to "$5,000,000, or imprison[ment] not more than 20 years, or both."[58]

Besides certification that the report "fairly presents in all material respects the financial condition of the issuer"[59] the Act also required certification that signing officers were responsible for establishing and maintaining "internal controls," which had been designed to ensure material information relating to the issuer is made known.[60] The effect of section 302 was the same on issuers with foreign incorporation as it was on those incorporated in the United States.[61] In promulgating the requirements of section 302 of the Act, Congress did not define by what standard the officer's are considered to have "knowledge" of whether all "material" facts are included in the reports or whether reliance upon those facts must be proved in order to find a violation of section 302's certification requirements.[62] If any clarification of what the standards of CEO/CFO knowledge and materiality would to come from the Act it seems that Congress left this task to the SEC in their required rulemaking,[63] which was to come within 30 days after the enactment of the Act.[64]

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56. 15 U.S.C.A. § 7241(a)(1)–(a)(3) (2002).

57. H.R. 3763-62 § 1350 (c)(1), 107th Cong. (2d Sess. 2000).

58. *Id.*

59. 15 U.S.C.A. § 7241(a)(3) (2002).

60. *Id.* § 7241(a)(4)–(6) (outlining the management responsibility for establishing and maintaining internal controls which will ensure that material information relating to the issuer and its consolidated subsidiaries is made known to the signing officers; and that such information is to be disclosed to the issuer's auditors and the audit committee of the board of directors, including whether there have been significant changes in the internal controls. This part of §302 of the Sarbanes-Oxley Act will not be analyzed in much depth in this note.)

61. 15 U.S.C.A. § 7241(b) (2002); The impact of the Act on issuers with foreign incorporations is an interesting question worthy of further discussion but will not be addressed in this note.

62. *Id.* § 7241.

63. *Id.* § 7241(a).

64. *Id.* § 7241(b).

II. SEC'S FINAL RULE "CERTIFICATION OF DISCLOSURE IN COMPANIES' QUARTERLY AND ANNUAL REPORTS."[65]

A. THE SEC ISSUES GUIDANCE AS TO THE STANDARD FOR MATERIALITY IN CEO CERTIFICATION.

The Securities and Exchange Commission was given the responsibility for issuing final rules, under the Sarbanes-Oxley Act, pertaining to corporate officers responsibilities in certification of financial reports.[66] In issuing of final rules of CEO certification the SEC made statements concerning the "material accuracy" and "completeness" standards of periodic reports covered by section 302 of the Act.[67] According to the SEC's "Final Rule: Certification of Disclosure in Companies' Quarterly and Annual Reports", the standard for material accuracy and completeness of financial reports "mirrors the existing statutory disclosure standards for "material" accuracy and completeness of information contained in reports."[68] When making this statement, that the standards of "material" accuracy "mirror" existing standards, the SEC specifically referenced four sources of authority.[69] The SEC first referenced Rules 10b–5(b)[70] and 12b–20[71] of the Exchange Act of 1934 as a guide for what the existing standards were.[72] Besides explicit reference to Rules 10b–5(b) and 12b–20, the SEC also referred to the two leading cases on materiality standards in financial reporting, TSC Industries, Inc. v. Northway, Inc.[73] and Basic, Inc. v. Levinson.[74] The standards for material accuracy in Rule 10b–5(b) declare it to be:

> "unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, . . .
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, . . ."[75]

In order to understand the requirements for "material fact" in 10b–5(b)[76] the SEC also referenced Rule 12b–20 of the 1934 Act.[77] It requires that "in addi-

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65. Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35.
66. 15 U.S.C.A. § 7241(a).
67. "Content of Certification," SEC Release Nos. 33–8124, 34–46427, § II(B)(3).
68. *Id.*
69. *Id.*
70. 17 C.F.R. § 230.10b–5(b).
71. *Id.* § 240.12b–20.
72. Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35, at § II(B)(3).
73. 426 U.S. 438 (1976).
74. 485 U.S. at 224 (1988).
75. 17 C.F.R. § 240.10b–5(b) (emphasis added).
76. *Id.*
77. Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35.

tion to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statement, in light of the circumstances under which they are made not misleading."[78]

The term "material" in both Rule 10b–5(b) and Rule 12b–20 is defined in Rule 12b–2 of the Securities Exchange Act of 1934.[79] The term "material, when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to buy or sell the securities registered."[80] In making explicit reference to Rules 10b–5(b) and 12b–20, and the requirements for materiality, the SEC made note of two cases, which gave guidance as to what a "reasonable investor would attach importance in determining whether to buy or sell the securities registered."[81] The SEC's reference to TSC Industries and Basic, Inc. help to shape the limits of what types of information will be considered material because there "is a substantial likelihood that a reasonable investor would attach importance" to it.[82]

B. "MATERIAL" ACCURACY AFTER TSC INDUSTRIES, INC. V. NORTHWAY, INC.[83]

The SEC first referenced TSC Industries, Inc. v. Northway, Inc. in its final rule on certification of disclosure in company quarterly and annual reports, in relation to material accuracy and completeness of periodic reports.[84] In TSC Industries the Supreme Court considered the case of an acquisition of petitioner corporation TSC Industries (hereinafter TSC) by the petitioner corporation National Industries (hereinafter National).[85] Once National bought the voting shares, the founder and his family resigned from TSC's board of directors, and National had 5 of its nominees placed on TSC's board of directors.[86] The board of directors approved a proposal to liquidate and sell all TSC assets to National through an exchange of TSC common and preferred stock for National pre-

78. 17 C.F.R. § 240.12b-20.

79. *Id.* § 240.12b-2.

80. *Id.* (emphasis added).

81. *Id.*; Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35 (referencing *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988); *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976)).

82. 17 C.F.R. § 240.12b–2.

83. TSC Industries, 426 U.S. at 438.

84. Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35.

85. TSC Industries, 426 U.S. at 438 (National acquired TSC Industries by purchasing 34% of TSC's voting securities from the corporation's founder and principle shareholder and his family.)

86. *Id.*

ferred stock and warrants to purchase National common stock.[87] TSC and National issued a successful joint proxy statement to shareholders and recommended that the shareholders approve the proposal, resulting in TSC's liquidation as the exchange of shares took effect.[88] Respondent, Northway, was a TSC shareholder who brought action for damages, claiming that the joint proxy statement was incomplete and material misleading because it omitted material facts about National's control of TSC's board of directors, and about the "favorability" of the proposal to owners of TSC stock.[89]

Justice Marshall's unanimous opinion found the issue of materiality "a mixed question of law and fact, involving as it does the application of a legal standard to a particular set of facts."[90] The court found the question of materiality "an objective one, involving the significance of an omitted or misrepresented fact to a reasonable investor."[91] By framing the question in this manner the Court rejected the theory "that material facts are 'all facts which a reasonable shareholder might consider important'"[92] because it would set too low a threshold for liability.[93] Rather, the Court stated the general standard of materiality as follows: "An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote."[94]

The Court did not require proof that the omitted fact would have caused a reasonable investor to change his vote, but a showing of "a substantial likelihood" that the omission "would have assumed actual significance in the deliberations of the reasonable shareholder."[95] Thus, "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information

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87. TSC Industries, 426 U.S. at 438; *See also*, "warrant" "2. A document conferring authority, esp. to pay or receive money." BLACK'S LAW DICTIONARY 1580 (7th ed. 1999).

88. TSC Industries, 426 U.S. at 438 (1976).

89. *Id.*

90. *Id.* at 450 (The court confirmed an earlier ruling when it stated that the issue of materiality may only be resolved as a matter of law when "the established omissions are "so obviously important to an investor, that reasonable minds cannot differ on the question of materiality;" *quoting* Johns Hopkins University v. Hutton, 422 F.2d 1124, 1129 (C.A.4 1970)).

91. TSC Industries, 426 U.S. at 445.

92. *Id.* (quoting and rejecting the language used in the Court of Appeals for this matter, Northway, Inc. v. TSC Industries, Inc., 512 F.2d. 324, 330).

93. *Id.* (*aff'g* Gerstle v. Gamble-Skogmo, Inc., 478 F.2d 1281, 1301–02 (C.A.2 1973); Smallwood v. Pearl Brewing Co., 489 F.2d 579, 603–04 (C.A.5 1974)).

94. *Id.* at 449 (emphasis added; note the Court in *TSC Industries* was dealing specifically with what constituted a material fact in terms of Rule 14a–9 of the Securities Exchange Act of 1934, but as the SEC pointed to this case in issuing its final rule on Certification of Disclosure in Companies' Quarterly and Annual Reports, SEC Release No. 33–8124, 34–46427, it is helpful in this case to determine what the standard of materiality is for CEO/CFO certification).

95. *Id.* at 449.

made available."[96] The Court defined what was to be considered material information by focusing on what individual "reasonable investors" would deem important to their own decisions, rather than a blanket rule of what types of information is to be considered material.[97] The Court applied this standard to Northway's claims and rejected both of them.[98]

The first claim was that National's control over TSC was not made clear at the time of proxy solicitation, was based on the fact that the proxy statement did not state that National's President and executive Vice-President held positions on TSC's board.[99] The Court disagreed and found that these omissions, did not warrant summary judgment because the proxy statement clearly disclosed that National owned 34% of TSC's outstanding shares, and that 5 of 10 directors were National nominees with disclosure of those director's positions.[100] Thus, the Court found a real issue of whether the omission of other facts had rendered the proxy statement "materially misleading as a matter of law."[101] This interpretation of materiality suggests that for an investor to claim that a statement was materially misleading the investor must show more then that they could not understand the accurate information that was actually presented.

Northway's second claim stated that failure to disclose certain facts, "rendered the proxy statement deficient it its presentation of the favorability of the terms of the proposed transaction to TSC shareholders."[102] One of the omitted facts Northway claimed that made the statement deficient as to its favorability to shareholders was that an investment-banking firm had issued a letter with "bad news" concerning the fairness of the transaction towards TSC shareholders, which was not disclosed in the proxy statement.[103] The letter dealt with the value of warrants that National would be issuing in its acquisition of TSC, and the price fluctuation as more warrants were issued into the market.[104] The

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96. TSC Industries, 426 U.S. at 449; (using this phrase the court recognized that it was giving content to a rule promulgated by the SEC; *see* Rules 14a–3 and 14a–9, 17 C.F.R. §§ 240.14a–3, 240.14a–9; *cf., Ernst & Ernst v. Hochfelder*, 425 U.S. 185, at 212–14).

97. TSC Industries, 426 U.S. at 449.

98. *Id.* at 463.

99. *Id.* at 451; Northway further argued that because the proxy statement failed to state that both TSC and National had filed reports, as required by the SEC, that indicated that National "may be deemed to be a 'parent' of TSC as that term is defined in the Rules and Regulations under the Securities Act of 1933," there had been an omission of material fact.

100. *Id.* at 452–53.

101. TSC Industries, 426 U.S. at 452–53.

102. *Id.* at 454.

103. *Id.* at 454–62.

104. *Id.* at 457; The terms of the proposed securities exchange to TSC were said in the proxy statement to represent a "substantial premium over the current market values represented by the securities being offered to TSC stockholders. The value placed on the warrants to buy National stock was said to be $5.25 per warrant. Two weeks after the opinion, a representative of the investment bank sent a letter to National stating that if more warrants were issued, as required by the proposal in the proxy solicitation, the value of outstanding warrants would be lowered to $3.50 per warrant. This difference would

Court found that existence of this letter did not constitute an omission of a material fact as a matter of law, because the fact that the value of the warrants would drop once more came to the market had been previously disclosed in the initial opinion.[105] Furthermore, the potential for a "substantial premium" was just one of several factors considered in the favorable opinion.[106] The Court stated that it would not assume that a TSC shareholder would only focus on the "bottom line" of the investment bank's opinion "to the exclusion of the considerations that produced it."[107] This interpretation of materiality suggests that an investor must take into account not only the summary of the opinions contained within the corporation's proxy statements but also must account for the underlying assumptions that produced that "bottom line."[108]

C. THE IMPORTANCE OF TSC, INDUSTRIES TO CEO/CFO CERTIFICATIONS.

The portion of the TSC Industries, Inc. case that has the most bearing on what is to be deemed material for CEO/CFO certification is the Court's decision to use a standard of materiality where "an omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote,"[109] was adopted as opposed to a "standard of materiality [that] is unnecessarily low."[110] The Court warned against setting a standard that was too low "not only may the corporation and its management be subjected to liability for insignificant omissions and misstatements," but that management's fear of liability "may cause it simply to bury the shareholders in an avalanche of trivial information a result that is hardly conducive to informed decisionmaking."[111] It is important to note that in contemplating the standard for materiality the Court recognized that a balance was required between meaningful disclosure, which required investors to work to evaluate meaning, and a flood of documents, which would be difficult to put into any context.

In order to apply the TSC, Industries standard of materiality to CEO/CFO certifications it seems that the certifying executive must also perform a balancing test in deciding the scope and the volume of the information contained in periodic reports. This balance requires the certifying executive to consider what information a "reasonable investor" in their company would consider important.[112] TSC, Industries also suggests that the "reasonable investor" has some

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lower the TSC shareholder's premium from 27% to 12% for TSC preferred stock and from 2% to 22% for TSC common stock.

105. TSC Industries, 426 U.S. at 457–58.
106. *Id.* at 457–58.
107. *Id.* at 458.
108. *Id.*
109. *Id.* at 449 (emphasis added).
110. TSC Industries, 426 U.S. at 448.
111. *Id.* at 448–49.
112. *Id.* at 449.

duties to do something with the disclosed information.[113] In rejecting National's two claims, as a matter of law, the TSC, Industries Court stated that a material omission would not automatically be found if the alleged omission was "viewed against the disclosures contained in the proxy statement"[114] to be immaterial, or the statement required the investor to evaluate "the considerations that produced It."[115] The reality is that no quarterly or annual report can include every internal document that when into the creation of the company's issued statement, it would be impractical and would be the "avalanche of trivial information" the TSC, Industries Court feared.[116] The standard of materiality that was recognized in TSC, Industries also recognized that investors have a duty to evaluate the information that is presented.[117] The TSC, Industries standard for materiality suggests that investors will not be able to invest blindly in corporations, whose underlying economics they don't understand, and then bring an action under the CEO certification requirements, when the investment goes sour.

D. APPLICATION TO RULE 10B–5 ACTIONS, BASIC, INC. V. LEVINSON[118]

Twelve years after TSC Industries the Supreme Court dealt with the standards for materiality as it applies to §10(b) and Rule 10b–5 actions in Basic Inc. v. Levinson.[119] Like TSC Industries, the case focused on a merger between two companies, Combustion Engineering, Inc. and Basic Incorporated.[120] During the two years between the two firms' first discussions about the possible merger and the suspension of trading in Basic's stock just prior to the merger announcement, Basic made three public statements denying any merger negotiations were taking place or any knowledge of a reason for heavy trading in Basic's stock.[121] A suit was brought by a class of former shareholders of Basic, claiming injury by selling stock at "artificially depressed" prices, in reliance on Basic's misrepresentations thus violating § 10(b) and Rule 10b–5 of the Securities Exchange Act of 1934.[122]

Justice Blackmun, writing for the majority, expressly adopted the TSC Industries standard of materiality for § 10(b) and Rule 10b–5 cases.[123] The Court characterized the merger negotiations as an event which was "contingent or

113. *Id.* at 452–53, 458.
114. TSC Industries, 426 U.S. at 452
115. *Id.* at 458.
116. *Id.*, 426 U.S. at 448–49.
117. *Id.* at 452–53.
118. *Basic, Inc v. Levinson*, 485 U.S. 224 (1988).
119. *Id.*
120. *Id.* at 224.
121. *Id.*
122. *Id.*
123. Basic, 485 U.S. at 232 (omitted fact is material if there is substantial likelihood that its disclosure would have been considered significant by reasonable investor).

speculative in nature," making it "difficult to ascertain whether the "reasonable investor" would have considered the omitted information significant at the time."[124] In trying to formulate a test for what needs to be disclosed in such merger negotiations the Court rejected two tests before settling on a "fraud-on-the-market" theory.[125]

In rejecting the first proposed test the Court stressed that the use of materiality standards was not to paint investors as having a "child-like simplicity, an inability to grasp the probabilistic significance of negotiations"[126] but instead to filter "useless information that a reasonable investor would not consider significant."[127] In rejecting the second proposed test of materiality the Court held that in order to bring a successful Rule 10b–5 claim a plaintiff "must show that the statement were misleading as to a material fact," and that "[i]t is not enough that a statement is false or incomplete, if the misrepresented fact is otherwise insignificant."[128] Instead the Court clarified that the inquiry should be a "fact-specific" depending "on the significance the reasonable investor would place on the withheld or misrepresented information."[129] Note that in rejecting the two proposed standards the Court emphasized that the investor was presumed to have the ability to grasp the concepts involved in financial disclosures,[130] and that plaintiffs had to show that statements made were misleading and not just incorrect.[131]

Once the standard for materiality was announced the Court stated that it was permissible for courts to allow a rebuttable presumption of reliance, by the plaintiffs in a Rule 10b–5 action, on the statements made denying merger talks,

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124. *Id.*

125. Basic, 485 U.S. at 225; The Court first rejected an "agreement-in-principle" test; a bright line rule, which said that "preliminary merger discussions do not become material until "agreement-in-principle" as to the price and structure of the transaction has been reached between the would-be merger partners." The Court rejected this theory because it would make all information concerning negotiations prior to any agreement-in-principle immaterial and able to be withheld or misrepresented with no consequence as to a Rule 10b-5 violation. The second test the Court rejected was the Sixth Circuit's formulation that when a publicly traded company makes an affirmative denial that "no negotiations" are taking place and that it "knows of 'no reason for the stock's activity,'" information about continuing merger discussions becomes material "by virtue of the statement denying their existence"(rejecting the test of *Levinson v. Basic, Inc.*, 786 F.2d 741 (C.A.6 (Ohio)).

126. *Id.* at 234 (*quoting Flamm v. Eberstadt*, 814 F.2d 1169, 1175 (1987).

127. *Id.* (*citing TSC Industries*).

128. *Id.* at 238.

129. *Id.* at 240; In clarifying this standard the court also announced that this standard of materiality would not vary depending on who brought the action; and noted that "'[S]cienter is an element of a violation of §10(b) and Rule 10b–5, regardless of the identity of the plaintiff or the nature of the relief sought.'" (quoting *Aaron v. SEC*, 446 U.S. 680, 691(1980)).

130. Basic, 485 U.S. at 234.

131. *Id.* at 238.

based on a "fraud-on-the-market" theory.[132] The Court defined the fraud on the market theory as:

> "based on the hypothesis that, in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business . . . Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements . . . The causal connection between the defendant's fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations."[133]

The Court reasoned that in well-developed securities markets, as exists in the United States, "the price of shares traded on well-developed markets reflects all publicly available information, and hence, any material misrepresentations."[134] The Court noted that any evidence that "severs the link between the alleged misrepresentation and either the price received (or paid) by the plaintiff, or his decision to trade at a fair market price, will be sufficient to rebut the presumption of reliance."[135] Thus if "market makers" knew the truth about the value of the stock, and any alleged misrepresentation was not reflected in the market price, the causal connection between the alleged misrepresentation and the presumption of reliance will be severed.[136] It is important to note that the Court's use of the "fraud-on-the-market" presumes that all information that is in the market will be incorporated into a stock's price, even if the individual investor did not or could not understand all the information in the market.[137] Thus investor's decision to trade at the "fair market price" when they based their decision on one materially incorrect statement will be enough to rebut a presumption of reliance.[138]

E. THE IMPORTANCE OF BASIC, INC. TO CEO/CFO CERTIFICATIONS

Basic, Inc. illustrates that the Supreme Court has recognized that today's securities markets are highly intergraded and represent open flows of information.[139] The Court found it "hard to imagine that there ever is a buyer or seller who does not rely on market integrity."[140] When the Court recognizes that no

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132. *Id.* at 250; Note, that the Court also clearly stated that reliance is an element of a Rule 10b-5 cause of action, *Id.* at 243.) (In a separate opinion Justice White, joined by Justice O'Connor, disagreed with the application of the "fraud-on-the-market" theory. *Id.* at 250–63).

133. Basic, 485 U.S. at 241–42 (*quoting Peil v. Speiser*, 806 F.2d 1154, 1160–61(C.A.3 1986)).

134. *Id.* at 246.

135. *Id.* at 248.

136. *Id.* at 248.

137. *Id.* at 246.

138. Basic, 485 U.S. at 248.

139. *Id.* at 246 (noting that "Recent empirical studies have tended to confirm Congress' premise that the market price of shares traded on well-developed markets reflects all publicly available information, and, hence, any material misrepresentations).

140. *Id.* at 246–47.

investor makes their investment decisions within a vacuum it also gives tacit approval of the theory that investors do not just rely on the public statements of the companies they invest in but also rely on how the rest of the market has interpreted those statements. So while section 302 of the Sarbanes-Oxley Act requires CEOs and CFOs to certify that "the report does not contain any untrue statement of a material fact or omit to state a material fact,"[141] the cases the SEC uses as illustration show that the standard of materiality is not any different after the passing of the Sarbanes-Oxley Act then it was prior to its passing.[142] Under this familiar standard of materiality it is not enough for an investor to show that a particular fact was misstated or omitted if the total market took into account the existence of that fact and incorporated it into the market price of the stock.[143]

Extrapolating the standard of materiality from TSC Industries and Basic, Inc. to apply to CEO certification under the Sarbanes-Oxley Act, it seems that the CEO must only certify that the reports contain all the information that "a reasonable shareholder would consider. . .significan[t] in [their] deliberations."[144] Thus, the question of whether a specific certification failed to meet the standard of materiality would require a case-by-case assessment by the trier of fact as to whether the statement contained all the information a "reasonable shareholder would consider significant."[145] Under this standard every misstatement in a certified report would not automatically rise to the level of a failure to include all material facts.[146]

Even assuming that some misrepresentation had been made, and that an action under section 302 could prove both scienter on the part of the certifying official and reliance on the part of the individual shareholder, the accused certifying official could rebut that reliance if they could show that the market had already accounted for the misstatement.[147] This suggests that a reporting issuer could present their financial condition in such a way that the "reasonable investor" might not fully comprehend the information, and therefore make a uni-

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141. 15 U.S.C.A. § 7241(a)(2) (2002); *See also,* John J. Falvey Jr. and Matthew A. Wolfman, *The Criminal Provisions of Sarbanes-Oxley: A Tale of Sound and Fury?*, 8 No. 10 ANDREWS SEC. LITIG. & REG. REP. 17 (2002) (noting that "many criminal practitioners view the new provisions and get-tough rhetoric as little more than sound and fury signifying nothing).

142. Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35, at § II(B)(3).

143. Basic, 485 U.S. at 246.

144. TSC Industries, 426 U.S. at 449; Acknowledging that the question of what a "reasonable shareholder" would consider material requires "delicate assessments of the inferences a 'reasonable shareholder' would draw from a given set of facts and the significance of those inferences to him." *Id.* at 450.

145. *Id.* at 450.

146. *Id.* at 448 (rejecting setting the standard for materiality too low not only to avoid assigning liability for insignificant omissions but also to avoid encouraging management from releasing so much information of a trivial nature that it is of no value to making an informed decision.)

147. Basic, 485 U.S. at 248–49.

formed decision, but escape liability because the market had fully accounted for this misstatement.[148] In returning to our hypothetical, Endrun might illustrate how this could happen.

III. HOW ENDRUN'S CEO COULD ESCAPE LIABILITY FOR CERTIFICATION OF FINANCIAL STATEMENTS UNDER THE SEC'S STANDARD OF MATERIALITY.

Returning to our hypothetical, it seems that the same collapse would have occurred even if the CEO certification requirements of the Sarbanes-Oxley Act had been in place. It also seems that a certifying official could escape liability under section 302 of the Act. Even if Endrun's financial reports presented their complete financial condition, including all relevant cash flows and operations in accordance with appropriate accounting practices, the same collapse could easily have happened because the average investor could not understand the disclosures.[149]

As stated earlier, by Endrun trading complex securities and entering into partnerships to manage risk and debt, took advantage of a completely legal method of accounting; mark to market accounting.[150] The problem with mark to market accounting is that, because the corporation is reporting future cash flows through current quarterly reports, the reported earnings fail to match actual cash flow, which can only work so long as the future earnings eventually show up.[151] Endrun was making a bet that their future stock price would continue to climb and it would be able to cover any losses that had been moved to their special purpose corporations, thus turning the company into "nothing so much as a hedge fund."[152]

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148. *Id.*

149. Certification of Disclosure in Companies' Quarterly and Annual Reports, *supra* note 35, at § II(B)(3); The SEC defined a "fair presentation" of an issuer's financial condition as, "results of operations and cash flows encompasses the selection of appropriate accounting policies, proper application of appropriate accounting policies, disclosure of financial information that is informative and reasonably reflects the underlying transactions and events and the inclusion of any additional disclosure necessary to provide investors with a materially accurate and complete picture of an issuer's financial condition, results of operations and cash flows." *Id.*

150. *See*, McLean, *supra* note 1, at 58 (noting Enron's use of mark to market accounting and its acceptability).

151. *Id.*

152. *Id.* (noting that Enron's business model seemed to resemble a hedge fund); *See* "hedge fund" which is defined as "A specialized investment group- usu. organized as a limited partnership or offshore investment company- that offers the possibility of high returns through risky techniques such as selling short or buying derivatives. Most hedge funds are not registered with the SEC and are therefore restricted in marketing their services to the public." BLACK'S LAW DICTIONARY 727 (7th ed. 1999). Hedge funds are not required to register under federal securities laws, generally relying on Sections 3(c)(1) or 3(c)(7) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(c)(1) and (c)(7)), and on Section 4(2) of the Securities Act of 1933 (15 U.S.C.A. 77d(2)). Because Enron acted in many ways like a hedge fund as opposed to a standard publicly traded company it could be argued that the SEC

If Endrun's business model was a hedge fund, then thousands of average investors, who would not normally have access to such an investment product, were involved in something the SEC normally considers too complex for them to invest in.[153] Potentially very complex financial disclosures would not be materially deficient under the Basic, Inc. standard of materiality, if the market could be shown to have received the information and factored it into the price.[154] The same complex disclosures that shield against liability would also seem to "bury the shareholders" in information that was not "conducive to informed decisionmaking."[155] The employment of this standard of materiality creates the potential for a CEO to shield himself from liability by showing that market makers had factored the correct information into the price, even if individual investors had not.[156]

Under the materiality standard of CEO/CFO certification adopted by the SEC it seems like Endrun's CEO and CFO would have two possible ways to certify their financial statements and avoid liability. The first option would be to flood the statement with a full accounting of each of the special purpose entities' hedging activities and make each financial report a mirror of all of the corporation's trading in derivatives, leaving it up to the reader to figure out the full meaning. This method would be of little value to the average individual investor, who is not a financial expert, and would realize the fear of the Court in TSC, Industries; "an avalanche of trivial information" that a reasonable shareholder would probably not consider in deciding how to vote.[157] If the statement

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should have required that Enron meet the "qualified purchaser" requirements for a hedge fund, but this will not be addressed in this note.).

153. A hedge fund is not usually required to register because they normally only accept financially sophisticated investors and do not offer their securities publicly, thus they fall under the definition of selling to "qualified purchasers" as defined in section 2(a)(51) of the Investment Company Act (15 U.S.C. 80a–2 (51)(A)). Note the standards for who can invest in a hedge fund and who is the "reasonable investor" that the securities laws are meant to protect are two completely different standards.

154. For example, if Endrun reported a total gross profits of x minus total gross liabilities of y (with z liabilities moved to special purpose partnerships a, b, c, d, for shares of Endrun stock) for a total net profit of e the "reasonable shareholder" might not fully understand that the liabilities would eventually return to Endrun's balance sheet if the stock price did not continue to climb. In this sense Endrun's statement would omit to explain every detail of how liabilities would be managed by corporation that Endrun controlled but the CEO could escape liability for certification if the total market was shown to have "already accounted for the misstatement." Basic, 485 U.S. at 248–49. In this way the company could be fully disclosing the results of its business operation, but the "reasonable investor" would still not comprehend the results. *See e.g.*, McLean, *supra* note 1, at 58; citing David Fleischer, an analyst who followed Enron for Goldman Sachs, as one of the many "bulls" who could not understand Enron's accounting but were happy to go along with the reports because the company reported consistent earnings. Note that in the case of Enron, there is substantial evidence that the results of business operations were not fully disclosed, especially the use of special purpose entities, but the argument made here is not that fraudulent disclosure will go unpunished. Instead, the point is that inclusion of all material disclosures does not guarantee that the "reasonable investor" understands the disclosure.

155. TSC Industries, 426 U.S. at 448–49.

156. Basic, 485 U.S. at 248–49.

157. TSC Industries, 426 U.S. at 458–59.

also included a report of previous and projected earnings, it is more likely that individual investors would simply rely on the "bottom line" of the projections, without evaluating the reasoning that produced that result.[158] Any claim under the certification requirements of section 302 of the Act could be defended by showing that a full accounting was made but the investor was not sophisticated enough to understand it.

The second option the CEO and CFO would have in certifying would be to make a blanket statement about the inherent risk of the business of the corporation and leave it up to investors to cobble together their own picture of what was happening at the company. For example the management discussion and analysis could read as follows;

> Endrun trades futures derivatives as part of its business, and futures derivatives are an inherently risky investment. Endrun manages its exposure to risk in these products by entering into hedging agreements with a number of special purpose partnerships. Members of Endrun's executive committee manage these special purpose partnerships. As compensation for taking the risk of trading derivatives, Endrun gives each special purpose partnership shares of Endrun stock. The future stability of these partnerships depends on the value of Endrun stock.

Included in the statement would be the names of Endrun executives who also manage the special purpose entities. A full report of cash flows from each special partnership could also be included. As a result each reader would have to reason for themselves that Endrun was keeping debt off its books by using wholly owned corporations to execute hedging trades. This result would not provide individual investors with the whole picture unless they had the financial acumen to piece together the picture. It could also fail to give investment professionals all the necessary information to make informed recommendations to their clients. Under the Basic, Inc. standard of materiality the SEC relies on, the CEO could still escape liability for incomplete statements if it could not be shown that the statements were "misleading as to a material fact."[159]

Comparing this hypothetical with the facts of TSC Industries, it seems that Endrun's use of partnerships controlled by Endrun executives would not automatically create liability for material omissions as long as the financial statements stated the executives and their positions.[160] The net effect of this

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158. *Id.*

159. Basic, 485 U.S. at 238.

160. TSC Industries, 426 U.S. at 450. The Court in *TSC Industries* found that just because the proxy statement did not clearly state that National executives were on TSC's board of directors, liability would not be assumed if the same information could have been understood "when viewed against the disclosures in the proxy statement." *Id.* at 452. Likewise, if Endrun's financial statements did not clearly state that it controlled the special purpose corporations, liability would not be assumed if it could be shown that the statements clearly disclosed the names and positions of Endrun executives who controlled the special entities.

hypothetical appears to be that a corporation set up very similarly to Enron could have transacted business in the same way, had the same earnings performance, and fooled the same Wall Street professionals. If certification requirements had been in place the results of the collapse would have been the same, and the Act would not provide the protection to investors that it was meant to have. Even if the Act had been in place, there seems to be no incentive for CEO's to make financial statements less complex for the "reasonable shareholder."[161]

IV. AN ALTERNATIVE TO THE CURRENT DEFINITION OF MATERIALITY

In the wake of Basic, Inc. the Supreme Court held that the existence of true statements within complex financial reports would not automatically shield the reports from being materially misleading.[162] The Court in Virginia Bankshares, Inc. v. Sandberg, held that if it would take a financial analyst to spot the tension between what is true and misleading then those portions that are misleading would remain materially misleading.[163] The Court found that the point of a proxy statement was "to inform, not to challenge the reader's critical wits."[164] This article's proposed alternative definition of materiality challenges the assumption that proxy statements and financial reports should be aimed at the "reasonable shareholder."[165] Instead of focusing on what a reasonable investor would attach importance to, the standard of materiality should focus on what the reasonable market maker would attach importance to in determining whether to buy or sell the securities.[166]

The current standard of materiality ties disclosure to the sophistication of the reasonable individual investor, when a majority of investors enter the equities markets through investment professionals.[167] This begs the question, why focus on what an untrained individual considers in their investment decisions when most people invest on the recommendations of professional analysts or through the management of mutual funds? The current standard of materiality that the SEC relies on in its final rules on CEO certification, focuses on "those matters

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161. TSC Industries, 426 U.S. at 450.

162. Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1097 (1990).

163. *Id.*

164. *Id.*

165. TSC Industries, 426 U.S. at 450.

166. 17 C.F.R. § 240.12b–2.

167. NEW YORK STOCK EXCHANGE, SURVEY 2000 (2000) *available at* http://www.nyse.com/marketinfo/marketinfo.html (last visited April 4, 2004) (based on the 1998 Survey of Consumer Finances, an ongoing survey conducted by the University of Michigan for the Federal Reserve Board. The New York Stock Exchange web site also provides an option for a copy of Survey 2000 to be mailed upon request. A copy is on file with the author. The report states that in 1998, in comparison to the 33.8 million shareholders who own shares of individual corporations stock directly, there were 48.5 million shareholders who had stock ownership through mutual fund. Furthermore, 75.8 million investors held stock through Individual Retirement Accounts and 401(k) plans, which hold mutual funds.).

which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to buy or sell."[168] This standard fails to consider the myriad of factors that average investors never consider but are part of the everyday considerations of investment professionals.[169]

As part of the passage of the Act the role of investment analysts was considered and regulated along with the disclosures required of reporting issuers.[170] In early 2003 the SEC promulgated rules in Regulation AC requiring certifying statement by the research analysts, in connection to research reports.[171] Analysts will be required to certify that the opinions contained within the report are their own and do not influence their compensation.[172] In passing Regulation AC the SEC noted the potential conflicts of interest that research analysts may have if their firm had investment banking or similar business with the companies the analyst covered.[173] Implicit in the SEC's regulation of investment analysts is the assumption that the public relies on the opinions of professional analysts in making their investment decisions. It follows that in regulating corporate disclosures that the standard of materiality should be integrated with the standards regulating the investment analysts who digest the value of the disclosures for the public.

By defining materiality in terms of individual investors, instead of the professional investment community, it allows for CEOs to argue that their disclosures contained all material facts when they include information on the most widely used indicators of a stocks value.[174] If the definition of materiality were instead shifted to focus on what investment analysts would consider material the standard would still meet the SEC's goal of getting accurate information into the market without obfuscating the value of the information in an "avalanche of trivial information."[175] While financial analysts would be interested in tradi-

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168. 17 C.F.R. § 240.12b–2

169. *See* SEC Publication for Investors, "Analyzing Analyst Recommendations," *available at* http://www.sec.gov/investor/pubs/analysts.htm (last visited April 4, 2004) (advising individual investors to take caution when relying on analyst recommendations).

170. *See* H.R. REP. No. 107–414, at *13–14 (2002), *supra* note 4; H.R. REP. No. 107–418, at *34 (2002), *reprinted in* 2002 WL 704333, at *34; S. REP. No. 107–205 at *32 *reprinted in* 2002 WL 1443523, at *32.

171. 17 C.F.R. § 242 (2003). Final Rule: Regulation Analyst Certification, Release Nos. 33–8193; 34–47384 (Feb. 20, 2003).

172. *Id.*

173. *Id.*

174. *See,* Kurt Eichenwald, *4 at Merrill Accused of Helping an Enron Fraud,* N. Y. TIMES, Mar. 18, 2003, at C1. (reporting that executives in the investment bank were accused of helping Enron commit fraud by setting up transactions that would artificially inflate profits.) Part of the reason Enron focused so much attention on inflating valuations and profits was the intense focus on these factors in making investment decisions. It could be argued that average investors would consider these factors material to the exclusion of the stability of the underlying economics of the corporation because they could not possibly be expected to understand the complexity of the transactions.

175. TSC Industries, 426 U.S. at 448–49.

tional factors like revenue growth and earnings, they would me more likely to ask questions about how those numbers were produced and how likely they are to continue. Rather than constantly looking at what did happen the financial analyst would demand information about what will happen. That information would flow to the reasonable investor through the advice that they already purchase form investment professionals and through the fair market price that market makers create for the stock.[176]

Adopting a standard of materiality that focuses on the informational needs of financial professionals would also serve another purpose of the Sarbanes-Oxley Act. A major concern of the drafters of the Act was the link between financial analysts of a stock and the investment banking business generated by the corporations that they followed.[177] Tying the materiality standards of CEO certification to the reasonable "research analyst" would work in conjunction with the recently passed Regulation AC.[178] CEOs would be required to certify that issuer's reporting contained "all the material facts that a research analyst would consider significant in their deliberations on whether to recommend the stock as an investment."[179] At the same time the research analyst would need to certify that they share the opinions contained in the research report and are not being compensated based on the favorability of their recommendations.[180] Integrating certification, like integrating disclosure, would aid the SEC in regulating the market efficiently by requiring all certifications be measured by the same standards. Furthermore, such integrated certification would serve the broad spectrum of investors. Those investors who do their own analysis of issuer financial disclosures would be assured access to all of the same information that professional investment analysts use. Those investors who rely on professional advice to make investment decisions would be assured that their was not collusion

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176. *See, supra* notes 130–36, for an analysis of the "fraud on the market" theory and how market makers affect the materiality of financial disclosures.

177. H.R. Rep. No. 107–414, at *18–19 (2002), *reprinted in* 2002 U.S.C.C.A.N. 542, 2002 WL 661614 (Reporting that there were concerns that some analysts that provide recommendations of equity securities work for companies that do underwriting work for the same companies. The report mentioned recommendations establishing guidelines for analysts by self regulatory agencies that was under review by the SEC); *See*, SEC Release Nos. 33–8119, 34–46301, *Proposed Rule: Regulation Analyst Certification*, (Aug. 2, 2002); *See also*, Susan Pulliam and Randall Smith, *SEC's Pitt Seeks Split of Banking, Analyst Areas*, WALL ST. J., Sept. 26, 2002, at C1; Robin Sidel, *SEC Plan Would Make Analysts Certify Their Recommendations*, WALL ST. J., Sept. 24, 2002, at C16. If the SEC is proposing to force stock analysts to certify their recommendations then it would logically flow that they should be considered in the definition of what are material disclosures in the financial statements they base their recommendations on.

178. 17 C.F.R. § 242 (2003).

179. This proposed standard would mirror the Court's language in *TSC Industries* where the standard of materiality was defined in terms of what the "reasonable shareholder would consider. . .signfican[t] in [their] deliberations." 426 U.S. at 449.

180. 17 C.F.R. § 242 (2003).

between analysts and issuers, and that their advisor was getting the necessary information to provide thoughtful advice.

CONCLUSION

The passage of the Sarbanes-Oxley Act recognized that the equity securities market had grown larger and more complex since the passage of the Securities Act of 1933 and the Securities Exchange Act of 1934. This prompted a demand for more disclosure on the part of reporting companies and CEO certification of those disclosures. Stricter regulations have prompted a range of responses, including everything from hyper-concentration on compliance to the detriment of adequate corporate practices, to challenging the Act's certification standards as unconstitutionally vague.[181] If these certifications are to have any value in protecting the investing public the standard of materiality used in evaluating these disclosures should also recognize the reality of today's securities markets and focus on the disclosure needs of financial analysts. In this way the securities laws will be better able to insure that full and adequate disclosure will get to the entire market, and hopefully prevent another financial collapse.

If Congressman Dingell is correct, and disclosure under the securities laws leaves the average investor in the woods, it makes sense to give the investor that same information as someone who knows the way out.[182]

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181. Robert Julavits, *Another Risk: Too Much Focus on Compliance*, AM. BANKER, Apr. 6, 2004, at 4 (describing how financial companies are concentrating on regulatory compliance rather than improving their management); Carrick Mollenkamp and Chad Terhune, *Scrushy Challenges Sarbanes-Oxley*, WALL ST. J., Apr. 6, 2004, at B3.

182. McLean, *supra* note 1, at 58.

The Specter of the Debt Collector and the Unchartered Domain: The Case for Treating Domain Names as Garnishable Property

VITA ZELTSER*

I. INTRODUCTION

Next to the IRS auditor there is perhaps no greater modern-day fiscal antagonist than the debt collector. He is dreaded. He is evaded. He is cursed. This loathing is largely attributable to the fact that despite an individual's or a corporation's fiscal prudence, there is virtually no possibility to be wholly insulated from the risk of falling into grave and insurmountable debt.

Even if indebtedness such as mortgages, car loans, insurance payments, and the like, is voluntarily incurred by individuals, medical expenses, tort claims, and other such unpleasantries of reality cannot be reasonably guarded against. Likewise, corporations voluntarily incur various debts associated with business operations, accounts payable, payroll, and the like, but are never completely immune from involuntary debts such as tort suit claims by the Environmental Protection Agency, and similar potential liabilities. Thus, no contemporary exorcist can ever eradicate the specter of the debt collector.

Much of the debt collectors' ill-repute stems from the legal powers with which they are vested under the state collections laws.[1] Repossession of assets, liens, attachments, and garnishments make for popular subjects of recurring nightmares of those who are unable to repay their debts, or those who anticipate financial difficulties on the horizon. It is this last curious creature of collections law–garnishments—that is of interest in this note.

Creditors who are unsuccessful in obtaining payment from their debtors voluntarily turn to collections law to enforce their claims.[2] Most of the statutory means of enforcement deal with assets to which the hapless debtor has title and of which he has possession.[3] However, garnishment is a comparatively unique remedy since it involves the seizure of property to which the debtor is entitled but which he does not currently possess.[4] Specifically, garnishment involves the seizure of property which is in the possession of a third person who either

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1. ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE LAW OF DEBTORS AND CREDITORS 45–65 (4th ed. 2001).

2. LYNN M. LOPUCKE & ELIZABETH WARREN, SECURED CREDIT: A SYSTEMS APPROACH 5 (3d ed. 2000).

3. WESTBROOK, *supra* note 1, at 45–65.

4. *Id.*

holds the property for the debtor (such as a bailee), or who is indebted to the principle debtor in some way, such as an employer who owes wages to an employee.[5]

In the context of typical assets owned by debtors, such as money or tangible property, collections law is fairly straight-forward and thus typically does not lend itself to much academic musing.[6] However, as "technology and law combine to create endlessly new forms of property"[7], creditors have tested the boundary of garnishment law, seeking to use garnishment in "new and untried ways."[8] Thus, creditors tirelessly explore the unchartered domain of collections law.

In 1999, one such creditor, Umbro International, Inc., attempted to garnish several domain names maintained by Network Solutions, Inc. in order to satisfy Umbro's judgment against the Canadian company.[9] The Supreme Court of Virginia held that domain names cannot be garnished because they are a product of a contract for services, which is not garnishable under Virginia law.[10] Two Justices disagreed in a strongly-worded dissent, arguing for a recognition of domain names as garnishable property, which is distinct and separate from the contractual aspect of a domain name.[11]

In this article, I will argue that the *Umbro* case, as well as other cases with similar holdings, was incorrectly decided and that domain names are property and should be subject to garnishment proceedings. In assessing this note, I ask the reader to bear in mind that the issue of domain names in garnishment proceedings is one of increasing importance in light of the growing centrality of the Internet to contemporary commerce and communication. The importance of this topic is further compounded by the present economic downturn, and the resulting fiscal hardships plaguing both individual and commercial debtors. Thus, it is critically important to determine whether domain names can be garnished since this question will certainly emerge with ever-greater frequency during the course of the next several years as an increasing number of domain name holders will be forced to deal with debt collections law.

In light of the current state of the law, accepted legal theory, and general policy, I will argue that creditors should be allowed to conquer this unchartered domain of domain name garnishment. The following section provides a brief overview of my principle arguments.

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5. WESTBROOK, *supra* note 1, at 82.

6. This became evident to the author of this note after a thorough search of the Index to Legal Periodicals for the past 20 years yielded only a handful of titles of published scholarly articles in the field of garnishment law.

7. WARREN, *supra* note 2, at 91.

8. *Id.*

9. Network Solutions, Inc. v. Umbro Int'l, Inc., 529 S.E.2d 80, 81 (Va. 2000).

10. *Id.* at 81.

11. *Id.* at 88–89.

II. OVERVIEW

The Virginia Supreme Court, in refusing to treat domain names as a form of intangible property,[12] acted contrary to the directive implicitly provided by Congress in 1999 in a portion of the Lanham Trademark Act entitled the Anti-cybersquatting Consumer Protection Act (ACPA).[13] The Act permits plaintiffs to file in rem actions against a domain name,[14] but only when that domain name incorporates certain types of trademarks.[15] This Act is clear evidence that Congress's unequivocal intent is to treat at least some types of domain names as property.[16] Thus, Congress's apparent willingness to treat domain names as property for purposes of trademark infringement appears to be irreconcilable with the Supreme Court of Virginia in the Umbro case, and a small number of other courts, which have declined to characterize domain names as property.[17] Since the Congressional Act wields the greatest authoritative weight, its decision on the status of a domain name as property should be determinative.[18]

Domain names which do not fall under the specific trademark types that are treated as property by Congress under the ACPA should also be found to constitute a form of property based on other grounds. Domain names – whether they incorporate trademarks or not – fall squarely within the definition of property both under Locke's[19] labor theory of property,[20] and the common law "bundle of sticks" definition of property.[21] On these grounds, domain names cannot be distinguished from other long-accepted forms of intangible property such as trademarks, copyrights, and the like.

Further, there is growing evidence that domain names are being treated as property in other aspects of the law. For example, domain names are being

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12. Network Solutions, 529 S.E.2d at 81.

13. 15 U.S.C. § 1125 (d)(2)(C) (2003).

14. *Id.*

15. Xuan-Thao N. Nguyen, *Cyperproperty and Judicial Dissonance: The Trouble with Domain Name Classification*, 10 GEO. MASON L. REV. 183, 195 (2001).

16. *Id.*

17. David Dolkas & S. Tye Menser, *Is a Domain Name Property?* Nov. 2000, *at* http://www.gcwf.com/articles/interest/interest_42.html (last visited Oct. 10, 2002 and article is on file at journal office).

18. The authoritative weight that should be attributed to Congress's decision stems from the fact that Congress held countless hearings and invoked the views of numerous experts and scholars prior to passage of the Act.

19. John Locke (1632-1704) was an English philosopher whose social and political ideas had a profound effect on 18th century thought, and on revolutionary movements in France and what became the United States. NEW WEBSTER'S DICTIONARY AND THESAURUS OF THE ENGLISH LANGUAGE 581 (1995).

20. Susan Thomas Johnson, *Internet Domain Names And Trademark Disputes: Shifting Paradigms of Intellectual Property*, 43 ARIZ. L. REV. 465, 474 (2001).

21. John Edward Cribbet, *Concepts in Transition: The Search for a New Definition of Property*, 1986 U. ILL. L. REV. 1 (1986).

recognized as collateral for secured loans,[22] and are also being incorporated into a debtor's bankruptcy estate.[23] If this is the case, it would only be logical for domain names to be subject to garnishment proceedings given that state collections remedies (of which garnishment law is a part), secured credit law, and bankruptcy law, all fundamentally address analogous legal issues and are thus guided by largely similar policies.

Finally, there are strong policy reasons for assuring that domain names are garnishable. Many domain names are extremely valuable, and some have even been sold for millions of dollars.[24] If domain names cannot be garnished and, therefore, cannot be reached by creditors, debtors have incentives to shelter their assets by purchasing domain names with known or anticipated exorbitant resale values. Such machinations can be employed as a means for debtors to render themselves judgment-proof, thus resulting in grave inequities for creditors.

III. OVERVIEW OF THE LAW OF GARNISHMENT

Garnishment is defined as a "judicial proceeding in which a creditor (or potential creditor) asks the court to order a third party who is indebted to or is bailee for the debtor to turn over to the creditor any of the debtor's property. . . held by that third party. A plaintiff initiates a garnishment action as a means of either prejudgment seizure or postjudgment collection."[25] In other words, garnishment is "a suit by a creditor against his debtor's debtor"[26] initiated in order for the creditor to collect the amount he is owed by the principal debtor. Thus, garnishment, a state law remedy, can be applied when the property of the principal debtor is in the possession of a third party, known as the garnishee, or when the third party owes money or some other debt to the principal debtor.[27]

The word "garnishment" is a derivative of the Norman French *garnir*, meaning "to warn."[28] The name is an apt one since it warns the garnishee not to return the principle debtor's property directly to him, but to pay the money or turn over the property to the garnishor – the initiator of the garnishment proceeding.[29] Failure of the garnishee to comply with this requirement can result

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22. Jonathan C. Krisko, *UCC Revised Article 9: Can Domain Names Provide Security for New Economy Businesses?*, 79 N.C. L. REV. 1178, 1179 (2001).

23. Michele Dickerson, *From Jeans to Genes: The Evolving Nature of Property of the Estate*, 15 BANKR. DEV. J. 285 (1999).

24. *See infra* for details Chapter VII(C).

25. BLACK'S LAW DICTIONARY 689 (7th ed. 1999).

26. 13A Encyclopedia of Georgia Law § 2 at 58 (1990).

27. *See* WARREN, *supra* note 2, at 81–82.

28. 38 C.J.S. *Garnishment* § 2 (1996).

29. *Id.*

in the garnishee's personal liability for the full amount of the debt owed to the garnishor.[30]

A garnishment proceeding is typically initiated when the creditor obtains a writ of garnishment.[31] This writ has the effect of attaching the debt which a third party owes to the debtor for the benefit of the creditor.[32] Garnishment is available before and after a judgment is rendered.[33] The purpose of pre-judgment garnishment is to ensure that, should a judgment be entered in favor of the plaintiff, he will be able to collect the judgment (i.e. to ensure that, among other things, the debtor does not abscond with the property), as well as to bring the property in question within the jurisdiction of the court.[34] The purpose of post-judgment garnishment is to allow the victorious plaintiff to collect his judgment.[35]

Since garnishments are governed by state law, there are slight variations among jurisdictions in the details of the statutory language. For example, the Georgia garnishment statute does not reveal on its face what types of property are subject to garnishment.[36] The language of the statute on this point is quite broad: it provides that "[a]ll property, money, or effects" of the principal debtor which are in "possession or control" of the garnishee at the required time in the chronology of the proceedings are subject to garnishment.[37] In Georgia, a test for whether the funds or property held by the third person is garnishable is whether the original defendant himself could have recovered the funds or property by suing the garnishee directly.[38] However, in Virginia, the statute pertaining to garnishment proceedings allows the creditor to act against any person who has a "liability" to the principle debtor.[39]

IV. OVERVIEW OF THE INTEREST AND DOMAIN NAMES

The Internet as it is known today was established in the 1960s by the United States Department of Defense Advanced Research Projects Agency in order to link military bases together in case of an attack.[40] Today, connection for individuals and entities wishing to search the Internet is provided by numerous non-profit, governmental, educational, and commercial services.[41] No one authority

30. *See* WARREN, *supra* note 2, at 82.
31. *Id.*
32. *Id.*
33. *Id.*
34. 6 AM. JUR. 2D *Attachment* § 19 (1999).
35. *Id.*
36. GA. CODE ANN. § 18–4–20 (2004).
37. GA. CODE ANN. § 18–4–20(c).
38. Foster v. S. Bell Tel. & Telegraph Co., 69 S.E.2d 644, 646 (1952).
39. VA. CODE ANN. § 8.01–511 (1996).
40. Johnson, *supra* note 20, at 467.
41. Richard Zaitlen & David Victor, *The New Internet Domain Name Guidelines: Still Winner-Take-All*, 13 No. 5 COMPUTER LAW. 12, 13 (1996).

or sovereign controls the Internet as a whole, and no entity owns it.[42] In fact, it is possible for other "Internets" to be created and operated by separate entities.[43]

"Communication [on the Internet] depends on the use of domain names to locate specific networks or computers which are a part of the Internet."[44] This is achieved through "a numbering system called the "Internet Protocol" (IP) [which assigns] each individual computer or network a unique numerical address."[45] "The IP addresses consist of four groups of numbers separated by decimals" and are used by computers in order to find relevant areas of the Internet.[46] For convenience for human users, each IP address corresponds with a "domain name"[47] which is comprised of an address for the particular network or computer on the Internet.[48] While the domain name can also consist of numbers, it usually consists of words or names in order to facilitate human users to remember them.[49] In sum, a domain name facilitates communication on the Internet by identifying the computers that are "hosts" of certain web sites, or compilations of information on the Internet.[50]

Until 1999, Network Solutions, Inc. (NSI) held the exclusive right to assign domain names under its contract with the National Science Foundation.[51] However, the domain name registering industry has been privatized, and now domain names can be acquired through more than 80 companies worldwide.[52]

Domain names are acquired on a first-come, first-serve basis. Currently the Internet Corporation for Assigned Names and Numbers (ICANN) is responsible for the domain name system of coordinating and assigning domain names.[53]

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42. MTV Networks v. Curry, 867 F. Supp 202, 203 (S.D.N.Y. 1994).

43. Lisa Dritsas, *Part Seven: Trademarks And The Internet: Application of Trademark Law to Internet Domain Names*, 12 J. CONTEMP. LEGAL ISSUES 499 (2001).

44. *Id.*

45. *Id.*

46. *See* Intermatic Inc. v. Toppen, 947 F. Supp. 1227, 1230 (N.D. Ill. 1996) (stating that "[i]n its most generic form, a fully qualified domain name consists of three elements." These elements are the host name, the domain name, and the top level domain, separated from one another by periods. *See also*, Michelle A. Farber, *NSI Domain Name Dispute Policy Statement In Understanding Basic Trademark Law* 451 PLI/Pat. 133, 135 (1996). The fully qualified domain name is an alphanumeric word or combination of words, letters, and symbols.

47. According to the official ICANN website, "Domain names are the familiar, easy to remember names for computers on the Internet (such as internic.net). They correspond to a series of numbers (called Internet Protocol numbers) that serve as routing addresses on the Internet. Domain names are used generally as a convenient way of locating information and reaching others on the Internet." ICANN website, *at* http://www.icann.org/general/faq1.htm (last visited on October 23, 2002 and article is on file at journal office).

48. Dritsas, *supra* note 43, at 499.

49. Farber, *supra* note 46, at 133, 136.

50. Intermatic, 947 F. Supp at 1231.

51. Smith v. Network Solutions, Inc., 135 F. Supp. 2d 1159, 1161 (N.D. Ala. 2001).

52. Nguyen, *supra* note 15, at 195.

53. Johnson, *supra* note 20, at 468.

According to the ICANN website, "[e]ach registrar has the flexibility to offer initial and renewal registrations in one-year increments, with a total registration period limit of ten years."[54] The ICANN website also states that "[d]omain names ending with .com, .net or .org can be registered through many different companies (known as "registrars") that compete with one another."[55]

A typical Internet address consists of a top level domain name (.com, .edu, .gov, .org, etc.,) and a second level domain name (yahoo, hotmail, cnn, etc.,), so that what is colloquially referred to as a "domain name" (and what will be so referred to in this note) is actually a combination of a top level domain name and a second level domain name, such as yahoo.com, or uga.edu, or whitehouse.gov. Top level domain names are the main dividing lines between entities on the Internet, while a second- level domain name may be issued only once within a top level domain name.[56] Thus, if the University of Georgia owns the second-level domain name "uga" within the top-level domain name ".edu", no other entity can possess "uga.edu" at the same time that the University of Georgia's registration for that name remains valid. Thus, unlike a trademark which can be used by different entities simultaneously so long as certain (for example, geographic) requirements are satisfied, a domain name can only be used by one entity at one time.[57] However, other entities may acquire "uga.com" or "uga.gov" or the like as long as they are not in violation of federal laws such as the Anticybersquating Laws prohibiting registration of certain types of domain names which indicate "piracy," trademark infringement, or similar types of bad faith.[58] The owner of a second-level domain, however, may use an unlimited number of higher-level domains. Thus, for example, the domain name "law.uga.edu" can exist at the same time as the domain name "library.uga.edu"[59].

The commercial value of domain names is significant because trademark owners and business persons can use their trademarks and business names as domain name addresses.[60] This makes Internet addresses more intuitive, facilitating recall of the address and enabling a user to guess an address by applying the appropriate top level domain name after the business name or trademark.[61]

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54. ICANN website, *at* http://www.icann.org/general/faq1.htm (accessed on October 23, 2002 and article is filed in journal office).

55. *Id.*

56. Gary W. Hamilton, *Trademarks on the Internet: Confusion, Collusion or Dilution?,* 4 TEX. INTELL. PROP. L.J. 1, 3 (1995); *see also,* Intermatic, 947 F.Supp. at 1230–31.

57. Johnson, *supra* note 20, at 469.

58. 15 U.S.C. § 1125(d).

59. Sally M. Abel, *Trademark Issues in Cyberspace: The Brave New Frontier* 451 PLI/Pat. 151, 154 (1996).

60. Abel, *supra* note 59, at 154.

61. Hamilton, *supra* note 56, at 3.

V. OVERVIEW OF CASE LAW ON DOMAIN NAMES

A. CASES HOLDING THAT DOMAIN NAMES ARE NOT PROPERTY

1. *Network Solutions v. Umbro*

The most frequently cited case on the issue of garnishment of domain names is *Network Solutions v. Umbro Int'l, Inc.*[62] In *Umbro*, the Supreme Court of Virginia, reversing the judgment of the circuit court, held that a domain name is a service arising from a contractual right, not property which is subject to garnishment:[63]

The case arose after Umbro, an international company that manufactures soccer clothing and equipment, obtained a default judgment of $23,489.98 and an injunction in a South Carolina District Court against both a Canadian corporation called 3263851 Canada, Inc. and a Canadian citizen who owns that corporation.[64] Umbro filed the suit because the Canadian corporation registered the Internet domain name "umbro.com" and used it to distribute material of a pornographic nature.[65] When a representative from Umbro contacted 3263851 Canada, Inc. about their use of umbro.com, the Canadian company offered to transfer the umbro.com domain name to Umbro in exchange for $50,000 to both 3263851 Canada, Inc. and an Internet charity, and also for providing a lifetime supply of Umbro products to the company president.[66] Umbro declined the offer and filed suit.[67] The district court entered a default judgment in Umbro's favor.[68] Since the Canadian company had no assets in the United States, Umbro obtained a writ of fieri facias (a lien on intangible property) and instituted a garnishment proceeding against NSI in Virginia to force the sale of defendant's remaining domain names in order to collect on the default judgment.[69]

The garnishment summons was for 38 domain names, which the Canadian company had registered with NSI.[70] According to the Virginia Supreme Court, "Umbro subsequently asked NSI to place those domain names on hold and to deposit control of them into the registry of the circuit court so that the domain names could be advertised and sold to the highest bidder."[71] In its response to the garnishment summons, NSI stated that it had no money or property belonging to the judgment debtor since all it had was the "standardized, executory

62. 529 S.E.2d at 86.
63. *Id.*
64. *Id.* at 81.
65. *Id.*
66. *Id.*
67. Network Solutions, 529 S.E.2d at 81.
68. *Id.*
69. *Id.*
70. *Id.* at 81.
71. *Id.*

service contract" or "domain name registration agreements."[72] Moreover, domain name services do not have a readily ascertainable value.[73] Thus, the writ of fieri facias does not attach to the judgment debtor's contractual rights that are dependent on unperformed conditions, such as NSI's rights to indemnification and the registrant's continuing obligation to maintain an accurate registration record.[74] The lower court held that the debtor's domain name was valuable intangible property, and thus was subject to garnishment, and ordered NSI to deposit control over the debtor's domain name registrations in the registry of the court so that the domain names could be sold by the sheriff's office.[75] NSI appealed the ruling of the lower court.[76]

On appeal, the Supreme Court of Virginia reversed the lower court's ruling and sided with Umbro in reasoning that "a domain name registrant acquires the contractual right to use a unique domain name for a specified period of time. However, the contractual right is inextricably bound to the domain name services that NSI provides. In other words, whatever contractual rights the judgment debtor has in the domain names. . . those rights do not exist separate and apart from NSI's services that make the domain names operational Internet addresses."[77] For this reason the court held that domain names are not a new form of intangible property.[78] Rather, they are a product of a contract for services, and since a contract for services is not a liability under the Virginia statute, the domain name cannot be subject to garnishment.[79]

The court expressed a fear of perpetuating a slippery slope if it were to allow domain names to be garnished, stating that, if that were the case, "practically any service would be subject to garnishment."[80] Also, the court feared opening the door to "garnishment of corporate names by serving a garnishment summons on the State Corporation Commission since the Commission registers corporate names and, in doing so, does not allow the use of indistinguishable corporate names."[81]

Two judges dissented, stating that a domain name is tangible property.[82] They argued that "[b]ecause NSI has received everything required to give the judgment debtor the exclusive right to use the domain names it registered, the contractual right, a valuable asset, is the intangible personal property in which

72. Network Solutions, 529 S.E.2d at 81-82.
73. *Id.* at 82.
74. *Id.* at 81.
75. *Id.* at 82.
76. *Id.*
77. Network Solutions, 529 S.E.2d at 86.
78. *Id.* at 83.
79. *Id.*
80. *Id.*
81. *Id.* at 87.
82. Network Solutions, 529 S.E.2d at 88.

the judgment debtor has a possessory interest. This right is a 'liability' within the meaning of [the Virginia Code section pertaining to garnishments] and is subject to garnishment."[83] Thus, the dissenting judges stated that they would side with the lower court's decision, allowing the garnishment of the domain names to go forward.[84]

Scholars criticizing the majority decision in *Umbro* note that the Supreme Court of Virginia ignored the fact that NSI had acknowledged that the right to use a domain name was a form of intangible personal property.[85] Perhaps even more importantly, the court also ignored the fact that Congress had recently passed the Anticybersquatting Consumer Protection Act, which contains an in rem remedy against domain names, further supporting the position that domain names are intangible property.[86] The Virginia Supreme Court insisted that the NSI's acknowledgement and congressional action were not essential to the outcome of the case because they do not address "the relationship between an operational Internet domain name and its attendant services provided by a registrar."[87]

Further criticism of the majority's opinion stems from its erroneous reliance on *Dorrer v. Arel*, a 1999 case from the United States District Court for the Eastern District of Virginia.[88] The *Umbro* court misinterpreted *Dorer*,[89] citing it for the proposition that "a domain name registration is the product of a contract for services between the registrar and registrant"[90] but ignoring the fact that the Dorer court acknowledged that some domain names exist even without attached goodwill, and that they are attractive and appropriate targets for judgment creditors seeking to satisfy a judgment from a debtor.[91] Moreover, the Dorer court left undecided the question of whether domain names are property or merely contract rights.[92] Thus, the Supreme Court of Virginia's reliance on the Dorer decision was misplaced, and its holding in *Network Solutions Inc. v. Umbro* was without precedent.[93]

2. *Dorer v. Arel*

In *Dorer v. Arel*, the plaintiff trademark holder obtained a default judgment against the defendant infringer for using the phrase "Write Word Publications"

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83. Network Solutions, 529 S.E.2d at 89.
84. *Id.*
85. Nguyen, *supra* note 15, at 191-92.
86. *Id.*
87. *Id., quoting* Network Solutions, Inc., 529 S.E.2d at 82.
88. Dorer v. Arel, 60 F.Supp. 2d 558, 599 (E.D. Va. 1999).
89. Nguyen, *supra* note 15, at 200-201.
90. Dorer, 60 F.Supp. 2d at 599.
91. *Id.*
92. *Id.*
93. Nguyen, *supra* note 15, at 200-01.

and the domain name "writeword.com" in the course of its business.[94] A permanent injunction and damages in the amount of $5,000 were entered in plaintiff's favor.[95] To satisfy the judgment, the plaintiff sought a writ of fieri facias to execute on the infringer's domain name.[96]

The district court noted that under Virginia law, "on motion of a judgment creditor, the clerk of the court issues a writ of fieri facias, which writ orders an appropriate officer to satisfy the judgment out of the judgment debtor's personal property."[97] The officer has the authority to sell any property of the judgment debtor and collect any debts owed the judgment creditor to which the lien applies.[98] The court observed, however, that there was no statutory provision for direct transfer of the judgment debtor's property to the judgment creditor in satisfaction of the judgment.[99] The court state that "where a third party controls the property subject to the writ, a judgment creditor typically must follow garnishment procedure under Virginia law."[100]

Thus, under *Dorer's* interpretation of Virginia law, it is unclear whether the writ of fieri facias is operative on domain names. This question was one of first impression to the court.[101] The court observed that there are several reasons to doubt that domain names should be treated as personal property subject to judgment liens.[102] Since a domain name may consist of a protected trademark, the court first looked to trademark law for guidance.[103] The court noted that trademarks are "not assets that can be freely traded apart from the goodwill to which they attached,"[104] and that "a judgment creditor may not levy upon and sell a judgment debtor's registered service mark or trademark."[105] Thus, creditors may not place a lien on trademarked domain names.[106]

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94. Dorer, 60 F.Supp. 2d at 599.
95. *Id.* at 559.
96. *Id.*
97. *Id.*
98. *Id.*
99. Dorer, 60 F. Supp. at 599.
100. *Id.*
101. *Id.* at 558.
102. *Id.* at 560.
103. *Id.*
104. Dorer, 60 F.Supp. 2d at 561.
105. *Id.* at 561.
106. *Id.*

B. CASES HOLDING THAT DOMAIN NAMES ARE PROPERTY

1. *Online Partners.com Inc. v. Atlanticnet Media Corp.*

In *Online Partners.com Inc. v. Atlanticnet Media Corp.*, the U.S. District Court for the Northern District of California held that "a domain name is intellectual property and may be attached under the law."[107]

In this case, plaintiff, Online Partners.com Inc., sued for trademark infringement, unfair competition, dilution, and constructive trust under the Lanham Act as well as California law.[108] Defended failed to respond to the complaint filed by the plaintiff, thus the court entered a default injunction against the defendant.[109] The cause of action for the suit arose out of a trademark dispute. Plaintiff was distributing information on the Internet via the domain name gay.net.[110] Defendant began using the domain name gaynet.com, which contains erotic materials and other information.[111] Plaintiff alleged, and the court confirmed, that the defendant's use of gaynet.com caused confusion for persons looking for plaintiff's web site, gay.net, and the court found this use to be in violation of federal trademark law.[112]

The court found that defendant's use of the domain name gaynet.com "unjustly enriches defendant at plaintiff's expense" and ordered that judgment should be entered in favor of plaintiff.[113] In order to satisfy the judgment, the court ordered an equitable lien over the domain name "gaynet.com" transferring the domain name to the plaintiff.[114] The court found support for its order in the proposition that "[a] domain name is intellectual property and may be attached under the law."[115] The court cited *Umbro Int'l. Inc. v 326851 Canada, Inc.*[116] for this proposition.[117] The *Network Solutions v. Umbro* case discussed above overruled *Umbro Int'l. Inc. v 326851 Canada, Inc.*; however, *Network Solutions v. Umbro* was decided three months after *Online Partners, Inc.* Nevertheless, the U.S. District Court for the Northern District of California clearly agreed with the reasoning in *Umbro Int'l. Inc. v 326851 Canada, Inc.* For this reason, I will provide an overview of *Umbro Int'l. Inc. v 326851 Canada, Inc.*, even though it was subsequently reversed by *Network Solutions, Inc. v. Umbro.*

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107. Online Partner.Com Inc. v. Atlantaicnet Media Corp., 2000 WL 101242, at *9 (N.D.Ca. Jan. 20, 2000).
108. *Id.* at *1.
109. *Id.*
110. *Id.* at *3.
111. *Id.* at *4.
112. Online Partner.Com Inc., 2000 WL 101242, at * 5.
113. *Id.* at *9.
114. *Id.* at *11.
115. *Id.* at *9.
116. Umbro Int'l, Inc. v. 3263851, Inc., 1999 WL 117760, at *9 (Va.Cir.Ct. Feb. 3, 1999).
117. Online Partner.Com Inc., 2000 WL 101242, at *9.

2. *Umbro Int'l. Inc. v 326851 Canada, Inc.*

The underlying facts of this case were discussed above in the overview of *Network Solutions v. Umbro*. The Circuit Court of Virginia, which decided *Umbro Int'l*, essentially held that domain names are subject to garnishment.[118] The court stated that "[t]here can be little question that domain names are a form of intellectual property" since they can be protected by trademark law.[119] The court further stated that the "[t]he fact that this form of intellectual property results from a service that NSI provides does not. . . preclude the property from garnishment any more than the service provided by the Patent Office in issuing a patent immunizes patents from garnishment."[120] Further, the court noted that not only is there a market for domain names, but also domain names have substantial value.[121] Based on this reasoning, as well as on the court's finding that the domain name Registration Agreement did not preclude the garnishment of domain names, the court held domain names to be garnishable.[122]

3. *Caesar World, Inc. v. Caesar's Palace.com*

In *Caesar World, Inc. v. Caesar's Palace.com*,[123] Caesar's World Inc. filed an in rem action against several domain names under the ACPA, alleging violations of its trademark rights, in the U.S. District Court for the Eastern District of Virginia, where the registrar, Network Solutions, was located. Network Solutions, the defendant, maintained that domain names may not be considered property because they are merely data that form part of an Internet addressing protocol.[124] The court disagreed, holding that Congress can make data "property," and the domain name registration could therefore serve independently property for the in rem proceeding contemplated by ACPA.[125]

C. SUMMATION

The preceding overview of cases dealing with the property status and garnishability of domain names evinces a lack of uniformity not only in the outcomes of these cases, but also in their underlying reasoning. Such a state of the law is understandable given the relative novelty of domain names. However, the lack of legal harmony across jurisdictions is also unfortunate and potentially problematic as it impedes both domain name holders and their potential creditors from making informed decisions about their subsequent

118. Umbro Int'l, Inc., 1999 WL 117760, at *4.
119. *Id.*
120. *Id.* (citations omitted).
121. *Id.*
122. *Id.* at 144-45.
123. 112 F.Supp. 2d 505 (E.D. Va. 2000).
124. *Id.*
125. Caesar's Palace.com, 112 F. Supp. 2d at 505.

courses of action. For this reason, the law on this topic must be elucidated and a uniform standard must be determined.

My overview of the law in this area leads me to conclude that the better reasoned position is one, which holds that domain names are property that can be garnished. My reasons for this conclusion are discussed below.

VI. DOMAIN NAMES AS PROPERTY IS THE BETTER REASONED ARGUMENT

The conclusions reached in *Umbro* and *Dorer* are in dissonance with the apparent Congressional classification of domain names as property, as well as with the standard definitions of "property." I will first address Congress's views on the nature of a domain name, and then discuss the nature of property from a theoretical vista.

A. THE ACPA TREATS DOMAIN NAMES AS PROPERTY

Congress expressed its views on whether domain names are a form of intangible property in the Anticybersquatting Consumer Protection Act (hereinafter "ACPA"), which President Bill Clinton passed into law on November 29, 1999.[126] This act amends the Trademark Act of 1976 (known as the Lanham Act), adding a new in rem cause of action to section 43 of the Lanham Act.[127] This cause of action is intended to provide a remedy for victims of bad faith domain name registration.[128]

The ACPA's intent is to discourage "cybersquatting," a practice which Congress defined to consist of "bad faith and abusive registration of distinctive marks as Internet domain names with the intent to profit from the goodwill associated with such marks."[129] Cybersquatting is problematic because cybersquatters are able to register the trademarks of an established company inexpensively, and then force the company to pay substantial sums of money to get the name back.[130] The clever cybersquatters found ways to avoid liability under existing trademark laws and "hold domain names hostage at the expense of trademark owners."[131] Congress found that such actions "threatened 'the continued growth and vitality of the Internet as a platform' for 'communication, electronic commerce, education, entertainment, and countless other yet-to-be determined uses.' "[132] Such actions are also injuries to consumer confidence in the Internet economy, and destroy the value and goodwill of brand names and

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126. Nguyen, *supra* note 15, at 207.
127. *Id.* at 207-08.
128. *Id.* at 208.
129. *See* S.REP. No. 106-140, at 4 (1999).
130. Nguyen, *supra* note 15, at 207, *cited in* Virtual Works, Inc. v. Volkswagen of Am., Inc., 238 F.3d 264, 267 (4th Cir. 2001).
131. S. REP. No. 106-140, at 8, *quoted in* Virtual Works, 238 F.3d at 267.
132. *Id.*

trademarks.[133] These concerns prompted Congress to pass the ACPA in order to remedy the "failure of traditional trademark infringement law" in the context of domain names[134]

Under the ACPA, Congress allows an in rem action to be brought against a domain name.[135] The need for such an action arises because of the unique nature of cyberspace: the Internet has no physical or geographic boundaries, so any person in any state or foreign country can register a domain name with a registrar in any state "with the click of a mouse."[136] Foreign registrants of domain names elude trademark enforcement because a potential litigant within the United States would not be able to obtain personal jurisdiction over a foreigner whose only contact with the forum was registering a domain name through a registrar located in the forum.[137] And even if jurisdiction were to be found, the registrar does not necessarily know who the registrant of a domain name is since a person registering a domain name is not required to provide his or her true name and address.[138] Thus, without an in rem provision, a company whose trademark is infringed upon by such an elusive cybersquatter is left without a remedy.[139]

The in rem procedure in the ACPA is designed to provide a remedy for the trademark owners whose marks were infringed upon by the cyber squatters over whom the trademark owners are unable to obtain personal jurisdiction, and thus are unable to file suit.[140] The ACPA allows trademark owners who can demonstrate certain elements such as bad faith on the part of the cybersquatter, the validity of the trademark right, and several other trademark-related elements to initiate an in rem action against the domain name directly.[141] The in rem action can be brought in the judicial district of the domain name registrar, registry, or other domain name authority.[142] If the trademark holder is successful in the in rem action, he can get the domain name transferred directly to the trademark owner, or obtain a cancellation or forfeiture of the domain name if he is victorious in the suit.[143] The in rem provision allows for this end to be reached economically and expediently.[144] Moreover, according to Xuan-Thao N. Nguyen,

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133. Nguyen, *supra* note 15, at 207, *citing* Hortog & Co. AS. V. SWIX.com, 136 F. Supp. 2d 531, 536 (E.D. Va. 2001).

134. *Id.* at 207, *citing* Virtual Works, 238 F.3d at 276.

135. Caesars World, Inc. v. Caesars-Palace.com, 112 F. Supp. 2d 505, 508 (E.D. Va. 2000), *citing* 15 U.S.C § 1125(d)(2)(2003).

136. Nguyen, *supra* note 15, at 208.

137. *Id.*

138. *Id.*

139. *Id.*

140. *Id.*, *citing* S. REP. NO. 106-140, at 4.

141. Nguyen, *supra* note 15, at 209.

142. *Id.*

143. *Id.* at 209-10.

144. *Id.* at 210.

"the inclusion of in rem jurisdiction provides courts with the ammunition to declare that domain names are property as prescribed by the ACPA."[145]

Since the ACPA was passed, several district courts have already held that domain names are property for purposes of an in rem action under the ACPA because Congress has declared domain names to be property.[146]

The scope of the ACPA is narrowed by the fact that only domain names that are identical or similar to distinctive trademarks are subject to in rem actions.[147] Since the court, in applying the ACPA in rem provision, transfers a domain name from the registrant to a trademark owner, "the court implies that domain names that are identical or substantially similar to distinctive trademarks are considered property."[148] As a consequence, generic or descriptive domain names are not treated as property under the ACPA because "no trademark owner could bring a successful in rem action against such domain names because the trademark owner does not have a protectable trademark."[149] This presents a problem in light of the commercial reality of generic and descriptive domain names because these are frequently the ones with the highest value.[150]

Nonetheless, the ACPA evinces clear and unequivocal congressional intent that at least some types of domain names are deemed to be a form of property. It is important to note that the domain name involved in the *Umbro* case would have fallen into the categories of domain names which the ACPA teats as property since umbro.com contained a distinctive trademark.

Even if a domain name contains a trademark which is not treated as property under the ACPA, or even if it contains no trademark at all, the domain name's status as property can be defended on other grounds, as explored below.

B. LOCKE'S LABOR THEORY OF PROPERTY AND THE BUNDLE OF RIGHTS THEORY SUPPORT A CONCLUSION THAT DOMAIN NAMES ARE PROPERTY

While the ACPA provides evidence that domain names that incorporate distinctive trademarks, or domain names which are at least substantially similar to distinctive trade marks, should be treated as a form of intangible property, an examination of the theoretical definition of property leads to the conclusion that domain names, which include generic or descriptive trademarks, or even non-trademarked terms, should also be treated as property. The two most prevalent theoretical definitions of property – the "bundle of rights" theory and Locke's

145. Nguyen, *supra* note 15, at 210.

146. *Id.* at 211-12.

147. *Id.*

148. *Id.*

149. *Id.* at 212.

150. *See* Nguyen, *supra* note 15, at 212. (For example, sex.com and business.com are some of the most valuable domain names that exist today.)

labor theory–both lead to the conclusion that domain names are a form of intangible property.[151]

John Locke theorized that the rationale for property ownership was the expenditure of one's labor.[152] Locke reasoned that a person has property in an object when he commingles his labor with that object which, presumably, was previously unclaimed by any other individual.[153] Since a person's labor belongs to him, once he adds his labor to an object which previously belonged to the common, if a second person takes this now worked-on object, that person also takes the labor which does not belong to him.[154] While this theory was developed in the realm of tangible property, the same logic comfortably extrapolates to intellectual property ownership rights.[155] According to this theory, "[j]ust as one has a right to the crops one plants, so does one have a right to the ideas one generates and the art one produces."[156] A domain names is defendable as property under Locke's labor theory[157] because, in essence, a registrar takes the domain name from the "common" - the pool of available and unclaimed domain names, and combines this domain name reduced from its state of nature (as Thomas Hobbes[158] would put it) with the labor involved in registering the domain name.

Another standard definition of property comes from the common law. The "bundle of rights" conceptualization of property dictates that property ownership is equivalent to holding a number of distinct rights in relation to a tangible object or intangible idea.[159] The "sticks in the bundle" include the right to use the property, the right to exclude others from using the property, and the right to transfer the property to another entity.[160] Under this theory, a domain name is clearly property.[161] First, a registrant of a domain name has the right to exert control over the domain name and to use it as she choose. The registrant may employ the domain name for personal use by using it to host a personal web site, or she may employ it for a business purpose by starting an Internet-based business. She may use it to endorse a political candidate, to form a discussion

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151. Johnson, *supra* note 20, at 474; *see also* Nguyen, *supra* note 15, at 190-91.

152. Johnson, *supra* note 20, at 474.

153. *Id.*

154. Johnson, *supra* note 20, at 474-75.

155. *Id.*

156. *Id.*

157. *Id.*

158. Thomas Hobbes (1588-1679) was an English philosopher who developed a political theory based on the idea that without modern society which is developed in order to ensure individual security people would exist in a state of nature marked by anarchy, where individuals' actions re motivated entirely by selfish aims. NEW WEBSTER'S DICTIONARY AND THESAURUS OF THE ENGLISH LANGUAGE 460 (1995).

159. Cribbet, *supra* note 21, at 1.

160. *Id.* at *1-2.

161. *Id.*

group, or she may simply choose not to place any contents at all on the web site corresponding with the domain name.[162] Second, a registrant of a domain name may exclude others from using the domain name. This right is inherent in the nature of the domain name system since no person or entity can have exactly the same domain name on the Internet as any other person or entity, as discussed in the above overview of domain names. Third, the registrant of a domain name has the right to transfer the domain name to another entity.[163] She can assign the domain name to others for a profit (or a loss), or sell the domain name to the highest bidder online at an online auction site.[164] Further, if she has gained ownership of the domain name through fraudulent means, she can be forced to transfer the domain name to the rightful owner.[165] If she uses the domain name in a manner that may give rise to unfair competition, she will be forced to forfeit a portion of her property right.[166] Thus, since all of the "sticks in the bundle of rights" which are associated with accepted forms of tangible and intangible property are also present in domain names, domain names should be recognized as a form of property.[167]

Thus, under both the Locke's labor theory and the "bundle of rights" theory domain names fit squarely within the accepted definitions of property, regardless of whether the domain names contain a trademark or not.

Since the intent of Congress, as well as the definitions of property, dictate that domain names are a form of intangible property, I will devote the next section to a discussion of the reasons why this form of intangible property should be made subject to garnishment proceedings.

VII. SINCE DOMAIN NAMES ARE PROPERTY, THEY SHOULD BE GARNISHABLE

Arguments from analogy as well as policy support the garnishability of domain names. Treatment of domain names by the legal cousins of garnishment law – the secured credit system and the bankruptcy system – provides great insight, by way of analogy and illustration, into how garnishment law should treat domain names. Further, basic policy reasons behind garnishment law, as well as debtor-creditor law generally, support the thesis that domain names should be subject to garnishment proceedings.

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162. Andrew Beckerman-Rodau, *Are Ideas Within the Traditional Definition of Property? A Jurisprudential Analysis*, 47 ARK. L. REV. 603, 606 (1994).

163. *Id.*

164. GreatDomains.com is an example of such online auction sites.

165. Kremen v. Cohen, 2000 WL 1811403, at *6 (N.D. Cal. Nov. 27, 2000) (ordering the defendant to transfer the domain name to the original owner).

166. *Id.*

167. Nguyen, *supra* note 15, at 190-91.

A. DOMAIN NAMES AS COLLATERAL FOR SECURED CREDITORS

In the realm of secured credit,[168] there appears to be consensus among scholars that domain names can be used as collateral to secure an indebtedness if the second-tier domain name incorporates a trademark.[169] Logic dictates that if a domain name can serve as security for a debt, then the secured party has the right to sell the domain name to satisfy the debt in case of default on the security agreement. Thus, the secured creditor will treat a domain name as he would any other tangible or intangible asset of the debtor. Since the law of secured creditors opens its arms to domain names as security-bearable assets, so to should the law of garnishments.

B. DOMAIN NAMES AS PART OF THE BANKRUPTCY ESTATE

Domain names are viewed as property of the estate in bankruptcy. Under the Bankruptcy Code,[170] a debtor's interest in intellectual property, as well as all agreements governing intellectual property rights, are included as the property of the debtor's estate along with all other types of property and contractual rights.[171] In fact, in many settings, a debtor's intellectual property interest may be the most valuable, or even the only asset the debtor owns.[172] As a policy matter, bankruptcy courts tend to protect the rights of creditors in bankruptcy proceedings and to include as many assets–or, as the case may be, to classify as many "things" within the debtor's control as assets–as possible in order to maximize the value of the bankruptcy estate, and thus to maximize the payout to creditors.[173] In fact, bankruptcy courts will go so far as to protect creditors' rights even if this involves removing assets that might hinder the debtor's ability to reorganize after the bankruptcy.[174] In light of this, and in light of the fact that during the last decade there has been an explosion of Internet-based businesses, bankruptcy trustees have been successful in arguing that a debtor's interest in a domain name is included in the bankruptcy estate.[175] The trustees have argued that an interest in the domain name is an executory contract, which can be assumed by the debtor just like other contracts.[176] Thus, bankruptcy law is also recognizing domain names as property, and treating them as such.

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168. Laws governing secured credit can be found in the Revised Article 9 of the Uniform Commercial Code. While no provision of the Revised Article 9 expressly addresses domain names as collateral for security agreements, this topic has been addressed in several scholarly articles, as discussed below.

169. Krisko, *supra* note 22, at 179 (2001) (noting domain names as collateral in secured transactions). *See also* Brent R. Cohen & Thomas D. Laure, *Acquiring and Enforcing Security Interests in Cyberspace Assets*, 10 J. BANKR. L. & PRAC. 423, 433 (2002).

170. The U.S. Bankruptcy Code can be found in Title 11 of the U.S.C.

171. Dickerson, *supra* note 23, at 285.

172. *Id.*

173. *Id.*

174. *Id.*

175. *Id.*

176. Dickerson, *supra* note 23, at 285.

C. POLICY ARGUMENTS FOR GARNISHMENT OF DOMAIN NAMES

A sub-textual policy of garnishment law is one of fairness toward the creditor: the creditor is entitled to repayment on his debt, and if this repayment does not come directly from the debtor, the creditor may seek it from third parties who have property or money which belongs to the debtor. Grounded in this logic, fundamental concepts of fairness likewise dictate that domain names should be garnished in order to allow creditors to be repaid on their debts.[177] Many domain names have a resale value which is higher than the amount of their registration fee. This situation could lead to a highly inequitable result if the debtor is allowed to retain the domain name, which could potentially have a significant market value, while his creditor cannot collect the moneys to which he is entitled.

A holding that domain names cannot be garnished leads to some unsavory and inequitable incentives for creditors who foresee financial troubles on the horizon. This theory is evinced by the practice of domain name resale. Many a domain name holder has placed his address for sale on the web. While some companies or individuals do this because they once registered the domain name but no longer need it, others purchase the domain names solely in view of reselling them later for profit. As long as this practice does not cross the line of Cybersqatting (in which case it would be subject to the wrath of the ACPC), it is perfectly legal and increasingly widespread.[178] The priciest domain name sale known to date is that of the domain name sex.com.[179] The fair market value of these magic letters is $7 million![180] The runner up in price was business.com which grossed a comparatively puny $2.5 million.[181]

A more poignant illustration of domain name registration in view of for-profit resale occurred on September 11, 2001. Within several minutes after the hijacked airplanes struck the World Trade Center in New York City and the Pentagon in Washington DC, a handful of shrewd and quick-thinking computer junkies had already registered most of the domain names which could reasonably be associated with the act of terrorism.[182] While most people around the world, after hearing the news of the terrorist attacks, ran to the nearest television or radio, several people rushed to their computer to make sure that they

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177. Evidence for this policy direction of debtor-creditor law can be found in the Bankruptcy Code (Title 11 of the U.S.C.). Many of the laws under this Code evince a clear pro-creditor policy choice on the part of the Legislature. In fact, the proposed revisions to the Bankruptcy Code, which are currently being debated in Congress, contain even more stringent anti-debtor and pro-creditor provisions than the Code that is presently in force.

178. David Levinthal, *Master of Your Domain?,* DALLAS MORNING NEWS, Apr. 4, 2004, at 8A.

179. Sabra Chartrand, *Sale: Web Address, Unused, Not Cheap*, N.Y. TIMES, Aug. 22, 2000, at C4.

180. Chartrand, *supra* note 179, at C4.

181. *Id.*

182. Harriet Ryan, *Giving Name to Tragedy: Domains are hot items in terrible times, at* www.courttv.com (last reviewed Nov. 1, 2002).

could get september11.com, septermber112001.com, usattack.com, and the like, before anyone else could get them.[183] The market value of these domain names shot up instantly from the $35 annual registration fee to several hundred, and in some cases several thousand dollars.[184] While many – if not most – of those who registered these domain names did so in view of selling them in order to donate the proceeds to benefit 9-11 victims and families, the opportunity to draw a quick profit remained nonetheless.[185]

Thus, domain names can be used as an investment. A $35 dollar registration fee can blossom into millions, as it did with sex.com.[186] Indeed, that clever registrant obtained a profit of 20,000,000%.

Since domain names clearly have value, as evident by the fact that they are re-sold, they can also be used as a means of storing capital. And if they are a not subject to garnishment, they can be used as a means of shielding wealth from creditors. If a debtor anticipates financial difficulties on the horizon, he can liquidate all of his assets which a creditor would otherwise be able to seize or levy upon and invest those assets into a domain name. This way, the only means a creditor could use to obtain those assets would be via the route of involuntary bankruptcy. However, if a debtor has too few creditors to satisfy the statutory requirements of involuntary bankruptcy, the creditor will be out of luck.[187]

Thus, if garnishment law is not extended to domain names, the purchase of a valuable or potentially valuable domain names can be the Mecca of distressed debtors, or even for prudent debtors who are not currently experiencing financial difficulties but would like to insure their continued financial stability. A domain name not subject to garnishment is the ultimate off-shore bank account.

If domain names cannot be garnished, the creditor will be able to maintain his potentially most valuable asset, enjoy its use, and employ it in the furtherance of his business (as would be the case for an Internet-based business), while the creditor would be virtually powerless to collect the money he is owed.

Furthermore, ownership of a domain name with a high market value might mislead unsecured creditors and cause them to make loans in reliance of the appearance that the debtor has valuable assets. When time comes for repayment, however, these assets cannot be reached by the creditor. In order to avoid the above-discussed highly inequitable results, domain names should be treated as garnishable property.

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183. Ryan, *supra* note 182.

184. *Id.*

185. *Id.*

186. WARREN, *supra* note 2, at 7.

187. *See* 11 U.S.C. § 303.

VIII. CONCLUSION

Domain names should be treated as garnishable property. Their status as property derives from Congressional intention in the Anticybersquatting Consumer Protection Act, which permits an in rem action to be filed against a domain name. The enactment of the ACPA reveals Congress' acceptance that at least certain classes of domain names are a form of intangible property. Furthermore, a theoretical analysis of the nature of property through the lens of traditional definitions of property also leads to the determination that domain names deserve property status. Locke's labor theory, when applied to domain names, leads to the conclusion that when a domain name is registered by an individual or a business, labor, in the form of the registration, is applied to the unregistered domain name, which is available for anyone willing to fill out the registration form.[188] Thus, the domain name is a type of intangible property of the registrant. Under the "bundle of rights" theory, domain names can also be defined as property since the holder of a domain name enjoys the right to use the domain name himself, the right to exclude others from using the same domain name, and the right to sell or convey the domain name to others.

Inquiries into analogous spheres of law lead to the conclusion that since domain names are a type of property, they should be garnishable.[189] Domain names can be used as collateral for loans, and upon failure to repay the secured creditor can seize the domain name and sell it to satisfy the outstanding debt. Further, domain names can be included in the bankruptcy estate in order to maximize the return for creditors in bankruptcy.

Finally, strong policy reasons indicate that domain names should be garnishable. Since domain names have market value, which is sometimes very high, and because they can be resold by the registrant for a profit, domain names can be used as a form of investment. If they are not made subject to garnishment proceedings, they can also be used as an effective means by which to shield assets from creditors. A creditor anticipating financial distress, or one simply wishing to insulate himself from financial distress, has a strong incentive to simply invest his lucre in domain names, thus making himself judgment-proof.

The advent of the Internet, and especially its growing popularity and centrality as a tool and means of commerce and communication during the course of the past decade, necessitates clarity in Internet-related law. Domain names, as addresses of the Internet, deserve thorough consideration not only in light of their functional importance in allowing individuals to access Internet cites, but also because of their great pecuniary worth. This worth stems largely from the fact that many domain names contain trademarks, and thus many individuals

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188. Subject to some limitations relating to top-level domain names such as .gov and .edu, among others.

189. *Id.*

will intuitively attempt to employ a familiar trademark as a second-tier domain name when entering a web address. The fact that domain names are financially valuable necessitates a clear rule defining their status as property, and thus the status on their garnishability. The rule should be that domain names should be garnishable.

Even the above elucidation of one aspect of the unchartered domain of garnishment law does not completely insulate an individual or a corporation from the ever-present threat of falling into crippling debt. However, the specter of the debt collector becomes slightly less daunting if the hapless would-be debtor is a bit more certain of the status of the law.

2004 Case Comments

Governator – Rise of the Voting Machines: *Southwest Voter Registration Education Project v. Shelley*, 344 F.3d 914; Voting Rights and the 2003 California Recall Election

I. Introduction

The right to vote is fundamental, but a federal court cannot lightly stop a state election. The Supreme Court has even allowed elections to go forward even when there was an undisputed constitutional violation.[1] The state that grants the franchise also cannot value one citizen's vote more than another citizen's.[2] *Baker v. Carr*[3] is possibly the most oft cited case for the proposition that a state's debasement of a citizen's vote is a violation of the Equal Protection Clause of the Fourteenth Amendment to the United States' Constitution.[4] We must remember that the right of suffrage can be denied just as easily by debasement or dilution of the weight of a vote as by total prohibition on free exercise of the voting franchise.[5] Thus, the equitable relief supplied by the Supreme Court in *Baker*[6] becomes important in the face of a charge of a non-explicit equal protection violation such as involved in the *Shelley* case. The Ninth Circuit in *Shelley* was called upon to decide whether the effect of different voting technology debased the minority vote to the extent that enjoining the 2003 Gubernatorial recall election was a proper remedy.

II. The Facts of *Southwest Voter v. Shelley*

At the beginning of this litigation, several *Common Cause* plaintiffs sued former Secretary of State Bill Jones, in 2002, to declare VotoMatic and Pollstar machines unconstitutional.[7] Ultimately, he decertified such machines for elections after January 1, 2006.[8] Subsequently, the parties then agreed that the old machines should be replaced before the March 2, 2004 general election, and a consent decree was approved by the District Court in the *Common Cause* case. However, the next statewide election came earlier, on October 7, 2003, because of the certification of the ballot measures to recall Governor Gray Davis. The

1. S.W. Voter Registration Educ. Project v. Shelley, 344 F.3d 914, 918 (9th Cir. 2003) (en banc) (citing Ely v. Klahr, 403 U.S. 108, 113, 115 (1971) [hereinafter Shelley II], Reynolds v. Sims, 377 U.S. 533, 555, 585 (1964)).
2. Bush v. Gore, 531 U.S. 98, 104–05 (2000).
3. 369 U.S. 186, 187 (1962).
4. *Id.*
5. Reynolds, 377 U.S. at 555.
6. Baker, 369 U.S. at 250.
7. Shelley II, 344 F.3d at 916–17.
8. *Id.*

state would now vote on whether to remove their governor from office and replace him with another candidate. Pursuant to California law, Lieutenant Governor Cruz Bustamante set that election for October 7, 2003. Propositions 53 and 54 were then added to the October 2003 election.[9]

The preparations for the recall election were already beginning when this case was filed in District Court. The plaintiffs sought a preliminary injunction to delay the election until it could be held without the use of punch-card balloting machines.[10] Furthermore, the plaintiffs argued that the machines were disproportionately present in counties containing a large amount of minority voters.[11] Forty-four percent of the state's electorate resides in counties using punch-card machines. By holding the election with punch-card machines employed in some counties and better machines in the other fifty-four percent of the state, the plaintiffs claim that the California voting scheme violates the Equal Protection Clause.[12]

The VotoMatic system contains a single punch-card with pre-scored rectangles inserted under a booklet containing candidate names and other ballot measures, it is punched by the voter with a metal stylus. When turned, the booklet exposes different rows of the punch-card.[13] There are at least three scenarios, in which a vote may not be counted: if the card is not scored correctly, the machine is worn from extensive use, or if the user does not properly punch it.[14] To make things worse, the voter cannot inspect his card for accuracy because it contains no candidate names, only numbers and punched rectangles.[15] It is alleged that these limitations and the locations of such machines causes minority votes to have a disproportionately residual error rate, meaning less votes are counted and thus affecting the minority voting franchise.[16] The Voting Rights Act claim is similar to the equal protection claim, that a greater minority population in punch-card counties denies the right to vote on the basis of race.[17] The counties in question are primarily Latino and African American in population.

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9. Shelley II, 344 F.3d at 916; The two measures originally scheduled for 2004, Propositions 53 and 54, proposed amendments to the California Constitution dealing with budget and privacy matters.

10. *Id.* at 917; Punch-card systems were alleged to be so inferior to other voting machines that they debased the value of the vote of anyone who must use them.

11. *Id.*

12. *Id.*

13. *Id.*

14. Shelley II, 344 F.3d at 882, 888–89.

15. *Id.*

16. *Id.* at 917.

17. S.W. Voter Registration Educ. Project v. Shelley, 278 F. Supp. 2d 1131, 1134 (C.D. Cal. 2003) [hereinafter Shelley I].

III. PROCEDURAL HISTORY

Plaintiffs filed suit in federal court in the Central District of California to delay the California recall election, alleging violations of the Equal Protection Clause of the Federal Constitution and Section 2 of the Voting Rights Act, 42 U.S.C. 1973 et. seq. They wanted to enjoin the election until it could be held without pre-scored punch-card balloting machines.[18] The District Court denied the plaintiffs' motion for a preliminary injunction and temporary restraining order, saying that the plaintiffs failed to prove a likelihood of success on the merits of either claim; they could not pass the 9th Circuit's *Johnson-Clear Channel-Lujan* standard for a preliminary injunction. Thus, the election preparations continued.[19] In addition, the District Court stated that it was an unusual remedy to stop an election, and that the *Common Cause* case decided the issues herein, implicated res judicata as well as created an adequate remedy that mandated decertification for 2006.[20]

On appeal, a per curiam opinion of the Ninth Circuit reversed the District Court and granted plaintiff's motion for a temporary injunction, thereby halting the recall election. That injunction was stayed to allow the plaintiffs to appeal either to an en banc panel or to the Supreme Court. Accordingly, an en banc appeal then commenced and the Ninth Circuit withdrew the first appellate judgment upon their decision to rehear the case.[21]

IV. CLAIMS

Plaintiffs' equal protection claim is that voters in counties with punch-card machines are treated differently than those in counties with superior voting machines, because their votes are either not counted or are miscounted. In other words, the minority individual required to use punch-card machines will have a "comparatively lesser chance of having their votes counted than other voters in counties with [better] technologies."[22] The thrust of the voting Rights Act claim is counties, which employ the inferior punch-card systems had greater minority populations thereby disproportionately disenfranchising and/or diluting the votes on the basis of race, in violation of Section 2 of the Voting Rights Act.[23]

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18. Shelley I, 278 F. Supp. 2d at 1133.

19. The 9th Circuit preliminary injunction test: 1) combination of likely success on the merits and possibility of irreparable harm *and* 2) serious questions are raised and the balance of hardships tips in their favor.

20. Shelley I, 278 F. Supp. 2d at 1136; The decertification was later moved to March 2004.

21. Shelley II, 344 F.3d at 917 (en banc).

22. *Id.* at 1134; The court mentions that the Supreme Court in *Bush v. Gore* strongly hinted that rational basis is the proper scrutiny level for marginally disparate voting error rate cases; thus, the government will almost never lose a case if this standard is indeed employed.

23. *Id.* at 1131; Section 2 can be found at 42 U.S.C. § 1973.

V. COURT'S ANALYSIS OF FEDERAL COMMON LAW

As much as this case is a voting rights case, it is also a review of the correct standard for a preliminary injunction in the federal courts. The court in *Shelley I* states the injunction standard succinctly:[24]

> The first part of the test offers two alternatives, the party seeking a preliminary injunction (in this case the plaintiffs) must show:
> 1) A strong likelihood of success on the merits;
> 2) The possibility of irreparable injury to the plaintiffs if relief isn't granted;
> 3) A balance of the hardships favoring the plaintiffs;
> 4) Advancement of the public interest, in certain cases.
>
> Alternatively, injunctive relief may be granted if the plaintiffs:
> 1) Demonstrate either a combination of probable success on the merits and the possibility of irreparable injury; or
> 2) That serious questions are raised and the balance of hardships tips sharply in their favor.[25]

The second factor is that the two *Johnson* alternatives are extremes on a single continuum, not two separate tests.[26] Thus, the more potential hardship to the plaintiffs, the less probability of success on the merits is required.[27] The less the likelihood of success means the plaintiff must convince the District Court of an increased public interest and a balance of hardships in their favor.[28]

The en banc court stressed deferential review, stating the District Court must make an error of law for the decision to be reversed. The court also recognized that a federal court interfering with a state election is a big deal and not to be taken lightly, in fact "the Supreme Court has allowed elections to go forward even in the face of an undisputed constitutional violation."[29] On the equal protection claim, plaintiffs had not established a clear likelihood of success on the merits; the court determined that there was no abuse of discretion and that local entities should exercise their own expertise in elections systems implementation.[30]

Bush v. Gore[31] also presented an equal protection claim in the context of a high profile exercise of the voting franchise. The Supreme Court found a violation of equal protection in the standardless manual punch-card recounts of cer-

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24. Shelley II, 344 F.3d at 893 (per curiam).
25. Johnson v. Cal. State Bd. of Accountancy, 72 F.3d 1427, 1430 (9th Cir. 1995).
26. Clear Channel Outdoor v. Los Angeles, 340 F.3d 810, 813 (9th Cir. 2003).
27. Fund for Animals v. Lujan, 962 F.2d 1391, 1400 (9th Cir. 1992).
28. Shelley II, 344 F.3d at 918 (en banc) (relying on the deferential standard of review and the fact that the per curiam panel unanimously decided that the equal protection claim had merit to show that reasonable judges can differ).
29. *Id.*
30. *Id.* (citing Bush, 531 U.S. at 109).
31. 531 U.S. 98 (2000).

tain Florida counties.[32] They said that the deficiency lies in the Florida Court's lack of guidance on how to determine voter intent for improperly punched and miscounted ballots, which has led to varying standards both across those counties involved in the recount and even within one county.[33] The parallel to *Shelley* is: different standards for voting in California; some inferior and others superior in accuracy; and it presents a credible equal protection claim. The distinguishing factor in *Shelley* was that the election was still in process, votes were still being cast, whereas in the 2000 Presidential election they had already concluded. This is the overriding reason the California court was unwilling to use equal protection to stop the 2003 recall election.[34]

The Voting Rights Act claim presented more promise for adjudication on the merits, but the en banc court could not say that there had been a strong likelihood of success by the plaintiffs.[35] In this case, the public interest would have been greatly affected if the court had intervened, which would have caused voters to recast their ballots. This was not a recourse, the court was prepared to order. Enormous resources had already been invested by the state and the people and the court was thus very reticent to interfere and decided that to do so in *Shelley* would be improper.[36]

Furthermore, the court did not want to interfere with the scheduling of the ballot initiatives 53 and 54, even though they had not been originally scheduled until 2004. The court once again reasoned that interfering with an election once it has already begun is unprecedented, and this election had commenced because absentee voters had already cast their ballots on the initiatives. Also, the court opined, ballot timing of initiatives is for the states to decide. Although the claims do implicate a public interest, the balancing done by the District Court was not an abuse of discretion.[37] It was determined that the disparate use of punch-card machines was only speculatively likely to influence the election result. Thus, the District Court did not abuse its discretion in determining that the plaintiffs' hardship will not outweigh those of the state and the citizens of California if the election were to go forward.[38] So the Ninth Circuit, en banc, dismissed the motion for injunction and the election went as planned on October 7, 2003. The electorate voted to recall Governor Gray Davis. Then Arnold

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32. Bush, 531 U.S. 98 at 105.

33. *Id.* at 106.

34. The election had already started because absentee voters had already submitted their ballots. Shelley II, 344 F.3d at 914.

35. *Id.* at 918; Plaintiff must demonstrate a causal connection between the challenged voting practice and a prohibited discriminatory result.

36. Shelley II, 344 F.3d at 919.

37. *Id.*

38. *Id.* at 920; The court felt it was necessary to look at California's interest as a whole, including the state and its citizens, in weighing the public interest portion of the preliminary injunction standard.

Schwarzenegger was elected by a large margin, making him the first governor of California to replace a recalled governor.

VI. ANALYSIS

This case was important not only as a groundbreaking example of the power of American democracy, but also as a reminder of the continuing problems of disenfranchisement by the minority voter. Luis Fraga, in his article "Latino Political Incorporation and the Voting Rights Act," argues for more active participation by Latino-elected representatives to assimilate them into the community by taking an offensive approach to convincing Anglo legislators that their "communities will also benefit from policies designed to serve minority communities" instead of "relying on white sympathizers to be moved by righteous indignation."[39] The minority franchise can thus be seen as an integral part of the success of an entire community. Because the right to vote is considered fundamental, once the state allows a group to vote, they cannot then impinge that right by making one vote less valuable than the rest.[40] As the court said in *Shelley*, there was a valid claim lying in the plaintiff's complaint, likely in the Voting Rights Act portion, but given the fact that it was unlikely to affect the election, the court could not enjoin Secretary Shelley from continuing.[41]

The one man, one vote idea, which was introduced into American jurisprudence in *Baker v. Carr*,[42] is still a viable doctrine today, and the claim of minority voters appears valid to that end, especially the claim of the Latino voter in California. At the forefront of unequal vote counting in California is the Spanish-English language barrier, which may have prevented Latinos from properly voting in the 2003 special election. It appeared that the franchise had been impaired when the punch-card system was used in the selective counties, and there was no one available to explain the rather complicated punch-card in Spanish.

VII. CONCLUSION

We must recognize that this country speaks many languages. Language assistance provisions contained in the Voting Rights Act have had minimal impact because of a lack of enforcement[43], and thus possibly the only way to even the score has been through the litigation going down the equal protection or §1973 avenues. Perhaps in the future, when the Latino population has outgrown all other groups in Southern California, as is seemingly inevitable, a *Shelley*-like claim will prevail. This may be a rare area of jurisprudence where law is actu-

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39. CONTROVERSIES IN MINORITY VOTING: THE VOTING RIGHTS ACT IN PERSPECTIVE 278-82 (Bernard Grofman & Chandler Davidson, eds., 1992).

40. Harper v. Virginia, 383 U.S. 663, 665 (1966); Bush, 531 U.S. at 105.

41. Shelley II, 344 F.3d at 918 (en banc).

42. 369 U.S. at 186.

43. U.S. COMMISSION ON CIVIL RIGHTS, THE VOTING RIGHTS ACT: UNFULFILLED GOALS 78 (1981).

ally evolving faster than technology. Undoubtedly, in the wake of cases like *Shelley* and *Bush v. Gore*, states and counties across the country will begin to replace punch-card machines with internet and computer-based voting. In California at least, punch-card voting will have been decertified for statewide elections beginning in March 2004. Even though such claims as were involved in *Common Cause* and *Shelley* are now irrelevant in California because of the decertification now in effect, the electoral law atmosphere will be forever changed through the use of computers and more sophisticated and user-friendly balloting machines.

JASON W. CLECKNER

The *Rico* Dilemma

I. INTRODUCTION

In *Commonwealth v. Rico*,[44] Joseph Rico was found guilty by a jury of first degree murder and was sentenced to life imprisonment. On appeal, the Pennsylvania Superior Court vacated the judgment of life imprisonment and remanded for a new trial, concluding that "the trial court erred in failing to strike the jury panel as a result of the prosecutor's use of peremptory challenges to exclude jurors of Italian descent because such use violated the appellee's rights"[45] pursuant to *Batson v. Kentucky*.[46] The Commonwealth of Pennsylvania thereafter appealed to the Pennsylvania Supreme Court and contended that the Superior Court incorrectly assumed that *Batson* applied to Italian-Americans.[47] The court concluded that "whether Italian-Americans comprise a cognizable group needing protection from community prejudices for purposes of *Batson* is a question of fact within the sound discretion of the trial court."[48] Therefore, the Pennsylvania Supreme Court reversed the Superior Court's decision (vacating appellee's conviction of life sentence) and remanded for further proceedings.

Once the case was heard in the United States' Court of Appeals for the Third Circuit,[49] it held that it was not unreasonable for the lower state courts in Pennsylvania to consider challenges to Italian-American prospective jurors under *Batson* because the United States Supreme Court had not extended the *Batson* protection to any European-American ethnicity, and it still had not done so by

44. Commonwealth v. Rico, 711 A.2d 990, 991 (1998).
45. *Id.*
46. Batson v. Kentucky, 476 U.S. 79 (1986).
47. Rico, 711 A.2d at 991.
48. *Id.* at 994.
49. Rico v. Leftridge-Byrd, 340 F.3d 178 (2003).

the time *Rico* was heard.[50] The Court of Appeals ultimately justified the Supreme Court's consideration of *Batson.*

Thus, according to the interpretative analysis by the U.S. Court of Appeals of the 3rd Circuit, the Supreme Court does not extend the *Batson* protection to individuals of Italian-American ethnicity (including others of Caucasian foreign descent and national origin). This is an unfortunate analysis of the *Batson* rationale, considering that it has the dangerous potential to confine the scope of the Equal Protection Clause of the 14th Amendment. Pursuant to a plethora of Supreme Court decisions,[51] under the Equal Protection Clause laws, initiatives, or state actions that discriminate on the basis of race, sex, and *national origin* are often struck down. For instance, *Hernandez v. Texas* ruled that the exclusion of a class of persons from jury service solely because of their ancestry or origin is discrimination prohibited by the Fourteenth Amendment.[52] In arriving at this decision, the Court employed a "heightened scrutiny" review.

Accordingly, cases that have come before the Supreme Court involving the discriminatory use of peremptory challenges based on national origin or ethnicity have been decided in favor of the ethnic defendant. For example, in *United States v. Martinez-Salazar,* the Court held that under the Equal Protection Clause, "a defendant may not exercise a peremptory challenge to remove a potential juror solely on the basis of the juror's gender, ethnic origin, or race."[53] In this case, there was no distinction between which ethnic groups could be afforded this protection, and which ethnic groups could not be given similar protection. As a result, attorneys should not (and cannot) exercise peremptory challenges in order to strike down potential jurors on the basis of national origin or ethnicity because of the effect the aforementioned Supreme Court rulings had on the *Batson* decision. As *Batson* and *Hernandez* demonstrate, African-Americans and Latinos have been afforded the *Batson* protection regarding discriminatory peremptory challenges because they are recognized as cognizable racial groups. Italian-Americans should have this privilege extended to them as well taking into account the fact that it can be established that they too can be recognized as a cognizable racial class. However, prior to approaching this argument, we shall first delve into a brief study of the *Batson v. Kentucky* holding.

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50. Rico, 340 F.3d at 182-84.

51. *See, e.g.,* Loving v. Virginia, 388 U.S. 1 (1967); The Court ruled that laws that classify on the basis of race are reviewed under equal protection with strict scrutiny and will not be upheld unless they are necessary to accomplish some permissible state objective; *see also* J.E.B. v. Alabama, 511 U.S. 127 (1994); The Court ruled in a paternity suit, the equal protection clause prohibits gender discrimination in jury selection.

52. Hernandez v. Texas, 347 U.S. 475 (1954).

53. United States v. Martinez-Salazar, 528 U.S. 304, 315 (2000).

II. *BATSON V. KENTUCKY* (1986)

In this case, a black man was put on trial for second-degree burglary and receipt of stolen goods in Kentucky.[54] The prosecution used its peremptory challenges to strike all four black persons on the venire, and a jury composed of all whites was impaneled.[55] The defense counsel moved to discharge the jury on the ground that the prosecution's removal of the black veniremen violated the defendant's rights under the Sixth Amendment to a jury drawn from a cross section of the community, and under the Fourteenth Amendment to equal protection of the laws.[56] On appeal, the Kentucky Supreme Court affirmed the conviction and ruled based on the case of *Swain v. Alabama*,[57] which held that the defendant must demonstrate a systematic exclusion of a group of jurors from the venire.

On appeal to the Supreme Court, the issue before the Court was whether the defendant had to prove the systematic exclusion of blacks over a number of cases in order to succeed on an equal protection claim of discriminating use of the state's peremptory challenges.[58] Justice Powell, writing for the Court, held that the equal protection clause does not require that a petit jury be composed in whole or in part of persons of the defendant's own race, but the Equal Protection Clause guarantees to the defendant that a state will not exclude members of his or her race from the jury venire based on their race or on the idea that they are not qualified to serve because of their race.[59] The Court rejects the aspect of *Swain* that places the proof of discrimination solely on the defendant and creates a standard based on a three-step procedure: an establishment of a prima facie case of purposeful discrimination and demonstrating that the defendant is a member of a cognizable racial group; the burden of production shifts to the advocate of the peremptory strike; and the trial court must finally decide whether the defendant has proven purposeful discrimination.

The court in *Batson* held that an African-American criminal defendant could raise an equal protection challenge by demonstrating that the prosecution utilized peremptory challenges for the purpose of excluding potential jurors of the criminal defendant's race.[60] The Court explained that notwithstanding the prosecution's entitlement to use peremptory challenges for any reason, the Equal Protection Clause prohibits such use in a manner that challenges potential jurors solely based on their race.[61] The Court stated that "purposeful racial discrimi-

54. Batson, 476 U.S. at 82.
55. *Id.* at 83.
56. *Id.*
57. Swain v. Alabama, 380 U.S. 202 (1965).
58. Batson, 476 U.S. at 95–96.
59. *Id.* at 85–87.
60. Batson, 476 U.S. at 96.
61. *Id.* at 87.

nation in selection of the venire violates a defendant's right to equal protection because it denies him the protection that a trial by jury is intended to secure."[62]

Consequently, the Court sculpted a method that the defendant can present and prove discriminatory intent in a prosecutor's exercise of peremptory challenges. First and foremost, a defendant must establish and demonstrate a prima facie case of purposeful discrimination based solely on evidence concerning the prosecutor's exercise of peremptory challenges at the defendant's trial and by showing that the defendant is a member of a cognizable racial group.[63] The Court stated that in proving discrimination, the "defendant is entitled to rely on the fact, as to which there can be no dispute, that peremptory challenges constitute a jury selection practice that permits those to discriminate who are of a mind to discriminate."[64] Once the defendant satisfies a prima facie case, the burden of production shifts to the proponent of the peremptory strike to present a race-neutral explanation.[65] This is the second aspect of the *Batson* process. Finally, the third step is that the trial court must then decide whether the defendant has proven purposeful discrimination.[66] Furthermore, the most important aspect of the case (in regards to the argument of including Italian-Americans to the *Batson* protection) is that the Court cited *Castaneda v. Partida*,[67] which held that Mexican-Americans are a cognizable group under the Equal Protection Clause. Thus, the U.S. Supreme Court's jurisprudence leads to the conclusion that *Batson* can apply to purposeful discrimination in the use of peremptory challenges in jury selection based solely on ethnicity.

III. ANALYSIS: COGNIZABILITY AND ITALIAN-AMERICANS

In order for an ethnic individual to utilize the *Batson* protection, the main thrust of the prima facie case must be satisfactorily established by proving that one is a member of a cognizable racial or ethnic group. Cognizability is demonstrated by a defendant's showing that an ethnic group is discriminated against by the community and therefore needs to be protected from such community prejudices. Hence, a defendant must show that the ethnic group is: (1) defined and limited by clear and identifiable factors; (2) possesses a common thread of attitudes, ideas, or experiences; (3) shares a community of interests in a way that the group's interest cannot be adequately represented if the group is excluded from the jury selection process; and (4) is experiencing or has experienced discriminatory treatment and is in need of protection from community

62. Batson, 476 U.S. at 86.
63. *Id.* at 93-96.
64. *Id.* at 96.
65. Batson, 476 U.S. at 97.
66. *Id.* at 96-98.
67. Castaneda v. Partida, 430 U.S. 482 (1977).

prejudices.[68] Italians and Italian-Americans can unquestionably satisfy each component of satisfying cognizability.

Italians possess clear and identifiable factors and characteristics. They share a common language and a common culture that is distinct from any other culture throughout the world or within the United States. Their experiences emigrating from a politically and economically debilitated country was attributed to two devastating World Wars which induced a common relationship among Italians.[69] Similar to other immigrant groups, Italians faced many hardships when arriving to the United States, which was caused by heavy racism and prejudice. For instance, the U.S. federal and state governments led raids on Italian immigrants' houses because of the fear that they were Communists. This fact was evidenced in the Sacco and Vanzetti trial, when two Italian immigrants were convicted for murder even though the prosecution possessed no real substantial evidence.[70] The two men were convicted primarily because of their political beliefs. Religious beliefs also condemned the Italian immigrants. Job competition also exacerbated the major resentment against Italian-Americans. Native white workers perceived the Italian immigrants as competitors for jobs that they deserved. Most importantly, the U.S. federal government has discriminated against Italian-Americans. In the forty-eight hours following the bombing of Pearl Harbor, President Franklin Delano Roosevelt issued Proclamation 2527, which authorized restrictive rules for individuals of Italian descent.[71] This Executive Order was not only passed in response to the devastating attack on Pearl Harbor by the Japanese, but merely because of a paranoid delusion, ignited by xenophobic feelings, that anyone who was foreign or ethnic from Germany, Italy, or Japan living as an American could potentially be an enemy. As a result, 264 Italian-Americans were detained in internment camps by February 16, 1942.[72] As one can see, Italians, in conjunction with other immigrants, were discriminated against in their early years upon arrival to the United States.

Additionally, Italian-Americans face discrimination in contemporary times as well. Depictions in the media (which includes television, film, and print) instills a negative, inaccurate, and stereotypical portrayal of the Italian-American ethnic group. For example, there is an unacceptable depiction of Italian-Americans "as gangsters and undereducated individuals" in television shows such as

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68. United States v. DiPasquale, 864 F.2d 271, 277 (1988).

69. John De Ville, *Italians in the United States, available at* http://www.newadvent.org/cathen/08202a.htm (last visited Apr. 25, 2004).

70. *See* Felix Frankfurter, *The Case of Sacco and Vanzetti, available at* http://www.theatlantic.com/unbound/flashbks/oj/frankff.htm (last visited Apr. 25, 2004).

71. Honorable Matt Salmon, *Proclamation No. 2526, available at* http://www.foitimes.com/internment/Proclamation2526.htm (last visited Apr. 25, 2004).

72. *Id.*

The Sopranos and in films such as *Goodfellas* and *My Cousin Vinny.*[73] There was a recent placement of signs in Brooklyn reading, "Leaving Brooklyn Fugheddaboudit." The National Italian American Foundation (NIAF) stated that "while these signs were intended to promote the Borough of Brooklyn, they ha[d] nonetheless offended a considerable number of Italian Americans in the New York City area."[74] NIAF asked to have the language edited or have the signs removed. There was also a recent political cartoon drawn by the nationally renowned cartoonist Pat Oliphant, "which included a clearly pejorative term for Italians."[75] In response to this ethnic stereotyping, groups such as NIAF have mobilized in order to adequately represent and protect the interests of the Italian community. Consequently, it is plainly evident that Italian-Americans can be regarded as a "cognizable ethnic group" pursuant to past and present stereotypical discrimination.

IV. CONCLUSION

The Supreme Court in *Batson v. Kentucky* clearly stated that purposeful discrimination in the use of peremptory challenges in jury selection can be based solely on ethnicity, so long as the defendant is able to prove that he or she can be regarded as a member of a cognizable ethnic group. Furthermore, cases such as *Hernandez v. Texas* and *United States v. Martinez-Salazar* held that ethnicity and/or national origin were not sufficient bases for exclusion from jury panels. Therefore, attorneys cannot utilize peremptory challenges in order to strike down potential jurors on the basis of national origin or ethnicity because of the Equal Protection Clause of the Fourteenth Amendment; and this should not only include Latinos, but should also include Italian-Americans because it is clear that they can be perceived as a cognizable racial class, which is the primary requirement of engaging the *Batson* protection.

PHIL OLIVERI

A New Standard for Measuring Just Compensation?

I. INTRODUCTION

The impact of *Brown v. Legal Foundation of Washington* may create a new standard for measuring just compensation under the Takings Clause of the Fifth Amendment.[76] First, the net loss approach that the majority in *Brown* used to

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73. The National Italian American Foundation, *Focus: Image and Identity (Fall 2003),* http://www.niaf.org/image_identity/fall2003.asp (last visited Apr. 25, 2004).

74. The National Italian American Foundation, *supra* note 73.

75. *Id.*

76. U.S. CONST. amend. V.

determine the value of compensation owed when private property is taken is in sharp contrast with the traditional market value approach preferred by the *Brown* dissent. Second, the impacts and effects of net loss analysis will further reduce compensation given to property owners. Finally, recent just compensation proceedings suggest the market value approach is still widely preferred to the net loss approach used in the *Brown* decision.

II. SUMMARY OF *BROWN V. LEGAL FOUNDATION OF WASHINGTON*

Every State in the Union has established a program that uses interest on lawyers' trust accounts also known as "Interest On Lawyer Trust Accounts" (IOLTA) to provide legal services to the indigent.[77] The Washington IOLTA rules require attorneys to place trust funds in separate interest bearing accounts.[78] When the interest earned exceeds the bank charges associated with the account, the attorney must disperse interest payments to the client or reinvest the interest earned.[79] However, in some situations, funds are so nominal or short-term that it is not feasible to place the fund in an interest-bearing account; thus, the funds would be placed in noninterest-bearing accounts.[80] An IOLTA program permits attorneys to combine these nominal and short-term trust funds into one account, which generates interest earnings where net interest could not otherwise be generated.[81] The interest earned must then be used for, "law-related charitable and educational purposes."[82]

In *Brown,* two Washington residents, whose funds earned some interest in an IOLTA account, alleged that the IOLTA program constitutes a taking under the Fifth Amendment for which they are entitled just compensation.[83] The Fifth Amendment mandates that a taking must be for public use, in which just compensation must be paid to the owner.[84] The Supreme Court previously held that interest generated in IOLTA accounts is the private property of the principal owner.[85] In *Brown*, the Court further held that the interest generated in IOLTA accounts ultimately serve the public by providing funding for legal services.[86] Because the government physically takes possession of interest that belongs to private citizens for the public purpose of providing legal aid, a taking has occurred. Finally, the *Brown* court had to determine what just compensation is payable to the property owners.

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77. Brown v. Legal Foundation of Washington, 538 U.S. 216 (2003).
78. *Id.* at 224.
79. *Id.*
80. *Id.* at 223–24.
81. *Id.*
82. Brown, 538 U.S. at 224.
83. *Id.* at 228.
84. U.S. CONST. amend. V.
85. Phillips v. Wash. Legal Found., 524 U.S 156, 172 (1998).
86. Brown, 538 U.S. at 235.

The *Brown* majority held that the standard for measuring just compensation is the property owner's *net losses* rather than the value of the public's gain.[87] Net loss (or net interest), in this case, is calculated by deducting transaction and administrative costs and bank fees from the interest earned on a client's funds.[88] The Court poses this illustration when a client earns $0.55 of interest, the transaction costs incurred to disburse the earnings may equal $5.00. These transaction costs include a stamp and envelope to send the check, and the clerical and administrative fees incurred to determine how much interest was earned on the client's funds. Because the costs of receiving the interest exceed total interest earned, a client's net losses are zero and no just compensation is due.[89]

In sharp contrast, the *Brown* dissenters maintain that just compensation is measured by the *market value* of the confiscated property, rather than the net loss to the owner.[90] Market value is the full monetary equivalent of the property taken, it "is not reduced by what the owner would have lost in taxes or other exactions."[91] Under a market value approach, just compensation should be equal to the *gross* amount of the interest taken by the State.[92] In the above example, the client should be entitled to the $0.55 of interest, regardless of the transaction costs associated with the disbursal of the payment. The dissent fears that eighty years of precedent, applying a market value approach, has been overruled by the net loss approach in the *Brown* decision.[93]

III. IMPLICATIONS OF THE HOLDING

Brown, applying net loss calculations, could significantly influence the measure of just compensation awarded to private property owners. Net loss is measured by the market value of a property interest less significant transaction costs including administrative, legal, accounting or other fees that the property owner would have incurred in a typical market transaction. In contrast, market value is only the price upon which a buyer and seller would agree.[94] Therefore, if courts adopt this net loss approach, property owners would receive less compensation for the loss of their property.

A net loss approach should alarm property owners, as it would further decrease the compensation a government entity must pay to take private property. Applying a market value approach, the Supreme Court has recognized that property owners may not be fully indemnified particularly because market value

87. Brown, 538 U.S. at 235–36.
88. *Id.* at 238.
89. *Id.* at 237–38.
90. *Id.* at 250.
91. *Id.*
92. Brown, 538 U.S. at 238.
93. *Id.* at 243.
94. United States v. Miller, 317 U.S. 369, 374 (1943).

cannot account for the sentimental value placed on personal property.[95] Therefore, even the market value approach tends to underpay the property owner. A net loss approach will further reduce compensation owed to a property owner; not only will compensation lack sentimental value, transaction costs could also be deducted out of the final just compensation award.

For example, in *Brown,* the dissenting opinion illustrates the affects of the net loss approach. In a case where the government seizes rents received by the owner of the building, the government may not subtract out the costs incurred in collecting the rents when calculating just compensation.[96] Further, if the government seizes a private home, the net loss approach permits the government to deduct from the market value of the home, the sales taxes that would have been incurred and administrative fees that would be owed to the real estate agent. In either scenario, the property owner's compensation will be less if the net loss approach is applied as opposed to the market value approach.

As the Supreme Court has stated, the term "just" in the Fifth Amendment, "evokes the idea of fairness and equity."[97] These concepts cannot be ignored in determining what just compensation should be in a particular case. The Court has already recognized that the market value approach underestimates the value placed on property; by reducing just compensation to a level that is even lower seems to violate general principles of fairness and equity. This analysis suggests that the net loss approach is not intended to overrule the market value approach and should not become the standard measure of just compensation.

IV. THE FUTURE OF THE MARKET VALUE APPROACH

The Supreme Court has held that measuring just compensation is dependent on the facts of each case; there is no absolute rule.[98] However, the Court has also stated that when assessable, the market value should be the mechanism to calculate just compensation.[99] Because the Court has consistently used the market value approach, it is possible that *Brown*'s reach will only extend to cases factually similar. Some commentators may see the purpose of *Brown* as giving a "green light for IOLTA programs," rather than to overrule the established market value mechanism for determining just compensation.[100] Examinations of just compensation cases decided after Brown help determine the future of the market value approach and the scope of the net loss approach.

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95. United States v. 564.54 Acres of Land, 441 U.S. 506, 511 (1979).

96. Brown, 538 U.S. at 249, *quoting* Phillips, 524 U.S. at 170.

97. United States v. Commodities Trading Corp., 339 U.S. 121, 124 (1950).

98. United States v. Toronto, Hamilton & Buffalo Navigation Co., 338 U.S. 396, 402 (1949).

99. *Id.*

100. Ronald D. Rotunda, *Found Money: IOLTA,* Brown v. Legal Foundation of Washington, *and the Taking of Property without the Payment of Compensation,* CATO Supreme Court Review: 2002-2003, 245, 268.

A recent Ninth Circuit case applied the net loss approach articulated in *Brown*. In *McIntyre*, an inmate brought a suit claiming that the prison committed a taking of his property entitling him to just compensation.[101] Similar to an IOLTA program, the prison program required all money earned by inmates be kept in a trust account. These accounts were combined to earn interest, in turn, the interest was spent for the general welfare of the entire prison.[102] Like *Brown*, the *McIntyre* court concluded that this was a taking of private property. The *McIntyre* court held that just compensation is, "measured by the net value of the interest that was actually earned by the owner of the principal."[103] The court went on to say that the costs of administering the prisoner's property funds may be much higher than the interest earned by the prisoner; in that case there would be no net loss or compensation owed.[104]

Additionally, an Illinois court followed *Brown* by applying the net loss approach in a just compensation case.[105] The Illinois Unclaimed Property Act mandates that unclaimed personal property must be placed in the custody of the State until it is returned to the rightful owner.[106] In *Canel,* the property owner claimed his securities, but the State retained interest and dividends paid while in State custody. The court concluded that the interest and dividends earned remained the property of the owner and that they were taken by the State. The *Canel* court remanded the case to determine just compensation consistent with the *Brown* net loss approach.[107]

While the above cases suggest that some courts have adopted the net loss approach to calculate just compensation, the overwhelming majority of cases continue to apply a market value approach. In *Bustos*, the court reviewed the valuation of a residential lot in an eminent domain proceeding.[108] That court stated that "[j]ust compensation is determined by the property's market value."[109] In a similar case, a Tennessee county condemned private property in order to use the land to build a new jail.[110] The *Waters* court wrote:

Just compensation requires the fair cash market value on the date of taking of the property for public use. The fair market value of the land is the price that a reasonable buyer would give if he were willing to, but did not have to, purchase

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101. McIntyre v. Bayer, 339 F.3d 1097, 1100 (9th Cir. 2003); *see also* Schneider v. Cal. Dep't of Corr., 345 F.3d 716, 720 (9th Cir. 2003).

102. McIntyre, 339 F.3d at 1097.

103. McIntyre, 339 F.3d at 1100, *quoting* Brown, 538 U.S. at 238.

104. *Id.* at 1101.

105. Canel v. Topinka, 793 N.E.2d 845, 853 (Ill. App. 1 Dist. 2003).

106. *Id.* at 848.

107. *Id.* at 853.

108. City of Las Vegas v. Bustos, 75 P.3d 351 (Nev. 2003).

109. *Id.* at 352.

110. Sevier County, Tenn. v. Waters, 126 S.W.3d 913 (Tn. Ct. App. 2003).

and that a willing seller would take if he were willing to, but did not have to, sell.[111]

Additionally, several other courts have favored a market value approach when awarding just compensation.

For example, in a dispute about apartment properties, an Illinois court wrote, "the taking must be for public use and that the government must pay the owner just compensation, which is determined to be the property's fair market value."[112] Similarly, in a condemnation proceeding, a Nevada court wrote, "[c]onstitutional principles provide that just compensation is measured by the fair market value of the condemned property."[113] Moreover, a New Jersey court held that just compensation is the fair market value as of the date of the taking.[114] Finally, in an eminent domain action, a Connecticut court held, "just compensation is the market value of the condemned property when put to its highest and best use at the time of the taking."[115]

Although the dissent was concerned that *Brown*, "brushes aside 80 years of precedent on determining just compensation," in the year since *Brown* was decided only a handful of published cases have used the net loss approach.[116] Additionally, the applicability of the net loss approach appears to be limited to facts similar to an IOLTA program. In the few cases that used net loss calculations, the property in dispute was monetary income such as interest earned on trust funds and dividends earned on unclaimed property. Similarly, in *Brown,* the private property taken was interest earned on funds held in a Washington State IOLTA account. In contrast, courts applied a traditional market value approach where the private property taken consisted of real property as opposed to pure monetary property.

As *Brown* did not specifically overrule a market value approach, it is unclear, which standard of just compensation valuation should be applied in the fu5ture. However, if the Court's intent was to overrule 80 years of precedent, it seems they would have clearly stated it. Further, it is unlikely the *Brown* court intended to undermine the notion of fairness implied in the Just Compensation Clause by uniformly requiring courts to apply net loss analysis. Therefore, the future of the net loss approach will likely be limited to cases factually similar to

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111. Waters, 126 S.W.3d at 913, *quoting* Nashville Hous. Auth. v. Cohen, 541 S.W.2d 947, 950 (Tenn. 1976).

112. Shaikh v. City of Chicago, 341 F.3d 627, 632 (7th Cir. 2003).

113. County of Clark v. Sun State Prop. Ltd., 72 P.3d 954, 957 (Nev. 2003).

114. Hous. Auth. of New Brunswick v. Suydam Investors, L.L.C. 826 A.2d 673, 681 (N.J. 2003), *quoting* County of Monmouth v. Hilton, 760 A.2d 786, 788 (N.J. Super. Ct. App. Div. 2000).

115. Town of Montville v. Antonino, 825 A.2d 230, 234 (Conn. App. Ct. 2003), *quoting* Comm'r of Transp. V. Towpath Assocs., 767 A.2d 1169, 1177 (Conn. 2000).

116. Brown, 538 U.S. at 243.

Brown, while the market value approach will continue to be the favored valuation method for most other just compensation proceedings.

MONICA REYNOSO

"Working with an English only policy" *Iris Cosme v. The Salvation Army* 284 F. Supp. 2d 229

I. INTRODUCTION

In our melting pot of a society, the essence of communication between individuals is always at issue, especially in the workplace. While many inhabitants of the United States speak very little or no English today, employers have taken steps to assure that the work place is free of languages other than English. Employers have routinely taken steps to prohibit their workers from speaking any language other than English during work hours. Although this English only policy has been consistently upheld by the courts where the intent of the policy is not per se discriminatory, it has carried with it much controversy. The issue presented in *Cosme v. Salvation Army*[117], is whether the English-only policy used by the Salvation Army was *per se* discriminatory, and whether there were legitimate reasons for having and enforcing such a policy.

II. FACTS

In *Cosme v. The Salvation Army*, the plaintiff (hereinafter Cosme), was a Native Puerto Rican whose primary language is Spanish.[118] She was able to sufficiently understand and speak English.[119] Cosme was employed by the Salvation Army and was later terminated by the Salvation Army partially because of her disregard for their English-only policy.[120]

Cosme was a full-time clerk for the Salvation Army from August 1996 until January 2001.[121] While she was employed there, the Salvation Army maintained an English-only policy which stated that employees must speak English to the best of their ability, except when on breaks, during meal periods, and before or after work commences.[122]

In 1999, the Salvation Army began strictly enforcing this English-only policy as a result of receiving complaints from English speaking employees and volun-

117. Cosme v. Salvation Army, 284 F. Supp. 2d 229 (2003).
118. *Id.* at 232–34.
119. *Id.* at 232.
120. *Id.*
121. *Id.*
122. Cosme, 284 F. Supp. 2d at 232–33.

teers.[123] Cosme subsequently failed to abide by this policy.[124] In addition to failing to follow the English-only policy, Cosme was insubordinate and late on numerous occasions.[125] Prior to her termination, Cosme was warned numerous times about her violations.[126]

III. HOLDING

The court held that the Salvation Army's English-only policy was not *per se* discriminatory since there was sufficient evidence to support Cosme's ability to adequately speak English.[127] Additionally, the court held that there was a legitimate business reason to support the English-only policy.[128]

IV. COURT'S REASONING

In order for Cosme to have proven disparate treatment, the court required her to show four elements.[129] First, the plaintiff must show that she is a member of a protected class; second, she must show that she suffered some type of harm; third, she must show that there was discriminatory animus, and fourth she must show causation. In the case at hand, the Salvation Army concedes the first two elements, however it contends that there was no discriminatory animus.[130] Discriminatory animus may be shown directly or indirectly.[131]

Direct evidence of discrimination generally occurs where an employer makes statements with discriminatory intent to an employee.[132] To demonstrate direct evidence of discrimination, Cosme argued that she was asked by her employer to speak Spanish on numerous occasions; however on other occasions, when she spoke Spanish without being asked to do so, she was reprimanded for it.[133] In other words, she contended that the English-only policy was not enforced all the time.[134] The court concluded that even if the policy was not consistently enforced, direct discrimination was not present because the Salvation Army was allowed to require Cosme to speak English pursuant to its very clear policy.[135]

After the court, in *Cosme*, analyzed direct discrimination, it then considered indirect discriminatory animus under a three-stage burden-shifting approach

123. Cosme, 284 F. Supp. 2d at 233.
124. *Id.*
125. *Id.*
126. *Id.* at 233–34.
127. Cosme, 284 F. Supp. 2d at 240.
128. *Id.* at 239–40.
129. *Id.* at 235.
130. *Id.*
131. *Id.*
132. Cosme, 284 F. Supp. 2d at 235.
133. *Id.*
134. *Id.*
135. *Id.*

first expressed by the Supreme Court of the United States in the early 1970's.[136] The first part of this approach requires the plaintiff to make out a *prima facie* case of discrimination. If this first stage can be shown by the plaintiff, then there is a presumption of discrimination.[137] If this presumption is established by the plaintiff, the employer may rebut the claim in the second stage by showing a legitimate, non-discriminatory reason for its existence, supported by evidence.[138] In the third stage, the plaintiff must prove by a preponderance of the evidence that the discriminatory animus was the determinative cause for the business to make the decision to employ and enforce such a policy.[139]

V. FIRST STAGE

In order for Cosme to have proven a *prima facie* case of discrimination, in the first Stage, she would have had to show that she is a member of a protected class, that the Salvation Army took an adverse action against her, that Cosme was qualified to perform her duties at the Salvation Army, and the position at the Salvation Army remained open or was filled by someone with similar qualifications.[140] As previously discussed, the Salvation Army conceded the fact that she was a member of a protected class and that she suffered adverse action when she was fired.[141] The Salvation Army contended however, that based on her work performance, she was not qualified to carry out her duties as a Salvation Army employee.[142]

Since Cosme claims that she was unable to adequately speak English, the court reasons that under the third element of a *prima facie* case she would not be able to perform her job.[143] In other words, the court concludes that if she could not sufficiently speak English in order to perform her job, then is would be discrimination if the Salvation Army were to have asked her to do so.[144] The court however concluded that Cosme was able to speak English and therefore under the third element it was not discriminatory to ask her to speak English while working.[145] A key factor in the court's determination in this case was Cosme's ability to speak English.[146] Based on Cosme's ability to speak English, the court reasons that if she can speak English, even on a limited level, she

136. Cosme, 284 F. Supp. 2d at 235.
137. Cosme, 284 F. Supp. 2d at 235–36 (citing McDonnell Douglas Corp. v. Green, 411 U.S. 792, 802, 36 L. Ed. 2d 668, 93 S. Ct. 1817 (1973)).
138. *Id.* at 236.
139. *Id.*
140. Cosme, 284 F. Supp. 2d at 236.
141. *Id.*
142. *Id.*
143. *Id.* at 236.
144. *Id.*
145. Cosme, 284 F. Supp. 2d at 236.
146. *Id.* at 236–37.

cannot as a matter of law show *per se* discrimination merely because an English-only policy is enforced against her.[147]

The court subsequently concluded that Cosme had sufficiently proven the fourth element since her vacant position remained open.[148] Although Cosme had met her burden of making out a *prima facie* case, the court never the less failed to find in her favor for other reasons.[149]

VI. SECOND STAGE

In the second stage, the Salvation Army was able to provide legitimate reasons for terminating Cosme.[150] The Salvation Army produced evidence that Cosme was insubordinate and consistently tardy.[151] The court reasoned that where Cosme was insubordinate to her supervisor under the English-only policy, the Salvation Army's reasons for termination were both valid and nondiscriminatory.[152] The court supported this reasoning based on the evidence that Cosme was tardy on at least four documented occasions.[153]

VII. THIRD STAGE

In the third stage, the burden shifted back to Cosme to prove, that although there were legitimate reasons offered for her termination, the true reason for her termination was her speaking Spanish.[154] This argument by Cosme is refuted because the court finds evidence that the Salvation Army has terminated employees in the past, for tardiness. Furthermore, the court concluded that Cosme had failed to meet her burden since the English-only policy was not *per se* discriminatory.[155]

VIII. ANALYSIS

Many businesses throughout the United States employ English-only policies. Essentially, an English-only policy prohibits employees from speaking any language other than English during official work time.[156] There are usually exceptions in this policy that allow employees to speak other languages during breaks and lunch.[157]

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147. Cosme, 284 F. Supp. 2d.
148. *Id.* at 237.
149. *Id.*
150. Cosme, 284 F. Supp. 2d at 238–40.
151. *Id.* at 238–40.
152. *Id.* at 238.
153. Cosme, 284 F. Supp. 2d at 238.
154. *Id.* at 239.
155. *Id.*
156. *Id.* at 232.
157. *Id.*

Although controversial, the English-only policy has been upheld both in spirit by the EEOC[158] and by legal authority where the business can show that the business's policy was justified by some business necessity.[159] Under Title VII, employers are entitled to adopt English-only rules under certain circumstances, if it is adopted for nondiscriminatory reasons.[160] Additionally, under Title VII individuals are not guarenteed the right to speak their native language.[161]

Although some plaintiffs have argued that the EEOC regulations state that English-only policies are presumptively discriminatory, it has been upheld by the court that the burden is on the plaintiff to show that a policy is discriminatory.[162] In *Velasquez v. Goldwater Memorial Hospital*, the court held that under Title VII, a plaintiff must show that the employer took the adverse action against the plaintiff because of her protected status.[163]

In *Velasquez*, the plaintiff also argued that she was asked to speak Spanish on several occasions.[164] She argued that the English-only policy adopted by the Hospital was presumptively discriminatory.[165] As in *Cosme,* the court in *Velasquez* disagreed with the plaintiff and held that even where an English-only policy is applied at certain times and not at others, it is still permissible where the policy is employed for a legitimate business purpose.[166]

In *Garcia v. Gloor,* the court held that an English-only rule enforced against Hector Garcia, a Mexican employee was not discriminatory.[167] Similar to the plaintiff in *Cosme,* Garcia spoke both English and Spanish.[168] Garcia was employed by Gloor Lumber and Supply, Inc.[169] His major duties were stocking and selling lumber.[170] Garcia was ultimately terminated for failing to adequately perform his duties, as well as for his constant disregard for the English-only policy.[171]

As the Salvation Army did in *Cosme,* Gloor Lumber offered legitimate business reasons for the implementation of their English-only policy.[172] An English

158. The U.S. Equal Employment Opportunity Commission Complaince Manual *at* http://www.eeoc.gov/policy/docs/national-origin.html#VC (last visited Apr. 25, 2004) [hereinafter E.E.O.C. Manual].

159. Cosme v. Salvation Army, 284 F. Supp. 2d 229 (2003).

160. E.E.O.C. Manual, *supra* note 158.

161. Garcia v. Gloor, 618 F.2d 264, 268-69 (1980).

162. Velasquez v. Goldwater Memorial Hospital, 88 F. Supp. 2d 257, 262 (2000).

163. *Id.* at 262.

164. *Id.*

165. *Id.*

166. Velasquez, 88 F. Supp. 2d at 262.

167. Garcia v. Gloor, 618 F.2d at 266.

168. *Id.*

169. *Id.*

170. *Id.*

171. *Id.* at 266-67.

172. Garcia, 618 F.2d at 267.

only policy is not *per se* discriminatory where it can be shown that it is a business necessity.[173] The court held that discrimination does not exist in this case because Garcia, who could speak both English and Spanish, disregarded his employer's clear policy.[174] The court further held that it is acceptable if the violation of the policy led to Garcia's eventual termination.[175]

IX. CONCLUSION

It is clear from *Cosme* and other case authority that in order to prove discrimination, an employee must either show direct evidence of discriminatory intent or that there was no legitimate reasons for the business to establish its English-only policy. If a business provides legitimate reasons for employing such a policy, then the burden shifts to the plaintiff to prove that the reason for the termination was based specifically on the plaintiff's national origin and not on the legitimate business reasons proffered.[176]

KEVIN UNIGLICHT

173. Cosme, 284 F. Supp. 2d at 229.
174. Garcia, 618 F.2d at 272.
175. *Id.*
176. Cosme, 284 F. Supp. 2d at 229.

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