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Engage

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Letter from the Editor

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Engage: The Journal of the Federalist Society Practice Groups features scholarship on important legal and public policy issues from some of the best legal minds in this country. It is a collaborative effort, involving the hard work and dedication of our fifteen Practice Groups, along with outside authors who volunteer their time and expertise. Engage seeks to contribute to the marketplace of ideas in a way that is collegial and intelligent. We offer original ideas and perspectives, and hope to raise the level of debate in the legal community and beyond.

We hope that readers enjoy the articles and come away with new information and fresh insights. Articles are usually chosen by our Practice Group chairmen, but we strongly encourage readers to send us any suggestions and responses at info@fedsoc.org.

Sincerely,

Katie McClendon

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Administrative Law & Regulation

Agency Taxation

*By Christopher DeMuth Sr.**

In recent years Congress has delegated its taxing and appropriating powers to regulatory agencies under several guises. The new "agency taxation" is distinct from the economic transfers implicit in many regulatory programs and also from agency fees-for-service. Traditional electricity and telephone regulation has required cross-subsidized rate structures, with above-cost rates for urban and business customers and below-cost rates for rural and residential customers. Environmental, health, and safety regulations impose compliance costs that are paid by firms and their customers for the benefit of customers or the general public. And agencies have long charged fees for particular services and transactions, ranging from admission fees at national parks to FCC license fees and FDA and Patent Office filing fees. The subject of this paper, in contrast, is broad-based taxes unrelated to any transactions with the agencies, used to fund the agencies' budgets and grant programs.

I. Taxation by Delegation

The FCC Universal Service Program. The first recent instance of agency taxation is in the Telecommunications Act of 1996, which authorizes the FCC to set and collect taxes for promoting "universal service" and gives the Commission wide discretion to determine whom to tax and at what rate and how to spend the revenues.

Currently, the FCC collects the tax (which it calls a "contribution") on the interstate and international revenues of landline and wireless telecommunications companies, cable companies that provide voice service, and paging service companies. It is a substantial tax—much higher than the 3-percent statutory federal excise tax on telephone service—and the Commission adjusts it each quarter to keep pace with its program spending. Recently the tax rate has been 15.7 percent (3Q-2014), 16.1 percent (4Q-2014), 16.8 percent (1Q-2015), and 17.4 percent (2Q-2015).

The FCC spends the revenues, which come to about $8.8 billion per year, on grant programs for landline, wireless, broadband, and Wi-Fi equipment and services for schools, libraries, and rural health care facilities, and on rate-subsidies for low-income and rural customers. Thus the Commission's "Lifeline" program currently provides a free basic wireless phone or landline installation and free basic telephone service (250 minutes per month) to about 12 million low-income customers, at a cost of $1.6 billion annually. In May 2015, FCC Chairman Tom Wheeler announced plans to expand the Lifeline program to cover Internet broadband as well as telephone service.

The universal service program is a delegation not only of Congress's taxing power (Article I, Section 8: "The Congress shall have power to lay and collect taxes … to … provide for the … general welfare of the United States") but also of its appropriations power (Article I, Section 9: "No money shall be drawn from the treasury, but in consequence of appropriations made by law"). The FCC's annual operating budget of about $500 million is covered entirely by the Commission's licensing and other fees and a share of the net proceeds from its spectrum auction programs—but the expenditures are nonetheless subject to annual appropriations by Congress in response to FCC budget requests. The universal service program, in contrast, is administered for the FCC by a subsidiary not-for-profit corporation, the Universal Service Administrative Company, whose revenues and expenditures are independent of annual budget requests and congressional appropriations.

The Public Company Accounting Oversight Board. The Sarbanes-Oxley Act of 2002 established the PCAOB to regulate accounting firms that audit "public companies" (those that issue publicly-traded stock) and broker/dealers in public stocks. The PCAOB's annual budget of about $250 million is funded almost entirely by its own tax (which it calls an "accounting support fee") on the equity capital or net asset value of public companies and broker/dealers. The Board establishes its operating budget for the year, subtracts a small sum from annual fees it collects from the accounting firms it regulates (about $1.6 million), and allocates the remainder among public companies and broker/dealers according to their size as measured by equity capital or net asset value. (The Board exempts smaller public companies from its tax, and it typically funds part of each year's budget from carryover tax and fee revenues from prior years.)

The PCAOB, like the FCC's Universal Service Administrative Company, is a 501(c)(3) subsidiary of a regulatory agency—for the PCAOB, the parent is the SEC. Its annual budget must be approved by the SEC, but is entirely independent of congressional appropriations. The Sarbanes-Oxley Act contains several provisions emphasizing that the PCAOB is independent of Congress and that its tax revenues are not "monies of the United States." But the Board's taxes (as well of course as its accounting regulations) are federally enforced legal obligations.

The Consumer Financial Protection Bureau. The CFPB, established by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, enjoys a different form of agency self-financing. The Bureau is funded, not by its own tax, but rather by a draw (up to a statutory cap) from the profits of the Federal Reserve Banks. Those profits—revenues from fees and earnings from open market operations, minus the Federal Reserve's own operating expenses—were previously remitted to the Treasury as general revenue. Guaranteeing the CFPB a portion that would otherwise support other, discretionary government programs is a new entitlement program like Social Security or Medicare—an entitlement for a regulatory agency

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rather than citizens. Federal Reserve profits are currently more than $100 billion, while its own operating costs are about $6 billion and the CFPB's expenses are about $500 million. The Bureau's budget, like that of the Federal Reserve, is entirely independent of congressional appropriations.

II. Constitutional Questions

The case law is adverse to a constitutional challenge to the delegation of taxation and appropriations in the FCC, PCAOB, and CFPB programs. The Supreme Court held in *Skinner v. Mid-American Pipeline Co.* that the nondelegation doctrine, which is extremely lenient, does not apply differently to Congress's taxing powers than to its other enumerated powers.[1] Lower courts have upheld aspects of the financing mechanisms of both the FCC universal service program and the CFPB against constitutional challenge.[2]

A well-crafted constitutional challenge to the universal service program and PCAOB could, however, have substantially greater prospects than this (rather thin) case law might suggest. The agencies' delegated powers go far beyond anything that has been considered by the Supreme Court. *Skinner* involved pipeline user fees limited to funding Transportation Department regulation of pipeline safety, and the Court noted that the fee revenues were subject to congressional appropriations (the arrangement was akin to the FCC's operating budget). *Texas Office of Public Utility Counsel v. FCC* formally considered only a poorly argued challenge to the universal service program on Origination Clause grounds (the circuit court also spurned a Taxing Clause argument in a footnote, but cursorily and as dicta because the issue had not been properly briefed). The Supreme Court's decision on the constitutionality of the PCAOB did not consider the Board's taxing and appropriating powers at all.[3]

Recently, moreover, Congress's increasingly bold delegation of regulatory discretion, and several Executive Branch actions going beyond statutory delegations, have prompted some reconsideration of whether the nondelegation doctrine is really as dead as had been supposed. During the past two Supreme Court terms, three justices have issued striking invitations to relitigate nondelegation.[4] Justice Thomas's opinion in *Department of Transportation v. Association of American Railroads* includes an impressive analysis of how "intelligible principles" might be specified to distinguish permissible from impermissible delegations. He does not touch on taxing and appropriations powers, but the features of the universal service program and PCAOB discussed here—wholesale delegation of discretion to determine whom is to be taxed and at what tax rates, and to collect and spend tax revenues without congressional appropriation—would fit well with a new effort to define constitutionally clear, judicially workable principles.

The CFPB presents issues separate from those of the universal service program and the PCAOB. The Bureau does not possess autonomous taxing power, and its independence of appropriations is part of the broader independence of the Federal Reserve System, which occupies a special place among federal institutions. It is worth noting, however, that the Fed's special status dates from a time when its primary function was to manage the money supply, which was thought to necessitate extraordinary independence from short-term political pressures. But in recent years the Fed has acquired many new regulatory powers of its own (in addition to those of the CFPB), through the Dodd-Frank Act and other statutes. The Fed's and the CFPB's regulatory policies are often highly costly and controversial, and they do not involve the considerations that motivated special independence for monetary policy. The transformation of the Fed's responsibilities and the grafting on of CFPB regulation invite a reconsideration of its freedom from congressional appropriations.

III. Policy and Political Questions—and Guiding Principles

Regardless of the constitutional status of the universal service program, PCAOB, and CFPB under prevailing or prospective Supreme Court doctrines, they raise profound questions about separation of powers and national policy that ought to be of keen interest to the president, Congress, and the general public.

The text of the Constitution indicates that the framers regarded the taxing power as particularly sensitive; they went out of their way to require that revenue measures originate in the House, the people's chamber whose members face the voters every two years. The universal service and PCAOB taxes, along with the implicit tax in the CFPB's financing mechanism, do not loom large among federal revenue raisers. They are, however, recent initiatives adopted in the context of routine deficit spending and high political controversy over taxes. They are properly viewed as ingenious means of evading accountability for taxes, which if allowed to stand could encourage a trend toward a system where Congress takes the credit for new programs but does not bear the responsibility of paying for them. It is worth notice that the annual profits of the Federal Reserve Banks could finance numerous additional "entitlement agencies" on the model of the CFPB—whose automatic budgets, siphoned from funds that would otherwise go to the Treasury as general revenues, would in effect be deficit financed. *Presidents ought to resist statutory arrangements that give executive agencies responsibility to impose taxes and spend the revenue while restricting the president's ability to supervise either.*

The appropriations power is the lynchpin of congressional control over federal spending and much else. It is also a key mechanism for countering—through "appropriations riders"—executive actions opposed by congressional majorities. But Congress's "power of the purse" has been falling into disuse, and the statutes discussed in this paper are part of a broader trend. This was dramatically illustrated in late 2014 when President Obama unilaterally revised statutory immigration policies in ways that many in Congress opposed on constitutional or policy grounds or both. Shortly after the president announced his policy changes, Republican opponents in Congress responded that they would halt them with a rider to the appropriations of the U.S. Customs and Immigration Service. Then, a few days later, came an embarrassed follow-up: staffers had discovered that USCIS is not only self-funded by its own fees, but also (unlike the FCC's operating budget) exempt from congressional appropriations. Regardless of the merits of President Obama's immigration policies, *Congress's confusion over which agencies are and are not dependent on it should be worrisome to those who*

believe that robust inter-branch competition is an important feature of our system of government. Foremost among the worriers should be members of Congress themselves.

Finally, combining regulation, taxation, and appropriation in a single executive agency is a concentration of power conducive to both abuse and bad policy. The CFPB has been notably imperious concerning its regulatory powers and independence from the rest of the federal government. The chairman of the PCAOB draws a salary of $672,676 and the other Board members $546,891—they are by far the highest paid political officials in the federal government. The FCC's Lifeline program has been infamously beset by fraud and abuse.[5] More generally, regulatory agencies already possess tremendous power to impose costs and dispense benefits by rulemaking (as in the examples mentioned at the beginning of this paper), which in the nature of the case is independent of taxation, appropriation, and budgeting.

All single-purpose, mission-driven agencies tend to pursue their missions to excess—but regulatory agencies, unlike spending agencies, lack the conventional constraints of public finance that oblige trade-offs among competing public goods. To compensate for this problem, presidents from Ronald Reagan to Barack Obama have required regulatory agencies to follow a cost-benefit standard for their new rules. Congressional reform proposals would go further with such devices as a judicially reviewable cost-benefit standard, a "regulatory budget," and "regulatory pay-go" procedures. Giving regulatory agencies additional, highly discretionary authority to tax and subsidize the firms and individuals they regulate is a large step backwards from these mainstream, bipartisan reform initiatives. *Better policy requires greater institutional discipline, but the arrangements discussed in this paper relax institutional discipline to an unprecedented degree.*

The FCC's universal service program, the PCAOB, and the CFPB are signal innovations in government. With comprehensive taxing, spending, and regulatory powers, they are, in effect, autonomous special-purpose national governments, independent of elected officials so long as their enabling statutes remain on the books. They are innovations that friends of our constitutional order, and of sound and honest public policy, should seek to counter and reverse.

Endnotes

1 490 U.S. 212 (1989).

2 *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5th Cir. 1999); *CFPB v. Morgan Drexen Inc.*, – F. Supp. 3d –, No. SACV 13-1267-JLS, 2014 WL 5785615 (C.D. Cal., Jan. 10, 2014).

3 *Free Enterprise Fund v. PCAOB*, 561 U.S. 477 (2010).

4 *City of Arlington v. FCC*, 133 S. Ct. 1863, 1879 (2013) (Roberts, C.J., dissenting); *Department of Transportation v. Association of American Railroads*, Docket No. 13-1080, March 9, 2015 (Alito, J., concurring, and Thomas, J., concurring in the judgment).

5 A 2013 review of the Lifeline subscribers of the top telephone service providers found that 41 percent of more than six million subscribers receiving free or subsidized services either could not demonstrate their eligibility or failed to respond to requests for certification. *See* Spencer E. Ante, "Millions Improperly Claimed U.S. Phone Subsidies," *Wall Street Journal*, Feb. 12, 2013. Lifeline service is widely marketed as "Free Obama Phones," and one service provider has advertised for phone distributors under the headline, "Get Paid to Pass Out Free Government Cellphones." *See* Charles C.W. Cooke, "Life, Liberty, and a Free Phone," *National Review*, March 11, 2013.

Civil Rights

The Kudzu of Civil Rights Law: Disparate Impact Spreads Into Educational "Resource Comparability"

*By Carissa Mulder**

Note from the Editor:

This article is about a Dear Colleague letter from the Department of Education's Office of Civil Rights regarding the unequal distribution of school resources. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. But when we do, as here, we will offer links to other perspectives on the issue, including ones opposed to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• *Civil and Human Rights Coalition Applauds Dept. of Education Guidance to Advance Resource Equity for Minority Students*, The Leadership Conference on Civil and Human Rights, (October 1, 2014), http://www.civilrights.org/press/2014/resource-equity-guidance-1.html.

• Sonali Kohli, *Modern-Day Segregation in Public Schools*, The Atlantic, (November 18, 2014), http://www.theatlantic.com/education/archive/2014/11/modern-day-segregation-in-public-schools/382846/.

• Chester E. Finn Jr., *Punishing Achievement in Our Schools*, National Review, (November 25, 2014), http://www.nationalreview.com/article/393407/punishing-achievement-our-schools-chester-e-finn-jr.

Introduction

In June 2015, the Supreme Court issued its decision in *Texas Department of Housing v. Inclusive Communities Project, Inc.*, ruling that disparate impact claims are cognizable under the Fair Housing Act.[1] The Court's decision in *Texas Department of Housing* gives a limited blessing to the use of disparate impact in housing, where it has spread from its original home in employment law.[2] It remains to be seen whether this limited approval extends beyond the housing realm. However, even before the Court's decision, disparate impact was being used to regulate the use of criminal background checks in hiring,[3] school discipline,[4] housing patterns,[5] and now, availability of school resources.

The Department of Education's Office of Civil Rights Enforcement (OCR) is particularly enthusiastic about using disparate impact theory to promote de facto racial balancing in education and in October 2014 issued guidance in the form of a "Dear Colleague" letter regarding the distribution of school resources.[6] The guidance interprets racial disparities in the availability or utilization of resources—such as advanced courses, extracurricular activities, technology, and funding—as invidious racial discrimination, even when those disparities are not the result of racially disparate treatment, but rather of facially neutral policies. For example, if a predominantly white and Asian school district offers Advanced Placement courses and a predominantly black and Latino school district does not, the guidance presumes this is invidious racial discrimination, even if it is because the first school district has more funds through property taxes or a greater percentage of students performing above grade level who are therefore able to take advantage of the courses. The guidance also presumes it is invidious discrimination if a given school does offer Advanced Placement courses, but a smaller percentage of black or Latino students than white and Asian students enroll in those courses. This guidance is a dubious interpretation of Title VI, encourages school districts to engage in racially disparate treatment, is economically unrealistic, and infringes on decisions best made by local authorities.

I. Guidances and Dear Colleague Letters: Are They Really Non-Binding?

As a preliminary matter, it is questionable whether OCR has the authority to notify school districts of sweeping policy changes like this through a Dear Colleague letter rather than by promulgating a rule. This is, alas, a time-honored tradition at the Department of Education (and other agencies) that persists despite criticism of the practice.[7] It is much easier for OCR to issue a controversial policy change through a guidance document than to expose it to the rigors of notice-and-comment rulemaking required by the Administrative Procedure Act.[8] The rulemaking process puts the regulated parties on notice of the proposed policy change, as was intended, and allows the regulated parties to mount fierce opposition to the proposed rule if they wish. This can make it very difficult for the agency to achieve its policy goals.[9] As a result, OCR usually issues guidance documents such as "Dear Colleague" letters, which are written without the formal opportunity for public participation provided by the notice-and-comment process.[10]

Although Dear Colleague letters purport to be mere explanations of how OCR will enforce already-existing statutes and rules,[11] they often go beyond explanation and into substantive policy-making.[12] Although OCR has the power to revoke federal

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funds if they find a school district to be in violation of Title VI, they rarely do so. School districts fall in line as best they can with the requirements included in the latest Dear Colleague letter because an investigation alone is punishment enough for an alleged violation. A brief glance at recent resolutions of investigations against school districts makes this clear. This is what the Manchester, New Hampshire school district was subjected to during an investigation for an alleged disparate impact violation of Title VI regarding the racial composition of AP and other advanced high school classes:

> During the investigation, OCR requested information from the District for the 2010-2011 and 2011-2012 school years. OCR reviewed documentation from the District regarding the policies and procedures relating to enrollment in its courses and programs. OCR also conducted onsite meetings and interviews with administrators, guidance counselors, principals, Building Level Instructional Leaders, classroom teachers, parents and students at the District's three comprehensive high schools, three middle schools, and five of the District's elementary schools, as well as the MST. Additionally, OCR analyzed student enrollment data for the District and for each high school in the District, and compared it to enrollment data OCR was able to obtain for several District programs, including AP course enrollment.[13]

An extensive investigation of this sort is tedious, time-consuming, and expensive.[14] It is no wonder, then, that announcements from OCR often include a variation of, "Prior to the conclusion of OCR's investigation, the District expressed an interest in voluntarily resolving this review."[15] This, along with the threat of losing federal funds, is why OCR is able to achieve its policy objectives through guidance documents. Much of the time, the case will not make it to litigation and OCR will not have to withhold funding. The investigation process is enough to cow the district into submission, and a guidance document tells other districts how to avoid an investigation.

II. Disparate Impact

a. Title VI and Disparate Impact

The problem with OCR's invocation of disparate impact theory, aside from the weakness of disparate impact theory itself[16] and the questionable use of Dear Colleague letters, is that the text of Title VI does not prohibit disparate impact discrimination, but only disparate treatment. Therefore, the disparate impact approach is suspect after the Supreme Court's decision in *Alexander v. Sandoval*. Although the Court assumed, for purposes of deciding the case, that regulations premised on Title VI were permissible, it called the use of disparate impact into question in footnote 6: "We cannot help observing, however, how strange it is to say that disparate-impact regulations are 'inspired by, at the service of, and inseparably entwined with' § 601 . . . when § 601 permits the very behavior that the regulations forbid."[17]

As Justice Scalia noted, § 601 "provides that no person shall, 'on the ground of race, color, or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity' covered by Title VI."[18] Notably, § 601 only prohibits discrimination "on the ground of" race, color, or national origin, which implies discriminatory treatment. It does not include language such as "discriminatory effects" or "disproportionately affect," which would indicate that Congress intended for Title VI to include a disparate impact component.[19] It is, therefore, an odd result to say that § 602, which only gives federal agencies the authority to act against violations of § 601, permits agencies to find violations of § 601 for behavior that the text of § 601 does not prohibit.[20]

Even if disparate impact is permitted under Title VI, the October 1 Dear Colleague letter is a use of disparate impact with a particularly expansive reach:

> Chronic and widespread racial disparities in access to rigorous courses, academic programs, and extracurricular activities; stable workforces of effective teachers, leaders, and support staff; safe and appropriate buildings and facilities; and modern technology and high-quality instructional materials further hinder the education of students of color today. Below I highlight the negative effects these inequalities can have on student learning and encourage school officials to assess regularly disparities in educational resources in order to identify potential—and where it exists to end—unlawful discrimination, particularly in districts with schools where the racial compositions vary widely.[21]

Elsewhere, OCR states, "Since research is mixed on whether within-school or between-school comparisons are more likely to find disparities in teacher quality, OCR retains discretion to focus on either or both comparisons depending on contextual factors."[22] It is difficult to understand how OCR intends to eliminate disparities in teacher quality within schools, as that more or less entails eliminating disparities in teacher quality, period.[23] It also seems unworkable. Unless a school is intentionally putting black and Latino students into classes with less effective teachers, what is to be done? One of the studies OCR cites to support its decision to investigate within-school variations in teacher quality posits that schools are likely unable to identify the best teachers, and even if they can identify the best teachers, they may not choose to hire them or union rules may prevent them from being hired.[24] Even if schools can identify the best teachers in the school, determining what the best use of their talents is seems to be a prudential judgment. Should the best math teacher teach AP Calculus so that high-achieving students master the challenging material, which might be very difficult or almost impossible with a lesser teacher? Or is it better for her to teach remedial math in hopes that she can bring low-achieving students up to par? These are decisions best made by principals who are familiar with the strengths and weaknesses of students and teachers at their school, not by a bureaucrat in OCR or a federal judge. This is common sense to almost everyone, including the Supreme Court, except OCR and DOJ.[25]

In short, everything that remotely touches on education is fair game for OCR to bring a claim of racial discrimination. Bear in mind that OCR is targeting statistical disparities in this area, not disparate treatment. Although the letter does mention

disparate treatment, referred to as "intentional discrimination," such discrimination is forbidden by the plain text of § 601 and is relatively easy to identify, particularly because it includes facially neutral policies that are pretexts for intentional discrimination.[26] Rather, what they are targeting are racial disparities that are the effect of what everyone agrees are facially neutral policies.

b. The Application of Disparate Impact

OCR determines whether disparate impact constitutes racial discrimination by asking a series of questions:

> 1) Does the school district have a facially neutral policy or practice that produces an adverse impact on students of a particular race, color, or national origin when compared to other students?
>
> 2) Can the school district demonstrate that the policy or practice is necessary to meet an important educational goal? In conducting the second step of this inquiry OCR will consider both the importance of the educational goal and the tightness of the fit between the goal and the policy or practice employed to achieve it. If the policy or practice is not necessary to serve an important educational goal, OCR would find that the school district has engaged in discrimination. If the policy or practice is necessary to serve an important educational goal, then OCR would ask:
>
> 3) Are there comparably effective alternative policies or practices that would meet the school district's stated educational goal with less of a discriminatory effect on the disproportionately affected racial group; or, is the identified justification a pretext for discrimination? If the answer to either question is yes, then OCR would find that the school district had engaged in discrimination. If no, then OCR would likely not find sufficient evidence to determine that the school district had engaged in discrimination.[27]

In other words, if a facially neutral policy or practice produces an adverse impact on students of preferred races—it is, after all, unlikely that OCR will be concerned about a policy that has an adverse impact on whites or Asians—it is probable that the school district will be found to have discriminated on the basis of race. If OCR does not agree about the importance of the educational goal the policy or practice is intended to promote, then the school will fail the second step and will be found to have discriminated. If OCR decides that the policy or practice is not *necessary* to achieve that goal, then the school will be found to have engaged in discrimination. How many practices are absolutely necessary? Much of the time, it is a prudential judgment as to which one of several options is the best. OCR can easily second-guess that decision. And even if the school district survives step two, is there some policy or practice somewhere in the world that might achieve the same goal? Of course most people can dream up some alternative policy that might be better, even if it is more expensive or unworkable in practice. If OCR dreams up such an alternative, yet again, the school will be found to have engaged in discrimination. And if the school manages to satisfy all those requirements, plus convince OCR that this practice is not a pretext for disparate treatment, "OCR *likely* would not find sufficient evidence to determine that the school district had engaged in discrimination," but it makes no guarantees.

The hypothetical school district had not engaged in disparate treatment discrimination, or OCR would have proceeded on that basis. Nor was OCR able to show that there was another policy that would achieve the same goal while causing less of a disparate impact, or that the school's reason for the practice was a pretext. So in the end, OCR is announcing, what really matters is whether we *think* your resource allocation is discriminatory, even if there is no evidence of discrimination other than a statistical disparity. This makes a laughingstock of the rule of law.

c. Some racial disparities are more important than others

OCR cherry-picks comparisons between racial groups to imply that there is something nefarious about racial disparities. For example, they note that black students are less likely than members of other racial groups to attend schools that offer Advanced Placement (AP) courses, and that black and Latino students enroll in calculus at levels below their representation in the population.[28] However, it is not until you read the footnotes that you realize that Asian students are the racial or ethnic group most likely to attend a school with AP courses.[29] In fact, a greater percentage of Latino students than white students attend a school that offers AP courses.[30]

As is common in all topics involving both education and race, Asians are almost entirely ignored in this document. The letter uses the term "students of color" rather than "minority students," and "students of color" refers to "black, Latino, Asian, Native Hawaiian/Pacific Islander, American Indian/Alaska Native, and students of two or more races."[31] Yet the document focuses almost exclusively on the resources and academic participation of black and Latino students as compared to white students. This is likely because focusing on black and Latino students as compared to white students allows OCR to present a simplistic contrast between adequate resources and academic participation for and by white students, and inadequate resources and academic participation for and by black and Latino students. Introducing Asian students into the picture blurs the contrast. The result of looking at black, white, Latino, and Asian students, instead of just the first three groups, reveals a state of affairs congruent with that at other education levels.[32]

An additional flaw in the Guidance, and in disparate impact theory generally, is its failure to recognize the fact that any policy or practice will benefit some groups more than others. Funding for an AP Spanish class will disproportionately benefit Hispanic students from bilingual families. Students whose families only speak English will be at a comparative disadvantage in the AP Spanish class. Funding for a soccer team will disproportionately benefit those who are athletic. Every decision about allocating funds benefits someone and does not benefit someone else. Every funding decision disparately impacts someone. If we divert funds away from the AP-offering schools attended by 94 percent of Asians to the non-AP-offering schools attended by 80 percent of blacks, there will be a disparate impact on Asians.[33]

OCR realizes this, which is why it only considers disparate

impact discriminatory if it has a negative effect on preferred groups: "For example, students in special education may be served by more teachers and support staff than other students, and therefore districts may spend more on those students, but that does not mean those students are receiving a disproportionate share of resources."[34] Similarly, "Funding disparities that benefit students of a particular race, color, or national origin may also permissibly occur when districts are attempting to remedy past discrimination."[35] Given that Title VI has been used to target intentional discrimination since its enactment in 1964, there is presumably little disparate treatment discrimination left to address. This means that most of this supposed historical discrimination would be disparate impact discrimination. OCR therefore encourages school districts to engage in blatantly racially motivated disparate treatment discrimination in order to rectify a disparate impact caused by a facially neutral policy.

III. Disparate Impact Encourages Entities to Engage in Disparate Treatment

As mentioned above, the Guidance encourages funding disparities that attempt to remedy purported past discrimination. These disparities do not result from a facially neutral policy that disproportionately affects particular racial groups, but from intentionally providing more resources to a particular school or district *because* the students are a preferred race. We are back to the dilemma Justice Scalia highlighted in *Ricci*: in an attempt to avoid disparate impact discrimination, entities often veer over into engaging into disparate treatment discrimination.[36]

This is an even more egregious example than in *Ricci*, however, as OCR contemplates that the school district will not be engaging in disparate treatment not only to avoid a charge of disparate impact, but to remedy supposed historical discrimination. This is impermissible. As Justice Powell wrote in *Bakke*, "helping certain groups whom the faculty of the Davis Medical School perceived as victims of 'societal discrimination' does not justify a classification that imposes disadvantages upon persons like respondent, who bear no responsibility for whatever harm the beneficiaries of the special admissions program are thought to have suffered."[37] The intended beneficiaries of the Davis Medical School racial quotas likely had experienced disparate treatment on the basis of their race. *Bakke* was decided in 1978, only fourteen years after the passage of the 1964 Civil Rights Act, which included Title VI. Yet even then, Justice Powell said, you cannot require innocent third parties to pay for others' sins. How much less can you require a second generation Chinese-American student to lose his AP Physics class because the high school across town is poor and disproportionately comprised of second-generation Mexican-American students?

IV. The Trouble with Resource Allocation as Discrimination

An additional flaw in the Guidance is that OCR tries to steal a base by treating disparate resource allocation, standing alone, as invidious discrimination. The cases it cites to support its claim that differential resource allocation by itself constitutes discrimination all relate to integration of school districts that had practiced de jure segregation.[38] In those cases, differential allocation of resources was one factor in determining whether school districts that had practiced legally-mandated racial segregation had dismantled their dual systems.[39] Examining the differential allocation of resources served as a way of smoking out racially disparate treatment and efforts to perpetuate segregation, particularly in determining compliance with a desegregation decree.[40]

Many school districts over which OCR is claiming authority based on resource allocation discrimination never practiced de jure segregation. Those that did were required to integrate their schools, often at the cost of great social disruption, forty years ago. No K-12 student today has ever been subject to de jure educational segregation. As the Supreme Court approvingly summarized the District Court's findings in a case that sought to lift a desegregation injunction, "The District Court found that present residential segregation was the result of private decisionmaking and economics, and that it was too attenuated to be a vestige of former school segregation."[41] And in a later case, "Where resegregation is a product not of state action but of private choices, it does not have constitutional implications. It is beyond the authority and beyond the practical ability of the federal courts to try to counteract these kinds of continuous and massive demographic shifts."[42] OCR's guidance is not limited to school districts that once practiced de jure segregation, but covers all school districts in the country. It does not allege that there is widespread intentional discrimination in allocation of resources between and within schools, but alleges that students of preferred races are more likely to be poor than students of non-preferred races. The poorer students are more likely to attend schools that have fewer resources, either because they live in a poorer area that has less property tax revenue or because it costs more to educate the poorer students. This is not invidious racial discrimination of the kind at issue in *Green*, *Freeman*, and *Dowell*. This is just a consequence of living in a poor area.[43]

V. Finances, Local Control, and Social Engineering

OCR's vision for implementing this guidance is not modest. OCR acknowledges that disparities in resources are not due to different treatment on the basis of race, but rather because schools are usually funded through property taxes.[44] This is not racial discrimination that any ordinary person would recognize. It is simply economic reality: wealthier areas will be able to afford nicer gyms and iPads for fourth-graders. Describing economic reality as racial discrimination is consistent with the Obama Administration's abuse of disparate impact in other areas. HUD's recent "Affirmatively Furthering Fair Housing" rule dubs geographic clustering of racial groups "segregation" because members of ethnic minorities are less likely to be able to afford housing in more genteel areas.[45] The fact that members of certain ethnic groups are more likely to be poor than are members of other ethnic groups, and therefore have less access to housing and schools in wealthy neighborhoods, which is what these two administrative dictates boil down to, is not racial discrimination. It is discrimination on the basis of your pocketbook. By that standard, the largely white population of poverty-stricken Appalachia has an axe to grind against Asians and Latinos, as the residents of Appalachia live in an ethnically homogenous area of concentrated poverty and almost certainly have scant access to AP courses.[46]

More importantly, the Supreme Court has already addressed this issue in regard to an Equal Protection claim in *San Antonio Independent School District v. Rodriguez*.[47] This is relevant to an analysis of Title VI because the Court interprets Title VI and the Equal Protection Clause in a very similar way.[48] Furthermore, the case was decided almost a decade after Title VI was enacted, and the Court did not even mention Title VI in its decision despite the fact that the poorer school district was 90 percent Mexican-American and 6 percent black, and the wealthier school district was about 81 percent white, 18 percent Mexican-American, and less than 1 percent black.[49] Significantly, although *Griggs v. Duke Power*, which incorporated disparate impact into Title VII, had been decided two years earlier, the Court makes no reference to disparate impact in *Rodriguez*, and says that it is impossible to identify a suspect class.[50] Instead of analyzing whether there is a suspect class defined by race—especially since the two representative school districts discussed in the litigation were majority-Hispanic and majority-white, respectively—the Court looked at whether there was a suspect class comprised of "poor people," and determined there was not.

The Court framed the issue thus: "the courts in these cases have virtually assumed their findings of a suspect classification through a simplistic process of analysis: since, under the traditional systems of financing public schools, some poorer people receive less expensive educations than other more affluent people, these systems discriminate on the basis of wealth."[51] This is the essence of the Resource Comparability Dear Colleague letter when it is stripped of the racial folderol that expresses concern for poor children of one race and not another. And, the Supreme Court found, there is no right to have the most expensive education on offer as long as education is being provided:

> [N]either appellees nor the District Court addressed the fact that, unlike each of the foregoing cases, lack of personal resources has not occasioned an absolute deprivation of the desired benefit. The argument here is not that the children in districts having relatively low assessable property values are receiving no public education; rather, it is that they are receiving a relatively poorer quality education than children in districts having more assessable wealth. Apart from the unsettled and disputed question whether the quality of education may be determined by the amount of money expended for it, a sufficient answer to appellees' argument is that, at least where wealth is involved, the Equal Protection Clause does not require absolute equality or precisely equal advantages. Nor indeed, in view of the infinite variables affecting the education process, can any system assure equal quality of education except in the most relative sense.[52]

OCR refuses to acknowledge that finances are limited and that tradeoffs must be made in the area of education as everywhere else. "Intradistrict and interdistrict funding disparities often mirror differences in the racial and socioeconomic demographics of schools, particularly when adjusted to take into account regional wage variations and extra costs associated with educating low-income children, English language learners, and children with disabilities."[53] If it costs more to educate the students at a particular school, that school will not have the same financial resources to provide a new football field or a music class as a school where it costs less to educate students in the basics. That is not racial discrimination, but economic reality. It is difficult to escape the conviction, though, that OCR is less concerned with excellence than egalitarianism, even if that means depriving middle-class children of the opportunity to excel.

The only way that OCR can achieve its goal is by forcing states and localities to remake their school funding systems. The reference to intradistrict and interdistrict funding disparities makes this plain. The Supreme Court has frowned upon this as well, reasoning that taxation and education policy are both subjects to which great deference is owed to state legislatures. The Court wrote:

> We have here nothing less than a direct attack on the way in which Texas has chosen to raise and disburse state and local tax revenues. We are asked to condemn the State's judgment in conferring on local subdivisions the power to tax local property to supply revenues for local interest. In so doing, appellees would have the Court intrude in an area in which it has traditionally deferred to state legislatures. . . . No scheme of taxation, whether the tax is imposed on property, income, or purchases of goods or services, has yet been devised which is free of all discriminatory impact. In such a complex area in which no perfect alternatives exist, the Court does well not to impose too rigorous a standard of scrutiny lest all local fiscal schemes become subjects of criticism under the Equal Protection Clause.[54]

VI. The Guidance Fails to Consider Individual Circumstances and Individual Choice

The Guidance rests on a flawed premise: that lack of resources is primarily responsible for the achievement gap between blacks and Hispanics and whites. (No word on what is responsible for the achievement gap between Asians and whites.) If we throw more money at the problem, it will be solved. There are no differences between poor students in predominantly minority schools and middle- and upper-class students in predominantly white schools that cannot be solved by offering more extracurricular activities, more laptops, and more AP courses. OCR is so committed to this premise that at points the Guidance descends into absurdity.

"English language learners represented five percent of high school students, but only two percent of the students enrolled in an AP course."[55] It is difficult to understand how the Department of Education can expect students who are still learning to speak English to participate in AP classes in great numbers. An inability to speak the language of the school system would seem to be an important predictor of educational difficulties. How can you expect someone who is not even proficient in English to take an AP English Literature course? If they are still trying to learn English, why would they take an AP French course? And, perhaps most importantly, if they are still trying to learn English, that is probably going to absorb much of the time and effort that they could have put into

studying other subjects.

Latinos are more likely to attend a school that offers AP courses than are white students.[56] And yet, the Guidance notes "students of color are less likely than their white peers to enroll in [advanced courses and gifted and talented programs] within schools that have those offerings."[57] So Latinos are more likely to have the opportunity to enroll in an AP class than are white students, but they apparently are less likely to take advantage of the opportunity when it is presented. Perhaps teachers need to push black and Latino students harder to enroll in advanced classes. But if, in the end, black and Latino students are for whatever reason disproportionately uninterested in enrolling in advanced courses, or are disproportionately likely to be at an academic level where they are unable to handle the coursework, no amount of pushing will erase the racial disparity.[58]

Similarly, OCR sees invidious discrimination in inexperienced teachers being disproportionately likely to teach in schools that primarily serve black and Latino students. If we can only identify the effective and experienced teachers, OCR says, we can assign them to teach black and Latino students. But what if teachers do not want to teach at those schools for any number of non-racially discriminatory reasons? OCR itself trumpets that black and Latino students are more likely to be subject to disciplinary action.[59] Additionally, "Low socioeconomic status, whether measured at the individual or school level, has been associated with an increased risk of school discipline."[60] What if that reflects disproportionate involvement in disruptive behavior, and teachers prefer to teach in a school with better-behaved students?[61] Or it could be as simple as teachers preferring to live near their homes in middle-class areas.[62] Regardless, OCR ignores the fact that teachers too have the ability to choose where they want to work. If the district tries to force them to teach at a school that is a particularly unpleasant assignment, they may simply quit. And since they are effective teachers, they can probably find teaching jobs in another district or a private school.

In short, OCR fails to recognize that human beings are individuals who have agency. The people whose lives are affected by the Guidance are not little square units who come in different colors but are otherwise identical. They come from particular families within particular cultures and have the ability to make choices, even if that choice is just foot-dragging.

VII. Forcing Less-Prepared Students into Advanced Courses May Hinder, Not Help, Their Educational Progress

The Guidance notes that black and Latino students are underrepresented in gifted and talented programs compared to their representation in student bodies.[63] The Guidance also notes that English language learners are far less likely to be enrolled in gifted and talented programs than are non-English language learners.[64] If the racial breakdown of students enrolled in gifted and talented classes is to exactly match their representation in the student body, schools have two options: prevent some white and Asian students from enrolling in those classes, or enroll more black and Latino students in those classes.

The latter option may seem attractive. Is there a downside to enrolling more black and Latino students in advanced classes? The answer is, "of course not," as long as they are equally academically prepared. If they are *not* as academically prepared as the median student in the gifted and talented class, research at the post-secondary education level suggests that being placed in an advanced class may result in these students learning less than they would have learned in a regular class. This theory is known as "mismatch," and has been extensively discussed in Richard Sander and Stuart Taylor, Jr.'s book of the same name. In the post-secondary environment, it is likely that placing students in classes where their academic preparation is weaker than the class's median student has, in the end, led to fewer black and Latino scientists and lawyers.[65] The negative effects of placing students in classes for which they are at a relative disadvantage academically seem to be the same across racial lines, but due to affirmative action policies it is usually black and Latino students who are the "beneficiaries" of these efforts.[66]

It is likely that placing elementary and high school students in advanced classes for which they are academically under-prepared would have a similar effect. It is unlikely that these students would be able to make up the ground necessary to succeed in the class—after all, their classmates will be learning at the same time they are. It is profoundly discouraging to know that you lag behind your classmates no matter how hard you work, which could easily cause students to question their overall academic ability and educational aspirations. Bureaucrats' desire to have the "right" racial mix in advanced classes is no reason to subject students to such a discouraging experience. Students who have the academic preparation and interest to succeed in an advanced class should be encouraged to enroll in that class, regardless of their race. Similarly, students whose academic preparation is better suited to another class should be encouraged to enroll in that class, regardless of their race.

Conclusion

When the Supreme Court imported disparate impact into Title VII in *Griggs v. Duke Power*, it was a well-meaning, if misguided, attempt to eliminate unnecessary job qualifications that disproportionately disadvantaged blacks. Forty years later, disparate impact has spread far beyond the confines of employment law and is being used as a tool by would-be social engineers. The Resource Allocation Guidance will increase the federal government's micromanagement of elementary and secondary education and reduce local control of schools. It will encourage school districts to favor certain schools over others when making funding decisions based on the racial composition of the schools. It will do little to improve the academic opportunities of black and Hispanic students, but it may harm the academic opportunities of white and Asian students.

There are doubtless some students in underprivileged schools who would benefit from and are interested in participating in AP courses and other advanced coursework. Accommodating those students does not require remaking the entire American school system under the auspices of a mandate from Washington. Allowing high-scoring students to transfer to public schools that offer advanced courses is one comparatively simple solution. Allowing charter schools to operate, or even providing vouchers for private schools, are alternatives. All these options are less disruptive than transforming property

tax systems and faculty assignments. However, those options quite possibly will not reduce racial disparities, but will provide an opportunity for youngsters of all races who have the drive and talent to pursue a challenging education. That ought to, but will not, be good enough for the social engineers at OCR.

Endnotes

1 Tex. Dep't of Housing v. Inclusive Communities Project, Inc., 135 S.Ct. 2507 (2015).

2 *Id.* at 2522-2524 (describing limitations on disparate impact liability).

3 *See* U.S. Commission on Civil Rights, Assessing the Impact of Criminal Background Checks and the Equal Employment Opportunity Commission's Conviction Records Policy (Dec. 2013), *available at* http://www.eusccr.com/EEOC_final_2013.pdf.

4 *See* U.S. Dep't of Educ., Office of Civil Rights, and U.S. Dep't of Justice, Dear Colleague Letter: Nondiscriminatory Administration of School Discipline (Jan. 8, 2014), available at http://www2.ed.gov/about/offices/list/ocr/letters/colleague-201401-title-vi.html; *see also* U.S. Commission on Civil Rights, School Discipline and Disparate Impact (Apr. 2012), *available at* http://www.usccr.gov/pubs/School_Disciplineand_Disparate_Impact.pdf.

5 *See* Affirmatively Furthering Fair Housing, 80 Fed. Reg. 42272 (July 16, 2015) (to be codified at 24 CFR Parts 5, 91, 92, 570, 574, 576, and 904); *see also* Abigail Thernstrom, Peter Kirsanow, and Todd Gaziano, "Comment re Docket No. FR-5173-P-01, 'Affirmatively Furthering Fair Housing,'" (Sept. 17, 2013), *available at* http://www.newamericancivilrightsproject.org/wp-content/uploads/2014/04/HUD-Comment-Affirmatively-Furthering-Fair-Housing.pdf.

6 U.S. Dep't of Educ., Office of Civil Rights, Dear Colleague Letter: Resource Comparability [hereinafter Resource Comparability] (Oct. 1, 2014), *available at* http://www2.ed.gov/about/offices/list/ocr/letters/colleague-resourcecomp-201410.pdf.

7 Robert A. Anthony, Interpretive Rules, *Policy Statements, Guidances, Manuals, and the Like—Should Federal Agencies Use Them to Bind the Public?*, 41 Duke L.J. 1311, 1354 (1992).

8 Ming Hsu Chen, *Governing by Guidance: Civil Rights Agencies and the Emergence of Language Rights*, 49 Harv. C.R.-C.L. L. Rev. 291, 339 (2014) ("agencies can change their legal stances relatively easily—indeed, that is one reason why they use guidance in lieu of more formalized rulemaking").

9 *See* R. Shep Melnick, *The Odd Evolution of the Civil Rights State*, 37 Harv. J.L.P.P. 113, 122-23 (2014).

10 *See* Ming Hsu Chen, *Governing by Guidance: Civil Rights Agencies and the Emergence of Language Rights*, 49 Harv. C.R.-C.L. L. Rev. 291, 301-02 (2014).

11 Resource Comparability at n. 3 ("This guidance does not add requirements to applicable law, but provides information and examples to inform recipients about how the Department evaluates whether covered entities are complying with their legal obligations.").

12 Nina A. Mendelson, *Regulatory Beneficiaries and Informal Agency Policymaking*, 92 Cornell L. Rev. 397 (2007). *See also* Jesse Krohn, *Sexual Harassment, Sexual Assault, and Students with Special Needs: Crafting an Effective Response for Schools*, 17 U. Penn. J. L. Soc. Ch. 29, 36 (2014) ("When schools are given clear, reliable guidelines for how they should behave – and clear, reliable guidelines for how they will be punished if they do not – they comply, to the benefit of students. . . . OCR released a 'Dear Colleague' letter mandating policy changes in the way schools address sexual harassment and sexual assault.").

13 Letter from Thomas J. Hibino, Regional Director, U.S. Dep't of Educ., Office of Civil Rights, to Dr. Debra J. Livingston, Superintendent of Manchester School District, Re: Case No. 01-11-5003 Manchester School District, at 2 (April 9, 2014) (on file with author).

14 For example, a recently settled Title IX investigation of a California school district was opened in November 2011 and resolved in October 2014. *See* Letter from Arthur Zeidman, Regional Director, U.S. Dep't of Educ., Office of Civil Rights, to Dr. John A. Garcia, Superintendent, Downey Unified School District, Re: Case No. 09-12-1095, at 1 (Oct. 14, 2014) (on file with author).

15 Letter from Thomas J. Hibino, Regional Director, U.S. Dep't of Educ., Office of Civil Rights, to Dr. Debra J. Livingston, Superintendent of Manchester School District, Re: Case No. 01-11-5003 Manchester School District, at 1 (April 9, 2014); *see, e.g.*, Letter from Arthur Zeidman, Regional Director, U.S. Dep't of Educ., Office of Civil Rights, to Dr. John A. Garcia, Superintendent, Downey Unified School District, Re: Case No. 09-12-1095, at 1 (Oct. 14, 2014) (on file with author); Letter from Taylor D. August, Director, Dallas Office, U.S. Dep't of Educ., Office of Civil Rights, to Dr. Gearl Loden, Superintendent, Tupelo Public School District, Re: OCR Docket 06-11-5002, at 1 (Sept. 25, 2014) (on file with author).

16 Tex. Dep't of Housing v. Inclusive Communities Project, Inc., 135 S.Ct. 2507, 2527 (2015) (Thomas, J., dissenting) ("We should drop the pretense that *Griggs'* interpretation of Title VII was legitimate.").

17 Alexander v. Sandoval, 532 U.S. 275, n. 6 (2001).

18 *Id.* at 278.

19 Sandoval at n.6. This argument is of course controversial; *see id.* at 306 (Stevens, J., dissenting).

20 Resource Comparability at 2.

21 *Id.* at n. 15.

22 *Id.* at 12-13. OCR writes that states and districts are developing teacher evaluation systems that will be able to provide information about teacher effectiveness. This seems overly optimistic. Even if the most effective teachers are identified, it is difficult to understand how districts will override the role of individual choice in teacher placement.

23 Cory Koedel and Julian R. Betts, *Re-examining the Role of Teacher Quality in the Educational Production Function* (April 2007), http://economics.missouri.edu/working-papers/2007/wp0708_koedel.pdf, 17-18.
The lack of between-school variation in teacher value-added is likely to be largely the result of the inability of schools to identify and hire the best teachers. In Section VIII, we show that the observable teacher qualifications most often linked to recruitment, retention and salaries are almost entirely unable to predict teacher value-added. Furthermore, Ballou (1996) shows that even when schools are able to hire seemingly superior teachers, they often choose not to. Finally, schools at SDUSD are further limited in their ability to select the most effective teachers by the labor contract between SDUSD and the teachers' union. This contract requires that schools with an open position choose from the five teachers with the most district seniority who apply for the position and meet the state qualifications, restricting each school's pool of potential applicants.

24 Milliken v. Bradley, 418 U.S. 717, 741-42 (1974) ("No single tradition in public education is more deeply rooted than local control over the operation of schools; local autonomy has long been thought essential both to the maintenance of community concern and support for public schools and to quality of the educational process.").

25 Resource Comparability at 6-8.

26 *Id.* at 8.

27 *Id.* at 3.

28 *Id.* at n. 10. Philip Handwerk, et al., Access to Success: Patterns of Advanced Placement Participation in U.S. High Schools, (July 2008), http://www.ets.org/Media/Research/pdf/PIC-ACCESS.pdf (finding six percent of Asian students, 12 percent of Latino students, and 14 percent of white students attend high schools without any Advanced Placement courses).

29 *Id.*

30 *Id.* at 2.

31 Richard Sander and Stuart Taylor, Jr., Mismatch: How Affirmative Action Hurts Students (2012) 34. Nationwide, the academic index of whites taking the SAT is about 140 points higher than the academic index for blacks (corresponding to a 300-point black-white gap on the current SAT I test, and a 0.4 GPA gap in high school grades), and it has hovered in that range for the past twenty years. Hispanics, in contrast, have an average academic index that is about 70 points lower than that of whites. The gap for American Indians is very similar to the black-white gap, and the academic index of Asians is about thirty points higher than that of whites. J.P. Wright, et al., *Prior problem behavior accounts for the racial gap in school suspensions*, 42 J. of Crim. Justice 257 (2014) ("Recent studies, for example, reveal that black youth, in comparison with their white counterparts, are often less prepared for school entry"), *available at* http://www.sciencedirect.com/science/article/pii/S0047235214000105. *See also* Katherine A. Magnuson and Jane Waldfogel, *Early Childhood Care and Education: Effects on Racial and Ethnic Gaps in School Readiness*, 15 The Future of Children 169, 183 (2005) ("the average Hispanic-white reading gap at school entry is about 0.50 of a standard deviation"), *available at* http://futureofchildren.org/futureofchildren/publications/docs/15_01_09.pdf; Monte Morin, *Study examines achievement gap between Asian American, white students*, L.A. Times, May 5, 2014 ("Even if they come from poorer, less educated families, Asian Americans significantly outperform white students by fifth grade"), http://www.latimes.com/science/sciencenow/la-sci-sn-why-do-asian-american-students-perform-better-than-whites-20140505-story.html.

32 Resource Comparability at n. 10.

33 *Id.* at 10.

34 *Id.*

35 Ricci v. DeStefano, 557 U.S. 557, 594 (2009) (Scalia, J., concurring) ("[R]esolution of this dispute merely postpones the evil day on which the Court will have to confront the question: Whether, or to what extent, are the disparate-impact provisions of Title VII of the Civil Rights Act of 1964 consistent with the Constitution's guarantee of equal protection?").

36 Regents of Univ. of Cal. v. Bakke, 438 U.S. 265, 310 (1978).

37 *Id.* at n. 40.

38 Bd. of Educ. of Okla. Pub. Schools v. Dowell, 498 U.S. 237, 250 (1991), *quoting* Green v. County Sch. Bd., 391 U.S. 237, 435 (1968)("In considering whether the vestiges of *de jure* segregation had been eliminated as far as practicable, the District Court should look not only at student assignments, but "to every facet of school operations—faculty, staff, transportation, extra-curricular activities, and facilities.").

39 Green v. County Bd. of New Kent County, 391 U.S. 430, 435 (1968). The pattern of separate 'white' and 'Negro' schools in New Kent County school system established under compulsion of state law is precisely the pattern of segregation to which Brown I and Brown II were particularly addressed, and which Brown I declared unconstitutionally denied Negro school children equal protection of the laws. Racial identification of the system's schools was complete, extending not just to the composition of student bodies at the two schools but to every facet of school operations—faculty, staff, transportation, extracurricular activities and facilities. In short, the State, acting through the local school board and school officials, organized and operated a dual system, part 'white' and part 'Negro.'

40 Dowell at 243.

41 Freeman v. Pitts, 503 U.S. 467, 495 (1992).

42 *See* Erika K. Wilson, *Toward a Theory of Equitable Federated Regionalism in Public Education*, 61 UCLA L. Rev. 1416, 1421-22 (2014).

43 Resource Comparability at 5.

44 Affirmatively Furthering Fair Housing, 80 Fed. Reg. 42272 (July 16, 2015) (to be codified at 24 CFR Parts 5, 91, 92, 570, 574, 576, and 904).

45 Kelvin Pollard and Linda A. Jacobsen, The Appalachian Region: A Data Overview from the 2007-2011 American Community Survey, Appalachian Regional Commission, at 14, 41 (Feb. 2013), http://www.arc.gov/assets/research_reports/PRBDataOverviewReport2007-2011.pdf. The Appalachian region is significantly less diverse racially and ethnically diverse than the United States as a whole, and most parts of the region have remained far below the national average in their minority populations. In two-thirds of Appalachian counties, minorities (defined as anyone who identifies with a racial or ethnic group other than "white alone, not Hispanic") made up less than 10 percent of the population during the 2007-2011 period. . . . In 23 Appalachian counties, per capita income was less than $15,000. . . . Indeed, per capita income in the 2007-2011 period was just $18,720 in rural Appalachian counties as a whole, and just $18,197 in central Appalachia.

46 San Antonio Independent School District v. Rodriguez, 411 U.S. 1 (1973).

47 Guardians Ass'n v. Civil Service Comm'n of City of New York, 463 U.S. 582, 589-90 (1983).

48 San Antonio Independent School District v. Rodriguez, 411 U.S. 1, 12-13 (1973).

49 *Id.* at 25.

50 *Id.* at 19.

51 *Id.* at 23-24.

52 Resource Comparability at 5.

53 Rodriguez at 40-41.

54 Resource Comparability at 3.

55 *Id.* at n. 10.

56 *Id.* at 3.

57 John H. McWhorter, *Explaining the Black Education Gap*, The Wilson Quarterly (Summer 2000), *available at* http://archive.wilsonquarterly.com/essays/explaining-black-education-gap. Victimologist arguments are put to a fuller test in another affluent community halfway across the country, the Cleveland suburb of Shaker Heights. The community's excellent public schools spent about $10,000 a year per student in 1998, compared with a national average of $6,842. The town is affluent and racially integrated; half of the student population is black. Students track themselves into advanced courses. There are after-school, weekend, and summer programs to help children whose grades are slipping, and a program in which older black students help younger ones. As early as kindergarten, students needing help with language arts skills are specially tutored. There are special sessions on taking standardized tests. A counselor works with students who have low grades but appear to have high potential. Shaker Heights is beautifully tailored to helping black students, and one would be hard pressed to call the black families sailing through these wide streets in their Saturns and Toyotas "struggling blue collar." Yet in four recent graduating classes, blacks constituted just seven percent of the top fifth of their class—and 90 percent of the bottom fifth. Of the students who failed at least one portion of the ninth-grade proficiency test, 82 percent were black.

58 U.S. Dep't of Educ., Office of Civil Rights, and U.S. Dep't of Justice, Dear Colleague Letter: Nondiscriminatory Administration of School Discipline (Jan. 8, 2014), *available at* http://www2.ed.gov/about/offices/list/ocr/letters/colleague-201401-title-vi.html. The Civil Rights Data Collection, conducted by OCR, has demonstrated that students of certain racial or ethnic groups tend to be disciplined more than their peers. For example, African-American students without disabilities are more than three times as likely as their white peers without disabilities to be expelled or suspended. Although African-American students represent 15% of students in the CRDC, they make up 35% of students suspended once, 44% of those suspended more than once, and 36% of students expelled. Further, over 50% of students who were involved in school-related arrests or referred to law enforcement are Hispanic or African-American.

59 J.P. Wright, et al., *Prior problem behavior accounts for the racial gap in school suspensions*, 42 J. of Crim. Justice 257, at 258 (2014), *available at* http://www.sciencedirect.com/science/article/pii/S0047235214000105.

60 *Id.* at 263.

61 The school district in Freeman v. Pitts, 503 U.S. 467, 482 (1992), faced a similar problem in achieving racial balance in its faculty. The District Court found the crux of the problem to be that DCSS has relied on the replacement process to attain a racial balance in teachers and other staff and has avoided using mandatory reassignment. DCSS gave as its reason for not using mandatory reassignment that the competition among local school districts is stiff, and that it is difficult to attract and keep qualified teachers if they are required to work far from their homes. In fact, because teachers prefer to work close to their homes, DCSS has a voluntary transfer program in which teachers who have taught at the same school for a period of three years may ask for a transfer. Because most teachers ask to be transferred to schools near their homes, this program makes compliance with the objective of racial balance in faculty and staff more difficult.

62 Resource Comparability at 3-4.

63 *Id.*

64 Sander and Taylor, *supra* note 31, at 52-53; 74-75.

65 *Id.* at 47 ("[W]hen Elliott and Strenta looked closely at the data, they realized that the distinguishing characteristic of students who fell away from science was not their race but rather the weakness of their academic preparation."); *id.* at 48-49; *id.* at 74-75 ("[O]ne of my students wondered whether older white students (whom law schools often gave admissions to in pursuit of a different kind of diversity) might also encounter mismatch problems. The BPS allowed us to identify the age of students and confirm that, indeed, a larger percentage of older white students were attending schools with credentials a good deal lower than their classmates. Yes, they had disproportionate trouble on the bar. And yes, when we controlled for mismatch, the difference in performance disappeared. Poor outcomes were not a function of age, race, or any other group characteristic—it was about large preferences.").

Anecdotes as Evidence: Proving Public Contracting Discrimination in a Strict Scrutiny World

*By John Sullivan**

Note from the Editor:

This article is about the use of anecdotal evidence to justify racial preferences in public contracting under *City of Richmond v. Croson*. As always, the Federalist Society takes no position on particular legal or public policy matters. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. But when we do, as here, we will offer links to other perspectives on the issue, including ones opposed to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• *Disparity Studies as Evidence of Discrimination in Federal Contracting*, U.S. Commission on Civil Rights (May 2006), http://www.usccr.gov/pubs/DisparityStudies5-2006.pdf.

• Ian Ayres and Fredrick E. Vars, *When Does Private Discrimination Justify Public Affirmative Action?*, 98 Colum. L. Rev. 1577 (1998), *available at* http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=2256&context=fss_papers.

• Vin Gurrieri, *DOD, SBA Urged To Overturn Minority Contracting Program*, Law360 (May 16, 2014), http://www.law360.com/articles/538449/dod-sba-urged-to-overturn-minority-contracting-program.

The perception is just there that if you're Black or if you're a woman you probably don't know how to do X, Y and Z type of work. So they've already put [you] in that pigeonhole.[1]

This excerpt is typical of the anecdotal evidence which has appeared in hundreds of disparity studies since the United States Supreme Court's decision in *City of Richmond v. Croson*, the landmark case regarding race conscious procurement programs.[2] In *Croson*, the Supreme Court struck down Richmond's public contracting racial preference, in part because the city's anecdotal evidence of racial discrimination was insufficient to withstand scrutiny under the Equal Protection Clause. The city's anecdotal evidence was testimony offered at a public hearing. Anecdotal evidence consists primarily of personal accounts of discrimination told from the perspective of the person claiming discrimination. This article examines the use and misuse of anecdotal evidence in public contracting discrimination cases since *Croson.*

Part I of the article examines *Croson,* a landmark civil rights decision about racial preferences in public contracting. Part II discusses how the *Croson* decision caused the proliferation of disparity studies, and the fact, often misunderstood by courts, that the *government* bears the burden of justifying preferences in a court challenge to the constitutionality of a public contracting program. Part III analyzes lower court decisions evaluating anecdotes and points out two common flaws of anecdotal evidence: interviewer bias and response bias. Part IV addresses the central issue with the sufficiency of anecdotal evidence: whether anecdotal claims of discrimination must be corroborated, or whether perceptions of discrimination are sufficient to justify preferences. Courts are split on this issue. Some circuits have rejected the need for verification because they do not think sufficient public policy arguments for requiring verification have been offered. This article argues in Part V that investigation and corroboration of anecdotal evidence is required, and it offers three public policy arguments for this conclusion.

I. *City of Richmond v. Croson*

Croson's path to the Supreme Court began in 1983, when the city of Richmond, Virginia began to set aside 30% of its contract dollars for Minority Business Enterprises (MBEs).[3] Six months later, the J.A. Croson Company was the low bidder on a project to install urinals in the city jail. The company, a white male-owned mechanical plumbing and heating contractor, was denied the construction contract because it did not meet the required MBE participation goal. Croson filed suit. The case bounced around the federal district and circuit courts for six years, eventually reaching the United States Supreme Court.[4]

In January 1989, the Court ruled 6-3 that the MBE set-aside requirement violated Croson's right to equal protection under the 14th Amendment, Section 1, which mandates that "No state shall…deny to any person within its jurisdiction the equal protection of the laws."[5] The Equal Protection Clause of the 14th Amendment is an individual right, guaranteed regardless of an individual's race, ethnicity or sex, so Croson could claim its protection even though he was not a racial minority.[6]

Justice Sandra Day O'Connor, writing for the plurality in *Croson*, noted that Richmond had offered "no evidence that qualified minority contractors have been passed over for City contracts or subcontracts."[7] Nor had the city presented any evidence about how many MBEs were in the relevant market and how many city dollars these firms had received. Discrimination against MBEs should have been carefully identified, but was not.[8] Also, there was no evidence of discrimination against the various minority groups Richmond had included in its preferential program.[9] *Croson* explicitly condemned any non-remedial purpose for preferences, saying

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that "Classifications based on race carry a danger of stigmatic harm. Unless they are strictly reserved for remedial settings, they may in fact promote notions of racial inferiority."[10] The *Croson* Court did not eliminate preferences in public contracting, but it did limit their use to the "extreme case" where patterns of deliberate exclusion are shown.[11]

The *Croson* Court established that racial preferences in public contracting are analyzed under strict scrutiny, and therefore that both a compelling governmental interest and narrow tailoring are required. As Justice O'Connor explained, "[p]roper findings in this regard are necessary to define both the scope of the injury [compelling interest] and the extent of the remedy necessary to cure its effects [narrow tailoring]."[12]

The Court also discussed the relevance of anecdotal evidence, stating that anecdotal evidence "of a pattern of individual discriminatory acts can, if supported by appropriate statistical proof, lend support to a government's determination that broader remedial relief is justified."[13] However, the Court did not specifically define the methodology that would characterize proper anecdotal evidence in these cases. This article recommends methodological guidelines for obtaining reliable anecdotal evidence.

II. *Croson*-Proofing Preference Programs Through Disparity Studies

Following the *Croson* decision, many states, cities, counties, and local agencies commissioned disparity studies in order to produce the strong basis in evidence needed for their preference programs to withstand strict scrutiny.[14] One law journal article referred to this as "*Croson*-proofing" the preference programs.[15]

As a result of *Croson*, government entities began to conduct disparity studies to justify their use of preferences in awarding contracts. Disparity studies have been described as "the strange fruit of the most significant civil-rights decision of the 1980s, *City of Richmond v. Croson*."[16] The decision requires "proper findings" of discrimination to justify racial preferences, and such findings are offered in disparity studies. The contents and methodological approaches of disparity studies vary widely, but they all have statistical analyses of availability of MBEs, and nearly all contain anecdotal sections as well.[17]

The anecdotal evidence that appears in disparity studies is obtained through a variety of sources, including public hearings, interviews, focus groups, and surveys by both mail and telephone. Sometimes the anecdotal evidence is quantitatively summarized, sometimes it is paraphrased without context, and sometimes it appears in the form of verbatim excerpts. Rarely are any of the anecdotal sources named in disparity studies, forcing governments and courts to evaluate the validity of anonymous allegations of discrimination.

Disparity studies generally categorize anecdotes. The October 24, 2014 "State of Missouri Disparity Study" is typical, and includes these categories: unequal access to industry and information networks, discriminatory attitudes and negative perceptions of competence, obtaining private sector work on an equal basis, and obtaining private sector work or "no goals" work on an equal basis.[18] The anecdotes often refer to a survey respondent's or interviewee's negative experiences in the procurement process. That negative bias may reflect reality, or it may reflect the kinds of people who choose to respond to the survey, or it may even result from editorial decisions by the study authors. Because there is rarely a third party check on the representativeness of anecdotes used in a disparity study, the study authors control the narrative.

A. Anecdotal Evidence and Strict Scrutiny

Anecdotal evidence in disparity studies has been offered to satisfy both prongs of strict scrutiny: compelling interest and narrow tailoring. For state and local governments to demonstrate a compelling interest in maintaining a racial preference, they must satisfy two conditions. First, the government must identify the discrimination it seeks to remedy, whether public or private, with enough specificity to at least approach a prima facie case. This is accomplished by showing that the government actively or passively participated in the discrimination in the local market.[19] Second, there must be a strong basis in evidence to support the conclusion that remedial action is necessary.[20] Remedial action addressing the present effects of identified past discrimination is the only compelling interest that can justify the use of preferences in public contracting.[21]

Engineering Contractors of South Florida v. Metropolitan Dade County is one of the leading lower court cases on the sufficiency of anecdotal evidence.[22] The record in that case contained anecdotal complaints of discrimination by MWBEs. These anecdotes described, among other things, incidents in which suppliers quoted higher prices to MWBEs than to their non-MWBE competitors, and in which non-MWBE prime contractors unjustifiably replaced a MWBE subcontractor with a non-MWBE subcontractor.[23] These kinds of anecdotes go to the compelling interest prong of strict scrutiny.

Even where a government shows a compelling interest, it is still constrained in how it may pursue that valid end. The means "chosen to accomplish the [government's] asserted purpose must be specifically" and narrowly tailored to accomplish the compelling interest.[24] The purpose of the narrow tailoring requirement is to ensure that "the means chosen 'fit' … the compelling goal so closely that there is little or no possibility that the motive for the classification was illegitimate racial prejudice or stereotype."[25]

There are six requirements to show narrow tailoring in cases involving racial preferences in public contracting: (1) the program's MWBE group classifications cannot be overly inclusive;[26] (2) the program must show that race neutral alternatives have been tried, evaluated, and found insufficient;[27] (3) the program's goals must be related to the actual availability of MWBE firms;[28] (4) the program and its MWBE goals must not create an undue burden on third parties; (5) the preferences must be shown to be necessary; and (6) the program must be flexible and have adequate waiver provisions.[29]

In *Rowe v. North Carolina Department of Transportation*, the Fourth Circuit found that evidence from a telephone survey, personal interviews, and focus groups was strong evidence of discriminatory treatment of African American and Native American firms.[30] Based on this anecdotal evidence (coupled with statistical evidence), the court ruled that contracting preferences for those two groups were justified, but that

preferences which had been in force for other MWBE groups were not justified.[31] The result that some minority groups remain in the MWBE program while others are removed from the program is an application of the narrow tailoring requirement that a program's MWBE classifications not be overinclusive.

B. Allocating the Burden

Although preferential programs supposedly supported by disparity studies have often been challenged, courts are still confused on the issue of which party bears the burden in this type of constitutional litigation. Determining who bears the burden is a three-step analytic process; courts typically get the first two steps correct and ignore the third.

Courts have properly held that, where a government has implemented a preferential program, the government bears the initial burden of showing a strong basis in evidence (typically through a disparity study) to support its program; the evidence must show that the groups who will benefit from the preferential program have suffered from patterns of discrimination against them in public contracting that should be remedied by the preference.[32] After the government makes this initial evidentiary showing, the burden shifts to the plaintiff to rebut that showing.[33] This is usually done by attacking the sufficiency of the statistics and anecdotes in the disparity study. Lower courts usually correctly require litigants to meet these two burdens.

In any equal protection action questioning the constitutionality of racial or gender preferences, it is the defendant-government that bears the third and ultimate burden of proving that its preferences satisfy the appropriate level of scrutiny (strict for race, intermediate for gender).[34] In *Johnson v. California*, a case involving race-based assignments of prisoners to cells, the Supreme Court declared, "We put the burden on state actors to demonstrate that their race-based policies are justified."[35] In *United States v. Virginia*, a case involving differing treatment for men and women, the Court placed the "burden of justification" for the differing treatment of the sexes on the government.[36] The Ninth Circuit correctly placed the burden of justification on the government in *Western States Paving v. Washington State Department of Transportation*, but lower courts usually err by placing the final burden on plaintiffs.[37]

III. The Sufficiency of Anecdotal Evidence

A. Anecdotes Alone Are Never Enough

In all the many challenges to preferential programs, no race conscious program has ever been upheld solely on the basis of anecdotal evidence.[38] In *Coral Construction v. King County*, the Ninth Circuit noted that 57 affidavits from MWBEs alleging discrimination were not sufficient to establish the constitutionality of the preference because, "[w]hile anecdotal evidence may suffice to prove individual claims of discrimination, rarely, if ever, can such evidence show a pattern of discrimination necessary for the adoption of an affirmative action plan… the MBE program cannot stand without a proper statistical foundation."[39]

However, anecdotal evidence "nevertheless is essential if a government is to defend a MBE program successfully."[40] This is because disparity ratios alone cannot identify the source of the discrimination, if any, and a preferential program in government contracts cannot remedy a problem if its source is unknown. Regression analysis, a statistical tool found in many disparity studies, suffers from this same flaw of being unable to identify the source of a problem.[41]

B. Croson*'s Progeny on Anecdotes*

Since *Croson* did not address anecdotes at any serious length, its lower court progeny must provide guidance.[42] The two leading cases on anecdotal evidence are *Engineering Contractors of South Florida v. Metropolitan Dade County*[43] and *Associated General Contractors v. City of Columbus*.[44] These two cases offer the most thorough analyses of standards for anecdotal evidence.

The district court in *Engineering Contractors* struck down Dade County, Florida's MBE and WBE programs, declaring that the county's statistical[45] and anecdotal[46] evidence was too weak to survive strict scrutiny. The court concluded that the anecdotal evidence offered could not cure the weaknesses of the statistical evidence because the anecdotal evidence showed something more akin to societal discrimination that was "not the sort of 'identified discrimination' contemplated by *Croson*."[47] Concerning anecdotes, the district court in *Engineering Contractors* stated:

> Plaintiffs respond with several points the Court believes to be valid concerning the reliability of this anecdotal evidence. First, whether discrimination has occurred is often complex and requires a knowledge of the perspectives of both parties involved in an incident as well as knowledge about how comparably placed persons of other races, ethnicities, and genders have been tested. Persons providing anecdotes rarely have such information. Attributing an incident to discrimination when the practice is just aggressive business behavior, barriers faced by all new or small businesses, or bad communication is always a possibility . . . . individuals who have a vested interest in preserving a benefit or entitlement may be motivated to view events in a manner that justifies the entitlement. Consequently, it is important that both sides are heard and that there are other measures of the accuracy of the claims. Attempts to investigate and verify the anecdotal evidence should be made.[48]

More specifically, the *Engineering Contractors* court focused on three issues: interviewer bias, response bias, and verification of anecdotes. After addressing the first two issues in this section, this article will go on to address the third in Part IV.

1. Interviewer Bias

According to the *Engineering Contractors* district court, interviewer bias could occur when the interviewer either phrases questions in a suggestive manner or implies the political purpose of the question to the respondent.[49] This problem can also arise where there are only questions about discrimination and not about difficulties arising from nondiscriminatory factors.[50]

The other leading case on anecdotal evidence is *Associated General Contractors of America v. City of Columbus.*[51] Like the district court in *Engineering Contractors*, the district court in *Columbus* addressed interviewer bias, insisting that

"investigators should be impartial and unbiased and they should be reasonably thorough and diligent."[52] The court further warned that "investigators should consider the credibility and potential bias of witnesses and respondents."[53] After an extensive discussion of the anecdotal evidence before it, the court ruled that the Columbus MWBE program failed to meet the Equal Protection requirements of *Croson*. The ruling presents a thorough evaluation of the statistical and particularly the anecdotal evidence.[54] The anecdotal evidence under review in the case was extensive and included a disparity study. Nevertheless, the court declared that the anecdotal evidence was "poorly executed" and "fell far short of proof of pervasive discrimination in the private sector."[55]

2. Response Bias

Response bias becomes a concern when a sample of respondents is not carefully constructed and consequently is unrepresentative of all potential respondents. As the court in *Engineering Contractors* observed, this may occur because the people most likely to respond to surveys are those who feel most strongly about the problem under review.[56] Anecdotes might be motivated by the knowledge that the continuing use of preferences is dependent on "their ability to create a record of discrimination" such that "the incentive to engage in memory contrivance, consciously or unconsciously, is substantial."[57] Investigation could well determine if memory contrivance has occurred. George LaNoue, Professor of Political Science at University of Maryland, Baltimore County, has noted that, "[w]here vested interests are so clear and constitutional rights are at stake, the researcher's need to use careful methodologies and to report only verified information is strong. Unfortunately, disparity studies do not meet the test."[58]

The *Columbus* opinion expressed a similar concern: "Extra care should be taken in gathering and evaluating anecdotal evidence from advocates of race- and gender-based preferences. Such informants may be prone to exaggerate or fabricate circumstances and events or omit important details."[59] One way to take the "extra care" is to ensure that those questioned "include a fair sampling of all segments of the community who have relevant knowledge and who would be impacted by such legislation."[60]

IV. Verification of Anecdotes

The problems of interviewer bias and response bias can be most effectively addressed by verification of the anecdotal evidence. Anonymous, unverified anecdotes are at best hearsay evidence. Anecdotes of discrimination should be corroborated:

> As the Dade County and Columbus cases make clear, it can be fundamentally important for jurisdictions to demand that [disparity study] consultants diligently seek to verify individuals' accounts of discrimination. Adequate verification will require consultants to approach the task with skepticism. They should assess the perspectives of parties accused of discriminatory acts, and consider potential nondiscriminatory explanations.[61]

In *Engineering Contractors,* Dade County offered anecdotal evidence in two forms: testimony from program staff and the results of a survey of black-owned firms.[62] The court pointed out that the anecdotal evidence offered in *Engineering Contractors* needed to be investigated and verified; otherwise, "[w]ithout corroboration, the Court cannot distinguish between allegations that in fact represent an objective assessment of the situation, and those that are fraught with heartfelt, but erroneous, interpretations of events and circumstances."[63] Anecdotal claims of discrimination can be unreliable, so they should "be treated cautiously" due to the inherent difficulty in verifying that they are being "remembered, perceived, or reported accurately."[64] Even if accurate, anecdotal allegations of discrimination are suspect because they may be anomalous and reflect no pattern of discrimination such as might justify a preference program. In such cases, the compelling interest prong of strict scrutiny has not been met. The possibility of response bias may make anecdotal evidence unreliable.

The *Columbus* opinion shares *Engineering Contractors*' concerns about the need for verification. The court maintained that "attempts should be made to verify claims of discrimination where it is reasonable to do so," and insisted that for anecdotal evidence to be persuasive, the collection of the anecdotes must meet "minimum standards of objectivity and diligence."[65] In a somewhat exasperated tone, the court went on to say that investigators should ask the same sorts of questions "any first-year journalism student knows to ask: 'who, what, when, where, why and how?'"[66] The court was also worried that the anecdotal evidence incorrectly emphasized *perceptions* of discrimination, rather than *actual* discrimination.[67]

One federal court has considered the specific problem of whether *perception* of discrimination is sufficient to support racial preferences. The court in *Phillips & Jordan v. Watts* emphatically rejected perceptions as evidence of discrimination when it pointed out that:

> Individuals responding to FDOT's [Florida Department of Transportation] telephone survey have described their *perceptions* about barriers to FDOT's bidding procedures. But FDOT has provided no *evidence* to establish who, if anyone, in fact engaged in discriminatory acts against Black and Hispanic businesses. The record at best establishes nothing more than some ill-defined wrong caused by some unidentified wrongdoers; and under *City of Richmond* [v. *Croson*] that is not enough![68]

Other courts have disagreed with the *Engineering Contractors*, *Columbus*, and *Phillips* & *Jordan* decisions, ruling instead that it is not necessary to investigate and possibly verify allegations of discrimination. For these courts, perceptions of discrimination are sufficient to justify preferences. In *Concrete Works v. City and County of Denver*, the Tenth Circuit held that "Denver was not required to present corroborating evidence and [the plaintiff] was free to present its own witnesses to either refute the incidents described by Denver's witnesses or to relate their own perceptions on discrimination in the Denver construction industry."[69] The Tenth Circuit opinion assumes, at the very least, that depositions can be taken of those anecdotal witnesses claiming discrimination as part of the disparity study, or that these witnesses could be cross examined at trial. The financial burden on the plaintiff to pursue these paths to question the witnesses claiming discrimination could well prove

to be overwhelming.

The Fourth Circuit in *H.B. Rowe Company v. Tippett* found that the State's anecdotal evidence of discrimination against African American and Native American subcontractors, obtained through telephone surveys, sufficiently supplemented the statistical evidence to justify preferences for these two groups.[70] The court ruled that the telephone survey exposed an informal, racially exclusive network which systematically disadvantaged the two groups.[71] The court felt confident to rule this way since no public policy reasons were presented as to why the unverified survey answers might be untrustworthy. The court specifically rejected the requirement that anecdotal evidence be investigated or corroborated.[72] The Fourth Circuit stated that:

> Rowe offered no rationale as to why a fact finder could not rely on the State's "unverified" anecdotal data. Indeed, a fact finder could very well conclude that anecdotal evidence need not–and indeed cannot–be verified because it "is nothing more than a witness' narrative of an incident told from the witness' perspective and including the witness' perceptions."[73]

In contrast, a disparity study company has recognized the potential problems with perceptions of discrimination. The 1993 MGT disparity study for the North Carolina Department of Transportation, the same agency whose preferences were at stake in *Rowe*, includes this cautionary statement: "Firms and individuals who lose contracts no doubt sometimes believe they were discriminated against even when no discrimination exists."[74]

V. Public Policy Reasons for Requiring Verification of Anecdotes

Are there rationales for demanding that perceptions of discrimination be verified in order to satisfy strict scrutiny? Why should investigation and corroboration of anecdotal claims of discrimination be necessary? The court in *Engineering Contractors of South Florida v. Dade County* warned that there are costs of accepting unverified anecdotes:

> Without corroboration, the Court cannot distinguish between allegations that in fact represent an objective assessment of the situation, and those that are fraught with heartfelt, but erroneous, interpretations of events and circumstances. *The costs associated with the imposition of race, ethnicity, and gender preferences are simply too high* to sustain a patently discriminatory program on such weak evidence.[75]

First, it is a matter of basic fairness that any preferential program which disadvantages some people according to their race, ethnicity, and gender while advantaging others should only be implemented where discrimination has been shown to be real, and not simply perceived. Unless they are investigated, these anecdotal accounts remain mere perceptions of discrimination. Political scientist Mitchell Rice has observed that "[a]necdotal evidence, interviews and affidavits must be from reliable and trustworthy sources and should include counter explanations and rebuttals from sources accused of bias. In other words, the gathering of evidence utilizing these approaches must be fair and deliberative."[76]

Second, unless the claims of discrimination can be verified, the right remedy to that discrimination cannot be fashioned. To find and implement the most effective remedy, perception must be distinguished from reality. For example, consider a situation in which a telephone survey includes a MBE owner's claim that he was denied a bank loan due to discrimination, but investigation of the claim would have revealed that he had a faulty business plan and prior bankruptcy? Simply accepting this perception of discrimination as accurate would mean the most effective remedy–one which addresses the business plan and bankruptcy—would never happen. The district court in *Associated General Contractors of Connecticut v. New Haven* addressed this need to connect evidence of discrimination to its proper remedy.[77] The court discussed a number of anecdotal complaints of discrimination, such as having tools stolen, being harassed, having difficulty in obtaining loans, enduring animus on the part of trade unions, and problems in training, bonding, or insurance, but concluded that these anecdotes did "not rise to the level of showing a systematic pattern of discrimination to the exclusion of any other explanation."[78]

Third, strict scrutiny demands investigation of anecdotal claims of discrimination. Consider the following hypothetical. Two cars collide at an intersection. The police arrive and take statements from both drivers. Unsurprisingly, each claims the other is at fault. The police would investigate. Are there skid marks to support Mr. Smith's claim that he braked suddenly to avoid the other car running a stop sign? Ms. Jones claims she saw the other driver on a cell phone; is a cell phone visible? For that matter, is there a stop sign? Has either party been drinking alcohol? What were the weather and road conditions? The police and involved insurance companies would undoubtedly investigate in order to determine fault.

Now, vary the hypothetical to include this single claim: Mr. Smith alleges Ms. Jones deliberately hit him because she is a racist. Should Ms. Jones be convicted of a hate crime on the basis of his accusation alone? Shouldn't that claim of discriminatory action be investigated if at all possible? If a fender bender is thoroughly investigated, doesn't strict scrutiny require investigation of claimed discrimination when the constitutional rights of others to not be disadvantaged because of race are at stake? There is at present no consistently applied judicial approach to the verification of anecdotes on the discrimination issue. Consistency is certainly needed. Once courts have been presented with the public policy reasons for verification offered in this article, as the Fourth Circuit in *Rowe* requested, that inconsistency may change.

VI. Conclusion

The 1989 Supreme Court decision *City of Richmond v. Croson* is a landmark civil rights ruling. *Croson* launched the disparity study industry, which arose as governments attempted to meet *Croson*'s requirement that discrimination be identified with enough specificity so that effective remedies could be fashioned. When disparity studies are challenged in court, the burden of justification should be on the government. Virtually all disparity studies contain anecdotal accounts of discrimination, which can be more or less reliable depending

on the extent to which anecdotes are investigated. Verification of anecdotal evidence supporting racial preferences is a matter of fairness to those who are disadvantaged by those preferences. Without verification, the right remedy for discrimination cannot be fashioned.

Endnotes

1 Colette Holt & Associates, *State of Missouri Office of Administration Disparity Study* (2014), 110, *available at* http://oeo.mo.gov/wp-content/uploads/2011/09/2014-State-of-Missouri-Office-of-Administration-Disparity-Study.pdf.

2 488 U.S. 469 (1989).

3 Related acronyms which appear in this article are MWBE (minority and/or women-owned business enterprise); WBE (women-owned business enterprise); and DBE (disadvantaged business enterprise).

4 Croson, 488 U.S. at 477.

5 Similarly, the Due Process Clause of the Fifth Amendment of the United States Constitution, into which Equal Protection principles have been incorporated, protects an individual's right to due process of the law: "No person shall be . . . deprived of life, liberty, or property without due process of law." The obligations imposed by the Fifth and Fourteenth Amendments are indistinguishable. Adarand v. Peña, 515 U.S. 200 (1995).

6 Adarand, 515 U.S. at 224.

7 Croson, 488 U.S. at 510.

8 *Id.* at 497.

9 *Id*. at 506. The *Croson* court declared that the city had no evidence of past discrimination against "Spanish-speaking, Oriental, Indian, Eskimo, or Aleut persons in any aspect of the Richmond construction industry." The Court elaborated: "The random inclusion of racial groups that, as a practical matter, may never have suffered discrimination in the construction industry in Richmond, suggests that perhaps the city's purpose was not in fact to remedy past discrimination. If a 30% set-aside was 'narrowly tailored' to compensate black contractors for past discrimination, one may legitimately ask why they are forced to share this 'remedial relief' with an Aleut citizen who moves to Richmond tomorrow?" *Id.*

10 *Id.* at 493.

11 *Id.* at 509.

12 *Id.* at 506, 510.

13 *Id.* at 509.

14 As of December 2014, more than 350 disparity studies had been released, according to a list compiled by the Project on Civil Rights and Public Contracting. The estimated total cost of these studies likely exceeds $150 million.

15 Docia Rudley & Donna Hubbard, *What a Difference a Decade Makes: Judicial Response in State and Local Minority Business Set-asides Ten Years After* City of Richmond v. J.A. Croson, 25 S. Ill. U. L.J. 39, 42 n.17 (2000).

16 George R. LaNoue, *Social Science and Minority "Set-Asides,"* 110 *The Public Interest* 49, 49 (Winter 1993).

17 One circuit court has referred to this variety as an "evidentiary mosaic." Concrete Works of Colorado, Inc. v. City of Denver, 36 F.3d 1513, 1520 (10th Cir. 1994). In the early years after *Croson*, disparity studies often had historical sections, though such sections are rare today. George LaNoue, *Selective Perception: The Role of History in the Disparity Study Industry*, 17 The Public Historian 2 (Spring 1995).

18 *See supra* note 1 at 109-16 (Qualitative Evidence of Race and Gender Barriers in the Missouri Economy).

19 Croson, 488 U.S. at 492, 499-500.

20 *Id.* at 500, *quoting* Wygant v. Jackson Bd. of Educ., 476 U.S. 267, 277 (1968).

21 *Id.* at 493. In public education, by way of contrast, preferences may also be justified by a desire for diversity.

22 943 F. Supp. 1546 (S.D. Fla 1996).

23 *Id.* at 1579.

24 Shaw v. Hunt, 517 U.S. 899, 908 (1996).

25 Croson, 488 U.S. at 493.

26 A preferential program is narrowly tailored only if its application is limited to those groups which have actually suffered discrimination. Otherwise, the program provides MWBE groups who have not encountered discriminatory barriers with an unconstitutional competitive advantage at the expense of both non-MWBEs and women or minority groups that have been actual victims of discrimination.

27 On the narrow tailoring facet of race neutral alternatives, Supreme Court jurisprudence has advanced substantially in the 25 years since *Croson*. *Grutter v. Bollinger*, decided in 2003, declared that racial preferences will only be permitted for another 25 years, at most. 539 U.S. 306, 342 (2003). By the end of 2028, preferences will be unconstitutional, and only race neutral alternatives will be allowed.

28 In *Croson*, Justice O'Connor supplied the statistical test which a jurisdiction should use as its beginning point for the kind of proper findings which would determine whether patterns of discriminatory exclusion have been identified: "Where there is a significant statistical disparity between the number of qualified minority contractors willing and able to perform a particular service and the number of such contractors actually engaged by the locality or the locality's prime contractors, an inference of discriminatory exclusion could arise*."* Croson, 488 U.S. at 509-10.

29 United States v. Paradise, 480 U.S. 149, 171 (1987).

30 615 F.3d 233 (4th Cir 2010).

31 *Id.* at 251.

32 *See, e.g.*, Rothe Development Corporation v. Department of Defense, 545 F.3d 1023, 1036 (Fed. Cir. 2008); Monterey Mechanical Company v. Wilson, 125 F.3d 702, 713 (9th Cir. 1997); Hershell Gill Consulting Engineers, Inc. v. Miami Dade County, 333 F.Supp. 2d 1305, 1316 (S.D. Fla. 2004).

33 Engineering Contractors, 122 F.3d at 916.

34 Gratz v. Bollinger, 539 U.S. 244, 270 (2003). In *Gratz* the Court held that the admissions program used by the University of Michigan's College of Literature, Science and the Arts violated the Equal Protection Clause, Title VI of the Civil Rights Act of 1964, and 42 U.S.C. § 1981.

35 543 U.S. 499, n.1 (2005).

36 518 U.S. 515, 553 (1996).

37 407 F.3d 983 (9th Cir. 2005).

38 "Anecdotal evidence" includes trial testimony, evidence at trial, and anecdotal material in disparity studies.

39 941 F.2d 910, 919 (9th Cir. 1991).

40 Jeffrey Hanson, *Hanging by Yarns: Deficiencies in Anecdotal Evidence Threaten the Survival of Race-Based Preference Programs for Public Contracting*,

88 Cornell L. Rev. 1433, 1447-48 (2002).

41 *See, e.g.*, NERA Economic Consulting, *The State of Minority- and Women-Owned Business Enterprise: Evidence from New York* (April 2010), 139-86, *available at* http://www.esd.ny.gov/MWBE/Data/NERA_NYS_Disparity_Study_Final_NEW.pdf.

42 There seems to be a conflict among the circuits on the issue of whether appellate review of a strong basis in evidence, which includes reviewing anecdotes, is treated as a factual determination not to be overturned by the circuit court unless clearly erroneous (Engineering Contractors Association of South Florida v. Metropolitan Dade County, 122 F.3d 895, 903 (11th Cir. 1997)) or whether the strong basis in evidence is a legal determination to be reviewed de novo (Concrete Works of Colorado v. City of Denver, 321 F.3d 950, 958 (10th Cir. 1996)).

43 943 F. Supp. 1546.

44 936 F. Supp. 1363 (S.D. Ohio 1996), *vacated on jurisdictional grounds by* 172 F.3d 411 (6th Cir. 1999) (unconstitutionality of the Columbus MWBE preference on construction contracts undisturbed).

45 943 F. Supp. at 1560-77.

46 *Id.* at 1577-80.

47 *Id.* at 1580. On appeal, the Eleventh Circuit affirmed the district court's ruling without commenting directly on the district court's extensive criticisms of the anecdotal evidence. *Engineering Contractors*, 122 F.3d 895. The appeals court included a brief discussion of the anecdotal evidence because the County's statistical evidence was weak, and the court noted that "only in the rare case will anecdotal evidence suffice standing alone." *Id.* at 925.

48 943 F. Supp. at 1579.

49 *Id.*

50 Susan A. MacManus, *Minority Business Contracting with Local Government*, 25 Urb. Aff. Q. 455 (1990).

51 936 F. Supp. 1363.

52 Columbus, 936 F. Supp. at 1426.

53 *Id.* at 1428.

54 The court issued a 71 page opinion and 20 page appendix. The discussion of the anecdotal material runs more than 40 pages.

55 936 F. Supp. at 1373. The appeals court praised the extensiveness of the lower court's opinion: "The record in this case is voluminous and the district court's effort in reviewing that record and issuing its ruling was thorough and exhaustive."

56 943 F. Supp. at 1579.

57 George R. LaNoue, *Standards for the Second Generation of* Croson-*Inspired Disparity Studies*, 3 *The Urban Lawyer* 485, 524 (Summer 1994).

58 *Id*. at 525.

59 936 F. Supp. at 1426.

60 *Id.*

61 Hanson, *supra* at 1468-69.

62 943 F. Supp. at 1546, 1577-1580.

63 *Id.* at 1579.

64 LaNoue, *Standards for the Second Generation of* Croson-*Inspired Disparity Studies*, *supra* at 525.

65 936 F. Supp. at 1426.

66 *Id.*

67 *Id.* at 1373.

68 13 F. Supp. 2d 1308 (N.D. Fla. 1998) (emphasis in original).

69 321 F.3d 950, 989 (10th Cir. 2003).

70 Rowe, 615 F.3d at 250.

71 *Id*. at 251.

72 *Id.*, *quoting* Concrete Works, 321 F.3d at 989.

73 *Id.* at 249.

74 MGT of America, Inc., *Study of Minority and Women Business Participation in Highway Construction*, 7.

75 943 F. Supp. at 1584 (emphasis added).

76 Mitchell F. Rice, *Government Set-Asides, Minority Business Enterprises, and the Supreme Court*, 51 Public Adm. Rev. 2, 485 (March/April 1991).

77 791 F. Supp. 941 (D. Conn. 1992).

78 *Id.* at 948.

Criminal Law & Procedure

Interpol's Transnational Policing By "Red Notice" and "Diffusions": Procedural Standards, Systemic Abuses, and Reforms Necessary to Assure Fairness and Integrity

*By Peter M. Thomson**

Note from the Editor:

This article is about Interpol's use of Red Notices and Diffusions; it describes problems with the system and urges reforms. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. When we do so, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• *Notices*, Interpol, http://www.interpol.int/INTERPOL-expertise/Notices.

• *Interpol and the Case for Reform: Who Has Said What?*, Fair Trials International, (August 20, 2015), http://www.fairtrials.org/press/interpol-and-the-case-for-reform-who-has-said-what/.

• Shreya Dasgupta, *Interpol Rejects Malaysia's Request to Place Journalist on Red Notice List*, Mongabay, (August 31, 2015), http://news.mongabay.com/2015/08/interpol-rejects-malaysias-request-to-place-journalist-on-red-notice-list/.

• Jago Russell, *Letter to Prof. Dr. Jurgen Stock, Secretary-General of Interpol, Regarding Journalist Clare Rewcastle Brown*, Fair Trials International, (August 25, 2015), http://www.fairtrials.org/wp-content/uploads/25082015-Rewcastle-Brown-Letter.pdf.

Rasoul Mazrae, a citizen of Iran, was an outspoken critic of his government. Although his political speech would have been protected in the United States as a constitutional right, in Iran his conduct was considered a crime against the state. Fleeing his persecutors, Mazrae was taken into custody in Syria based on a wanted alert published by the International Criminal Police Organization—Interpol. He was extradited to Iran, jailed, tortured, and then sentenced to death. The wanted alert disseminated by Interpol for Mazrae's capture was a Red Notice, which under Interpol's constitution should not have been issued because Mazrae's crime was of a "political character." His case is just one example of numerous instances where Interpol's Red Notice system has been exploited by its members to locate, detain, and extradite persons for political, racial, or religious reasons. In these and even legitimate cases warranting Interpol's engagement, Red Notices come with considerable human impact. Those targeted often suffer serious financial, personal and professional harm; ultimately, they face arrest, detention, and extradition.

In many countries, Red Notices have the weight of an international arrest warrant, but they lack sufficient procedural safeguards to prevent regimes from using them to oppress, harass, and silence political and economic opponents. Even more troubling is the rise in the number of Interpol-sponsored Diffusions, which are informal electronic wanted alerts that countries are using to bypass the Red Notice system in order to achieve essentially the same goals. In fact, Diffusions are outpacing Red Notices at a rate of approximately two to one.

This article provides an overview of the procedures governing the publication of Red Notices, the legal strategies that can be employed to prevent and challenge them, the inherent flaws and systemic abuses in the Red Notice system, and possible reforms that could be implemented to improve Interpol's wanted notice system. This article also briefs the growing threat to human rights posed by Interpol's Diffusion alert and the reforms necessary to assure that fundamental due process rights of those targeted are not violated.

I. Interpol's Red Notice: Procedures and Requirements for Publication

An Interpol Red Notice seeks the provisional arrest (i.e., temporary detention) of a wanted person with a view towards extradition based on an arrest warrant or court decision issued by the requesting country.[1] Red Notices are processed through each Interpol member country's National Central Bureau (NCB)[2] and have the effect of an international wanted notice.[3] Red Notices typically contain two principal groups of information: (1) identity particulars (physical description, fingerprints, etc.) and (2) relevant judicial information (offense charged, maximum penalty, etc.).[4] Red Notices are routinely used to track and detain wanted persons whose whereabouts are unknown, particularly individuals who travel frequently through conventional means (i.e., commercial aircraft, cruise ships, trains, etc.) and who pass through official ports of entry staffed by customs or immigration personnel.[5]

The U.S. NCB within the U.S. Department of Justice provides the following guidance concerning Red Notices:

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> Red Notices are issued in order to seek the location and arrest of fugitives for the purpose of extradition. A Red Notice serves as an international wanted notice and provides information on the identification of fugitives charged with, or convicted of serious crimes. The country initiating the notice commits to seeking the provisional arrest and extradition of the fugitive in question should he or she be located.[6] A request for a Red Notice must concern a person who is the subject of an arrest warrant and is wanted for prosecution or to serve a sentence. *Approximately one-third of Interpol member countries consider a Red Notice to be a valid request for provisional arrest and will detain the subject of a Red Notice*.[7]

Most Interpol member countries commit themselves to honoring Red Notices because, generally, they are believed to be issued in compliance with both domestic and international law.[8] The ultimate goal of a Red Notice is to secure the wanted individual's extradition back to the requesting country. The most common method of extradition is by treaty between two countries.[9] However, absent proof that the foreign offense also constitutes a violation under the laws of the country in which the fugitive is located, there is no obligation to honor an Interpol Red Notice. Extradition treaties usually set forth a list of qualifying offenses. Many require "dual criminality," which means the extraditable offense's underlying conduct must also constitute a criminal offense in the country being asked to extradite.

A. A Red Notice Can Trigger a Fugitive's Provisional Arrest Pending Extradition

Once a fugitive is located pursuant to a Red Notice, the pursuing jurisdiction may follow up with a formal request that the subject be arrested and held on a provisional basis, until an extradition application can be filed through formal channels. Typically, however, a provisional arrest is requested in urgent situations where authorities believe the wanted person will flee the country before formal extradition documents can be filed and perfected. A judge or magistrate in the recipient country usually can authorize a provisional arrest only if the request legally comports with the respective extradition treaty and international law.

However, about one-third of Interpol's member countries consider a Red Notice *itself* to be the equivalent of a formal request for a "provisional arrest." Many countries, therefore, treat a Red Notice as an *actual* arrest warrant even though it is an administrative vehicle intended merely to provide "notice" that an arrest warrant has been issued by another member country.[10] The fact that some countries grant such legal status to a Red Notice guarantees that a fugitive in any of those countries will be placed immediately under provisional arrest once he has been located, and that the prosecuting jurisdiction will be informed of that fact so that the extradition process can begin.[11] This practice, of course, results in Red Notices having more of a "direct effect" in the recipient jurisdictions even when the request is not based on a previous agreement or treaty. It is important to stress that a Red Notice, although afforded such a status by some countries, is *not* the same as a request for extradition, which only takes place once a fugitive has been located and taken into provisional custody.

By contrast, federal law in the United States prohibits the arrest of an individual solely on the basis of a Red Notice. If a wanted subject is determined to be within the United States, the Criminal Division of the U.S. Department of Justice will determine whether a valid extradition treaty exists between the U.S. and the requesting country for the specified crime or crimes. If the subject is extraditable, and after a diplomatic request for a provisional arrest is received from the requesting country, the facts are communicated to the U.S. Attorney's Office in the district where the person is located. The U.S. Attorney's Office will then file a Criminal Complaint and obtain an arrest warrant requesting extradition.[12] Approximately two-thirds of Interpol member nations follow the U.S. model and only seek a person's provisional arrest after a formal request is received pursuant to an applicable treaty.

B. The General Procedural Requirements for Issuance of Red Notices

Interpol relies on its member countries to request Red Notices in compliance with Interpol's Constitution and international law. According to Interpol's stated legal basis, a Red Notice will be issued only where it fulfills "all conditions for processing the information."[13] For example, Interpol states that "a Notice will not be published if it violates Article 3 of its constitution, which forbids the organization from undertaking any intervention or activities of a political, military, religious or racial character. Notices are processed pursuant to Interpol's Rules on the Processing of Data, which ensure the legality and quality of information, and the protection of personal data."[14] Notwithstanding that Red Notices are presumed to be validly issued, on occasion they are based on inaccurate information, or even on factual and/or legal pretenses that do not meet Interpol's legal criteria. They might also be based on a criminal offense that was fabricated or mischaracterized by officials in the requesting state. Therefore, in an effort to prevent such abuses, Interpol requires that all NCB-processed applications satisfy the following criteria:

1. The penalty for the underlying offense must be at least imprisonment for one year;
2. The charging document has not been sealed; and
3. The responsible prosecutor (located in the originating country) has committed to extradite; has completed and signed a conformation of agreement to extradite; and has forwarded the agreement to the respective Interpol office with the application for Red Notice.[15]

Once the originating NCB assures the foregoing requirements have been met by the official applicant and approves the Red Notice, it forwards the application and supporting documents to Interpol's General Secretariat in Lyon, France. It is the General Secretariat's responsibility to ensure that all Red Notices meet international legal requirements prior to disbursement to member nations. Publication of a Red Notice may take several months to complete. Once approved, it is circulated worldwide to law enforcement agencies and border checkpoint locations.

C. The Role of Interpol's General Secretariat

Red Notices are processed by an ad hoc unit within the Of-

fice of the General Secretariat.[16] Occasionally, when legal issues involving Article 3 of Interpol's Constitution are implicated, Interpol's Office of Legal Affairs can also become involved in the review process. In its gatekeeping role, the General Secretariat has the responsibility of ensuring not only that Red Notices meet international legal requirements, but that they comply with Interpol's Constitution and its fundamental rules. In ensuring compliance, the General Secretariat may request that the prosecuting country address any concerns it may have of either a procedural or substantive nature and may reject the application where its publication would conflict with Interpol's rules or Constitutional principles.[17] As a threshold matter, there are three fundamental legal precepts that cannot be violated:

1. Rule of Law: A Red Notice must respect "the basic rights of individuals in conformity with . . . the Universal Declaration of Human Rights."
2. Neutrality: There can be no intervention of a "political, military, religious or racial character."
3. Legality: The General Secretariat must verify that domestic authorities process information through Interpol's communication channels in compliance with the international conventions to which they are a party, as well as "in the context of the laws existing" in their countries.[18]

In ensuring "that the conditions attached to [the given Red Notice] are met,"[19] the General Secretariat has the authority to scrutinize an application even more closely if it finds an apparent conflict with extradition law or if the charged offense appears to be of a "political" character. If the General Secretariat finds a conflict with accepted extradition law and/or international norms, or if it concludes the underlying offense is political in nature, it should decline the Red Notice application.[20] The General Secretariat also has the authority to refuse a Red Notice if it considers its publication to be "unadvisable."[21]

In the event that a Red Notice has been published without being timely challenged by an aggrieved party, however, the General Secretariat still has the authority ex officio to intervene if there is reason to believe that a violation of its constitution or governing rules has occurred. Moreover, Interpol's Executive Committee and the General Assembly also have the authority to review Red Notices following direct challenge of the issuing NCB. These two bodies serve as Interpol's dispute settlement institutions, and their decisions are reached by majority vote.[22]

II. Preventing and Challenging Red Notices

Preventing or defeating ex post the issuance of a Red Notice based on a legitimate or arguably legitimate criminal offense is an exceedingly difficult and complex process in most cases. Nevertheless, there are a number of legal and procedural options available through which one might successfully defeat a Red Notice.

First, the initial application can be challenged directly through the originating NCB in an attempt to prevent it from forwarding the Notice to Interpol's General Secretariat in Lyon, France, as long as Interpol has not yet reviewed or acted upon the Red Notice application. In such a case, the aggrieved party may file a "preemptory objection" with the NCB. Second, through local counsel, a court challenge in the originating jurisdiction can be mounted on procedural and/or substantive grounds against the application. Third, a Red Notice can be contested directly with the General Secretariat. Objections can be based on a number of procedural and substantive grounds, including violations of Interpol's constitution. Fourth, relief can be sought from Interpol's Office of Legal Affairs, also located at Interpol headquarters in France. Fifth, a "preventive request" can be filed with the Commission for the Control of Interpol's Files (CCF), Interpol's "watchdog" arm, based on violations of Interpol's constitution, rules, and/or the general law of extradition. Sixth, in the event that any or all of the above strategies fail to prevent publication of the Red Notice, an ex post challenge can be made pursuant to a formalized procedure available for its removal. This review procedure includes the filing of a complaint with Interpol's Office of Legal Counsel and the CCF, which can intercede post-publication as well on a peremptory basis.

A. Legal Arguments in Support of Red Notice Challenges

More particularly, to successfully defeat a Red Notice, evidence must be provided indicating that the request is in violation of Interpol's constitution, legal rules, and/or the general law of extradition. The following legal arguments present the strongest likelihood of success when challenging a Red Notice application:

1. The Prosecution is of a "Political Character"

Under Article 3, Interpol is strictly forbidden from intervening in matters of a "political character." The term "political character," however, is not defined by Interpol's Constitution. Where an individual is not charged with a "political" crime per se (for example, treason or sedition), a valid argument can nevertheless be presented that the prosecution *itself* is politically motivated.

2. The Criminal Charges Are Misrepresented

Misrepresentation or mischaracterization of a criminal charge against a defendant violates Interpol's rules. Accordingly, although the General Secretariat and its legal office cannot intervene to verify the guilt or innocence of a defendant, a challenge can nevertheless be made arguing that the charges have been concocted based on political and other reasons. Further, regardless of whether a mischaracterization argument can stand substantively on its own, it should be considered as an argument in support of a political challenge under Article 3.

3. A Violation of Due Process has Occurred

A challenge to a Red Notice may also be made by a claim of a due process violation. This kind of claim can also be supported with the evidence used to challenge the Red Notices based on the mischaracterization argument referenced above.

B. The CCF

The CCF, as an independent monitoring body within Interpol, is empowered to scrutinize Red Notices for compliance with the rule of law, including Interpol's specific legal requirements. If a Red Notice has not yet been filed, its intended target can file a "preventive request" so that, in the event a Red Notice is sought, "it should not be published for the alleged reasons. In

such a case, the information provided by the individual [target] could be taken into account upon reviewing the request (if submitted) and may lead to the application of the procedure in article 10.1(c) of the Processing Rules."[23]

In the event a Red Notice has actually been published and circulated worldwide, a formalized review procedure can still be initiated by the CCF. One of the CCF's primary functions is to ensure that the processing of information "conforms to all the relevant rules adopted by the Organization" and does "not infringe the basic rights of the people concerned."[24] Accordingly, the subject of an issued Red Notice may challenge its validity with the CCF, either on procedural or substantive grounds. If the CCF calls into question the processing of the Red Notice, it forwards its concerns to the General Secretariat, and the CCF may invite the General Secretariat to conduct a preliminary inquiry into the request.[25] The CCF then adopts conclusions and makes recommendations. An oral hearing into the matter with the requesting party is allowed only in exceptional cases. Otherwise, the aggrieved person is not entitled to a hearing.

As with a General Secretariat review, the CCF can only verify the validity of charges, not their accuracy.[26] The CCF cannot check or amend charges which could intrude into national sovereignty. Hence, the CCF has its limitations; it cannot assess the legal situation in a member country with a view to giving an opinion on the validity of an arrest warrant or legal decision. The CCF's power is advisory, so when doubts are raised with respect to a Red Notice, the CCF may only *recommend* that the General Secretariat proceed with caution or cancel the Notice. Further, a member state may challenge the General Secretariat's decision based on the CCF's advice, subjecting it to the dispute settlement procedure with the Executive Committee and General Assembly.

III. Interpol's "Diffusion" Alerts: Informal Alternatives to Red Notices Lacking Fundamental Procedural Safeguards

Although similar, even arguably equivalent to a Red Notice, a "Diffusion" is a less formal alternative that may be used to obtain international cooperation in locating, arresting and detaining a wanted subject. While Diffusions are not as widely known by the general public, they result in more arrests and detentions than Red Notices, without the latter's procedural safeguards (as imperfect as they might be).

Diffusions, like Red Notices, are originated by a member's NCB at the request of local authorities. Although Diffusions may be circulated worldwide over Interpol's "I-Link" network and recorded in Interpol's primary database, the requesting NCB has the same discretion as with Red Notices to limit Diffusions to select countries or police organizations of its choice.[27] This option has advantages because it permits an NCB to request foreign assistance in apprehending a wanted person without risking disclosure of its existence to a complicit member nation that might be providing aid and support to the same person. As with Red Notices, Diffusions must comply with Articles 2 and 3 of Interpol's constitution and are subject to CCF review. However, that is where the similarities end.

Whereas a Red Notice is published through Interpol's General Secretariat at the request of a member nation or an international organization, a Diffusion is published (i.e., disseminated) by a member country's NCB or by an international organization, not technically by Interpol.[28] Second, unlike with a Red Notice, there is no formal application and review process for a Diffusion seeking someone's arrest and detention. Any member NCB can issue and transmit a Diffusion within a matter of minutes, if not seconds, and once issued, a Diffusion alert remains active for at least five years. Third, a Diffusion can be disseminated to foreign police agencies of the originating NCB's choosing and, unlike a Red Notice, is not published by default to all Interpol member nations.[29] Fourth, a Red Notice application must state that a valid arrest warrant or court order exists and that the applicant country will seek extradition of the fugitive; a Diffusion, on the other hand, requires compliance only with Interpol's Rules for Processing Data. Fifth, unlike a Red Notice, a Diffusion is not automatically reviewed by the legal office of the General Secretariat prior to publication.[30] It simply is recorded in Interpol's database and distributed via its I-Link network[31] by the originating NCB. Sixth, although both Red Notices and Diffusions are required to comply with Article 3, a Diffusion can be issued without any legal review whatsoever by the General Secretariat. Finally, whereas a summary version of a Red Notice generally can be viewed by the public on the Interpol website, only authorized law enforcement personnel may view a Diffusion that seeks a person's arrest.

Although Interpol maintains that it is not technically responsible for Diffusions, the organization nevertheless plays an important role in their distribution to member nations. Notwithstanding the fact that Diffusions lack many of the procedural safeguards afforded by Red Notices, Interpol actually *encourages* its member police organizations to transmit Diffusions simultaneously with their Red Notice requests, including where the publication of a Red Notice might not be appropriate or factually justified.[32] Interpol also reviews Diffusions and takes credit for the arrests that result.[33] Therefore, although Diffusions are issued independently by member state NCBs, there is little doubt that Diffusions carry Interpol's stamp of approval and that Interpol shares responsibility for their dissemination.

IV. The Inherent Flaws and Systemic Abuses in Interpol's Wanted Notice System

The immediate and collateral consequences of being targeted by one of the thousands of Red Notices or less regulated Diffusions filed each year can be devastating to an individual, personally and professionally. The effects can be far-reaching and linger for substantial periods of time. Often the individual has not been charged with a crime that would, from a reasonable man's perspective, justify being tracked down, arrested, and jailed in a foreign country. Regrettably, once a Red Notice has issued, the target has little to no recourse against his accuser and, once detained, is subject to being extradited to the pursuing nation through a lengthy process.

Very often, the target of a Red Notice simply has no idea of the substantial risk he is taking by merely traveling between two countries. In such instances, the first notice he might receive is being swept out of a customs line and tossed into a local prison. In other instances, the target may have been apprised of his "wanted" status and fully understand the risks

he faces while traveling. For those individuals whose livelihoods require travel, an Interpol alert can result in disruption of their client base and substantial financial losses, both to the individual and his employer. Even if business travel is not required, the curtailed freedom of movement and the looming threat of arrest can be exceedingly disruptive and distressing. The person's reputation and credit rating undoubtedly will be harmed. He might become separated from his family for weeks, if not months. Further, he might find that he is unemployable, his bank accounts inaccessible, and his financial assets frozen.

Of course, there are circumstances that would justify arresting and detaining someone in a foreign country who has been legitimately charged with a serious criminal offense. Those who commit violent crimes and acts of terrorism, for example, should be subject to foreign arrest, detention, and extradition. Interpol's wanted notice system can be used legitimately to further such appropriate law enforcement goals. But far too often Red Notices are exploited for the purpose of locating and arresting someone based on weak evidence or for committing an offense for which foreign detention arguably or admittedly is inappropriate or unjustified. Under such circumstances, much of the damage is irreversible at the moment the Red Notice issues, because the process of removing a published Red Notice is difficult, complex, and time consuming.

In some cases, Interpol has taken years to retract an improperly issued Red Notice. The organization appears to lack the necessary resources, capacity, and expertise to address objections raised by targeted individuals, and there is no truly independent administrative, judicial, or parliamentary oversight. The only body claiming "independence" from Interpol and having an oversight role is the CCF, but the CCF is funded by Interpol and is part and parcel of the organization's internal legal structure. Further, in typical bureaucratic fashion, the CCF has a reputation of being slow to resolve complaints, and its investigative and decision-making process lacks transparency. Moreover, an aggrieved party has no right to a hearing, and the CCF typically does not provide detailed explanations for its decisions, from which there is no right to appeal.

Some have suggested that Interpol's fundamental problem is that it operates on a theory of sovereign equality with regard to its nearly 200 member nations.[34] Stated differently, Interpol's notice system presumes a global standard of integrity. But this assumption is not only wrong, it is patently dangerous. Red Notices do not have to be founded on "probable cause," as recognized under American law. In fact, they can issue regardless of the requesting jurisdiction's level of institutional corruption or its record with regard to human rights. As reported by Fair Trials International (FTI), a number of countries, including Russia, Sri Lanka, Turkey, Belarus, Indonesia, Iran, and Venezuela, have exploited Interpol's system to pursue political dissidents, refugees and journalists.[35] In those cases, Interpol's entire international community was used to further the corrupt regime's goals. Reliable procedural safeguards should exist to prevent the Red Notice system from being exploited to oppress and silence, or to arrest and extradite someone for less than a serious crime or for conduct that is arguably not even criminal at all. But Interpol's system of checks and balances has not sufficiently prevented these and other kinds of abuses. Red Notices certainly have been directed against political opponents, political dissidents, economic targets, human rights activists, refugees, and even journalists.[36] Of the offending regimes, half are "corrupt" as defined by Transparency International, and the abuses appear to be increasing.[37] Nevertheless, Interpol seems to be making some progress toward reforming the system.[38] In its recently updated 2012 Rules on the Processing of Data, Interpol tightened and improved its procedures for publishing and recalling Red Notices.[39] As a result, and though more reforms still are needed, some regimes apparently have started to resort to Diffusions to further their tactics of silence, oppression, and persecution.[40] Some circumstantial evidence suggests that this might be occurring: the most controversial cases over the past few years have involved jailings and deportations based on Diffusions.

V. Diffusions – A Growing Threat to Fundamental Due Process Rights

Diffusions present even more of a threat to human and due process rights than the flawed Red Notice system. For example, in 2012, a Diffusion was disseminated by Egypt for the arrest of 15 Non-Governmental Organization (NGO) democracy workers even though Interpol had refused to publish Red Notices. Because Interpol policy permits a Diffusion to be requested simultaneously with a Red Notice, Egypt effectively bypassed Interpol's review process by the General Secretariat – a process that subsequently rejected the same Red Notice requests because the charges against the NGO workers were politically motivated. From this example, it is easy to see how Interpol's current system basically invites member nations–expecting denial of their Red Notice applications–to file Diffusions simultaneously as a strategy to guarantee that their targets are arrested and detained pending extradition.[41] Unfortunately, and on average, twice as many Diffusions as Red Notices are issued on an annual basis through the Interpol system. This is a troubling statistic because Diffusions carry the weight of a Red Notice and Interpol's endorsement without equivalent procedural protections. For these reasons, Diffusions raise even more serious and pressing concerns. Diffusions are entered into the Interpol system without any formal or informal vetting process or institutional review. Interpol is autonomous, and it has not imposed adequate, much less robust, checks and balances on Diffusions.[42] Because there is no vetting of Diffusions, and because they are so easily obtained, the process naturally invites exploitation and corruption. Although Diffusions are in theory required to respect Article 3 of the Interpol constitution and other applicable rules, the fact that they are not reviewed by the General Secretariat, as Red Notices are, renders this requirement a mere recommendation in practice. Hence, there is nothing to prevent regimes from transmitting Diffusions for the purpose of harassing or silencing political opponents, racial or religious minorities, dissidents, activists, or anyone else for whom a valid arrest warrant has not been issued. The 2012 Egyptian Diffusion requesting arrests of the NGO workers is a prime example: Egypt achieved its political ends even though Interpol had refused to publish even one Red Notice on the same individuals.[43] After Diffusions have been kept active for five years, Interpol

requests updated information from the issuing NCB to support the Diffusion's continued publication. Even absent such information, the NCB independently can keep the Diffusion active indefinitely.[44] Although the same five-year procedure also applies to Red Notices, they are subject to the more rigorous review process within the office of the General Secretariat. As one scholar concluded, Diffusions "are not in conformity with basic requirements for criminal or administrative procedures affecting individual rights."[45]

Of course, Interpol argues that it does not endorse Diffusions, but simply allows member NCBs to use its system to disseminate them. Interpol has analogized itself to a news publisher, but the comparison is inaccurate if not disingenuous.[4] First, Interpol itself takes credit for arrests made as a result of Diffusions.[47] Second, by allowing its communications system to be used to transmit Diffusions, Interpol knowingly assists NCBs with requested arrests. Furthermore, it does so without confirming the NCB's factual representations or reviewing the Diffusions for compliance with Interpol's constitutional rules. Therefore, there is no question that Diffusions carry Interpol's endorsement and that the organization considers them to be a complementary addition to the Red Notice system.

VI. Necessary Reforms to Assure Fairness and Integrity in Interpol's International Wanted Notice Process

Although Interpol has recently made strides in improving its procedures for the issuance and retraction of Red Notices, the reforms have not gone far enough to prevent abuse and assure that due process is applied on an equal and consistent basis. As Interpol's processing platform has made it easier for NCBs to transmit Diffusions, publish provisional Red Notices, and access Interpol-held data directly, the number of troubling cases has increased. Absent further reforms, the increase likely will continue.[48] Therefore, more must be done to curtail the abuse and correct the systemic flaws in the application and review process, particularly with regard to those individuals who are unfairly targeted for corrupt or political reasons.

A. Due Process

Because due process is not administered equally by Interpol's sovereign members in the filing of Red Notice applications, a leveling of the playing field is needed to require that all nations and NCBs operate pursuant to the same procedural and substantive standards. Interpol should adopt more comprehensive procedural and enforcement mechanisms to better guarantee that a targeted person is afforded due process by both the requesting and arresting member nations. Reforms in procedural and substantive due process, comprehensively applied, will help reduce instances where the arresting jurisdiction, knowingly or unknowingly, aids and abets an originating jurisdiction in a *persecution*, rather than in a legitimate *prosecution* warranting Interpol's intervention.

Interpol should scrupulously abide by its own constitution, which requires that Red Notices respect the basic rights of individuals and that no intervention occur in matters of political, military, religious, or racial character. Questions have been raised regarding Interpol's intention to uphold its own constitutional mandates in view of several controversial cases in which the organization has become involved over the last few years.[49] In fact, in a recent report, FTI concluded that, because Interpol's procedural safeguards have proved ineffective, the organization should absolutely refuse or delete Red Notices where there are "substantial grounds to believe the person is being prosecuted for political reasons."[50] Likewise, Interpol should modify its current policy requiring that Red Notice applications merely certify the existence of a properly issued arrest warrant. Instead, Interpol should require that the requesting jurisdiction provide an actual certified copy of the arrest warrant as an attachment to its application. Interpol's practice of issuing provisional Red Notices is problematic as well. Even under circumstances where they are visible only to other law enforcement agencies, the practice allows applicant nations to circumvent (as with Diffusions) a wanted person's due process rights. A Red Notice, whether provisional or permanent, should only issue after its application and supporting documents are reviewed fully by Interpol and found to be in compliance with its constitutional principles and international due process standards. Provisional Red Notices, by definition, are not guaranteed by Interpol to be compliant with any standard. Accordingly, Interpol should not permit provisional Red Notices except in urgent cases involving life and death. In the American criminal justice system, the due process rights of a person facing serious criminal charges and imprisonment are no better exemplified than in that person's right to challenge his accusers in a public hearing administered by an independent judicial officer. Under Interpol's current rules, the person targeted for arrest through a Red Notice or Diffusion does not have to be notified of his wanted status, is not entitled to an Interpol hearing, and does not have access to an independent court to challenge the Red Notice or Diffusion. Therefore, with the possible exception for crimes of violence and terrorist acts, Interpol's rules should be amended to require notification of every person targeted by a Red Notice or Diffusion. Wanted persons should be notified the moment that an NCB has submitted an application for a Red Notice or entered a Diffusion into Interpol's system.

Interpol should also allow an aggrieved person the right to an evidentiary hearing, the right to call and cross-examine witnesses, and the right to review and introduce evidence. As an added benefit, such a process would inject a needed dose of transparency into the process, while enhancing public confidence in Interpol. The CCF would be the likely candidate to serve in the capacity of an independent tribunal. On the other hand, an independent court of review–or possibly independent regional courts–could be created by international convention for the same purpose. Judges could be drawn from the ranks of the least corrupt nations as identified, for example, by Transparency International. Regardless of whether the CCF or a court is delegated this function, it must have authority to act independently of Interpol, and the complaining party must have the right to appeal an adverse decision.

B. Transparency

With an eye toward comprehensive reform, additional measures are also needed to increase transparency in the process of issuing Red Notices and Diffusions. One author has suggested that Interpol completely end the practice of removing controver-

sial Red Notices from public view.[51] One of Interpol's practices, when faced with a controversial Red Notice, particularly ones questioned on Article 3 grounds, is to remove the summarized contents of the Red Notice from the Internet and therefore from public scrutiny.[52] In those cases, the Notices still remain active and visible to law enforcement agencies worldwide. However, if Interpol receives information post-publication that establishes grounds to believe that the Notice should not have been published, Interpol must be obligated to retract it completely, not merely from public view. Red Notices also should be subject to systematic review. For example, some Red Notices have remained published despite extradition decisions recognizing the political nature of the cases. Interpol, therefore, should routinely follow up with nations that have reported arrests based on Red Notices and inquire into the outcome of the post-arrest proceedings.

C. Interpol's CCF

The CCF itself has come under scrutiny as well. FTI has argued that the CCF's expertise is centered on data processing and that it therefore institutionally lacks the competence and requisite procedural safeguards to review challenges to either Red Notices or Diffusions.[53] FTI's recent report further suggests that Interpol explore the idea of creating a separate organization or chamber within the CCF that is dedicated to handling such complaints and challenges. This would allow the CCF, in its present form, to advise on data protection issues as intended. This idea is worthy of Interpol's consideration, particularly until an independent court of review can be established.

D. Diffusions

In contrast to Red Notices, Diffusions routinely are reviewed only after they have been internationally disseminated. By endorsing this policy, Interpol effectively is aiding member nations in circumventing the Notice system and its procedural safeguards. Together with provisional Red Notices, Interpol should end this practice. Except for urgent cases, there is no reason Diffusions should not be reviewed by Interpol's General Secretariat prior to transmission, particularly given their practical equivalence to Red Notices. Interpol's failure to subject Diffusions to the same review process as Red Notices makes a mockery out of Interpol's constitution and the entire Red Notice system. Absent pre-dissemination review by Interpol, the availability of a Diffusion seeking an arrest should be limited to the most serious criminal offenses. Alternatively, Diffusions should be limited to emergency situations not afforded the weight of an arrest warrant by member nations. In any case, a person aggrieved by a Diffusion should have the right to challenge it in the same manner provided for challenging a Red Notice.

Endnotes

1 *See* Int'l Criminal Police Org. [Interpol], *Interpol's Rules on the Processing of Data*, art. 82, at 33, Interpol Doc. III/IRPD/GA/2011 (2014) [hereinafter *INTERPOL's Rules on the Processing of Data*]. An arrest warrant (enforceable within the issuing country's jurisdictional bounds) is distinguishable from a Red Notice, which is essentially an administrative vehicle used to publish the warrant through an international communication and database system. *See id.* art. 87, at 35. Hence, a Red Notice is an autonomous administrative act conceptually distinct from the underlying warrant.

2 *Id.* art. 82, at 33. Each Interpol member country maintains an NCB, essentially an Interpol field office, staffed by law enforcement officers. *See* Int'l Criminal Police Org. [Interpol], *Constitution of the ICPO-Interpol*, arts. 31-32, at 6, Interpol Doc. I/CONS/GA/1956 (2008) [hereinafter *Interpol's constitution*]. "The NCB is the designated contact point for the General Secretariat, regional offices, and other member countries requiring assistance with overseas investigations and the location and apprehension of fugitives." Cliff Robertson & Dilip K. Das, An Introduction to Comparative Legal Models of Criminal Justice 254 (2008). The NCBs "are regulated by their respective domestic law, but act as domestic extensions of Interpol, not their government." Mario Savino, *Global Administrative Law Meets "Soft" Powers: The Uncomfortable Case of Interpol Red Notices*, 43 N.Y.U. J. Int'l L. & Pol. 263, 274 (2011).

3 The prosecuting country is the source of the wanted notice. *Interpol's Rules on the Processing of Data*, *supra* note 1, art. 82, at 33. Interpol by itself has no authority to require a member country's NCB to take any specific action. *See id.* art. 87(c), at 35.

4 Interpol has the authority to refuse to issue a Red Notice when it is not satisfied that the notice contains all the information needed to formulate a valid request for a provisional arrest. *Id.* art. 81(3)(c), at 33; *see also id.* art. 83, at 33 (listing the criteria for the publication of a Red Notice).

5 Police can also bypass (to a limited extent) the formal Red Notice system altogether by typing an informal notice of arrest in an e-mail and posting it on Interpol's internal communications system. *See id.* arts. 97-98, at 38. These e-mail notices, referred to as "Diffusions" by Interpol, go out instantly with no automatic Interpol review. *Id.* art. 98, at 38. A Diffusion therefore is an electronic dissemination of wanted person information to agencies in a particular country or area who then immediately broadcast the wanted person information to their officers. The Diffusion acts in the same manner as an "all points bulletin" or "APB," and precedes the official Red Notice. The principal difference between a Diffusion and a Red Notice is that the General Secretariat does not review a Diffusion prior to its dissemination. *Compare id.* art. 98(1), at 38, *with id.* art. 88, at 35. It may contain information similar to a Red Notice and is frequently disseminated while the issuing member country awaits an approval for a Red Notice. If a Diffusion is issued based on an improperly issued warrant, Interpol likely will refuse to issue the Red Notice. Diffusions, like Red Notices, can be challenged and are, therefore, subject to scrutiny by Interpol offices located in Lyon, France.

6 Hence a Red Notice is not, by itself, a request for extradition. The initiating country must file a formal extradition request after the person is located and detained. *See id.* art 97(1), at 38.

7 Timothy A. Williams, Interpol Washington Recognizes the Importance of International Police Cooperation and Information Sharing, Presentation at Foro de Líderes de Seguridad Nacional (Nov. 18, 2010) (emphasis added).

8 Savino, *supra* note 2, at 298.

9 A second, although less common, manner in which extradition can be granted is through diplomatic relations.

10 *'Wanted by Interpol' goes live on the Internet*, Interpol (Feb. 25, 2000), http://www.interpol.int/News-and-media/News/2000/PR001.

11 *Id.* ("If a red notice is considered to be a valid request for provisional arrest, the appropriate judicial authority in a country receiving the notice can decide, on the basis of the information it contains, and in accordance with the national laws, that the wanted person should be provisionally arrested as soon as he has been located by the police. In that case, the requesting country will be informed that the wanted person has been provisionally arrested and that the extradition process must be initiated. The requesting country will be assured that the person concerned will be detained in accordance with the applicable laws of the arresting country.").

12 If the United States is the *requesting* country, the Red Notice is generated by the U.S. NCB in coordination with the Criminal Division of the U.S. Department of Justice. *See Provisional Arrests and International Extradition Requests—Red, Blue, Or Green Notices*, U.S. Dep't of Justice, http://www.justice.gov/usam/organization-and-functions-manual-3-provisional-arrests-

and-international-extradition-requests (last visited July 29, 2015). The Notice will request that the subject be provisionally arrested. *Id.* The Notice is sent to all 188 Interpol member countries, and is posted at all U.S. border ports of entry. *Id.* The data is also entered into the National Crime Information Center (NCIC). *Id.*

13 *See Notices*, Interpol, http://www.interpol.int/INTERPOL-expertise/Notices (last visited July 29, 2015).

14 *Id.*

15 *Interpol Red Notice*, *in* Internal Revenue Service, Internal Revenue Manual § 9.4.12.18.1 (2008), *available at* http://www.irs.gov/irm/part9/irm_09-004-012.html#d0e937.

16 Savino, *supra* note 2, at 305.

17 *See Interpols Rules on the Processing of Data*, *supra* note 1, arts. 85-86, at 34-35.

18 Savino, *supra* note 2, at 304.

19 *Interpol's Rules on the Processing of Data*, *supra* note 1, art. 76(b), at 32.

20 Savino, *supra* note 2, at 305.

21 *See* Interpol, *Notices*, at 2, Interpol Doc. COM/FS/2010-01/GI-02 (2010), *available at* http://www.interpol. int/Public/ICPO/FactSheets/GI02.pdf.

22 Savino, *supra* note 2, 320-21.

23 *Id.* at 314 n.156.

24 *Id.* at 312.

25 *Id.*

26 *Id.*

27 *See* Fair Trials International, Strengthening Respect for Human Rights, Strengthening Interpol 15-16 (2013), *available at* http://www.fairtrials.org/wp-content/uploads/Strengthening-respect-for-human-rights-strengthening-INTERPOL4.pdf.

28 *Id.* at 15-16.

29 *Interpol's Rules on the Processing of Data*, *supra* note 1, art. 99, at 38.

30 Interpol, Annual Report 2011, at 34 (2011); *see also* Theodore R. Bromund & David B. Kopel, *Necessary Reforms Can Keep Interpol Working in the U.S. Interest*, Heritage Foundation Backgrounder, No. 2891, Dec. 11, 2013, at 12, 36 n.119, *available at* http://thf_media.s3.amazonaws.com/2013/pdf/BG2861.pdf.

31 Law enforcement officers worldwide routinely exchange thousands of messages using the I-Link system. Officers located in NCBs and other authorized users are able to access I-link through the I-24/7 network.

32 *Interpol's Rules on the Processing of Data*, *supra* note 1, art. 99(3)(c); *Data Exchange*, Interpol, http://www.interpol.int/INTERPOL-expertise/Data-exchange/I-link (last visited July 29, 2015).

33 Bromund & Kopel, *supra* note 30, at 15.

34 *Id.* at 11.

35 *See generally* Fair Trials International, *supra* note 27.

36 *See* Bromund & Kopel, *supra* note 30, at 8-11.

37 Libby Lewis, *Interpol's Red Notices Used by Some to Pursue Political Dissenters, Opponents*, The Cutting Edge, July 25, 2011, http://www.thecuttingedgenews.com/index.php?article=52447.

38 *See generally* Bromund & Kopel, *supra* note 30.

39 *See Interpol's Rules on the Processing of Data*, *supra* note 1.

40 *See* Bromund & Kopel, *supra* note 30, at 12-16.

41 *Id.*

42 James Sheptycki, *The Accountability of Transnational Policing Institutions: The Strange Case of Interpol*, 19 Canadian J. of L. & Soc'y, 107, 124 (2004).

43 Sara Sorcher, *Interpol Denies Egypt's Request for Arrest of NGO Workers*, National Journal, May 29, 2013, http://www.nationaljournal.com/nationalsecurity/interpol-denies-egypt-srequest-for-arrest-of-ngo-workers-201220423.

44 *See Interpol's Rules on the Processing of Data*, *supra* note 1, art. 100, at 38-39.

45 Bettina Schöndorf-Haubold, *The Administration of Information in International Administrative Law–the Example of Interpol*, 9 German L.J. 1719, 1742 (2008), *available at* https://www.germanlawjournal.com/pdfs/Vol09No11/PDF_Vol_09_No_11_1719-1752_Articles_Haubold.pdf.

46 Bromund & Kopel, *supra* note 30, at 15 (citing Michael Olmsted, briefing, Interpol, January 12, 2010).

47 *See, e.g.*, Interpol, Annual Report 2011, *supra* note 30, at 33.

48 *See* Bromund & Kopel, *supra* note 30, at 8-11.

49 Fair Trials International, *supra* note 27, at 4.

50 Bromund & Kopel, *supra* note 30, at 27.

51 *Id.*

52 Fair Trials International, *supra* note 27, at 52-65.

Environmental Law & Property Rights

EPA's Use of Co-Benefits

*By C. Boyden Gray**

Note from the Editor:

This article is about environmental regulation and the EPA's questionable practice of using co-benefits to justify its regulations. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. When we do so, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• Alan Neuhauser, *EPA Power Plant Rule 'Modestly' Lowers Rates, Carbon Emissions*, U.S. News & World Report (May 22, 2015), http://www.usnews.com/news/articles/2015/05/22/epa-power-plant-rule-modestly-lowers-rates-carbon-emissions.

• Adam Liptak and Coral Davenport, *Supreme Court Blocks Obama's Limits on Power Plants*, New York Times (June 29, 2015), http://www.nytimes.com/2015/06/30/us/supreme-court-blocks-obamas-limits-on-power-plants.html?_r=2.

• Benjamin Zycher, *President Obama's Clean Power Plan: All Cost, No Benefit*, American Enterprise Institute (August 14, 2015), https://www.aei.org/publication/president-obamas-clean-power-plan-all-cost-no-benefit/.

I. Cost-Benefit Analysis in Environmental Regulation

In keeping with longstanding Executive Orders and guidance from the Office of Management and Budget (OMB), EPA must subject its proposed major rules to cost-benefit analysis in an effort to demonstrate that the regulations will protect Americans' "health, safety, environment, and well-being" and bolster "the performance of the economy," but "without imposing unacceptable or unreasonable costs on society." This practice is consistent with the primary purpose of the Clean Air Act: "to protect and enhance the quality of the Nation's air resources"—not for their own sake—but "so as to promote the public health and welfare and the productive capacity of [the U.S.] population." A regulation that achieved cleaner air at a net cost to national health, welfare, and productive capacity would be inconsistent with this congressional purpose.

II. The Increasing Costs of Environmental Regulation

Thanks to technological advances, our environment is dramatically cleaner today than it was in the early days of EPA. In sector after sector of the American economy, the low-hanging fruit of environmental regulation has largely been picked. An unfortunate result of EPA's early success is a larger and larger EPA making smaller and smaller marginal improvements in the air we breathe, at greater and greater cost to the U.S. economy.

Take two examples of these high costs. First, EPA's proposed Clean Power Plan for regulating greenhouse gas emissions from existing power plants comes with an annual cost of $5.5 billion by 2020 and $7.3 billion by 2030, according to the Agency's own estimates. Second, the proposed revision to the National Ambient Air Quality Standard (NAAQS) for ozone will carry an annual price tag of between $3.9 billion and $15 billion by 2025, depending on the stringency of the standard EPA finalizes. As shown below, the corresponding benefits represent a small fraction of these costs.

III. The Co-Benefits Temptation

Faced with the staggering costs of regulation and the requirement of cost-benefit analysis, EPA is under considerable pressure to identify corresponding benefits to outweigh the costs. That is where co-benefits come in. Often a rule designed to reduce emissions of one pollutant claims most of its benefits from incidental reductions of secondary pollutants. Those incidental reductions are known as "co-benefits."

One such co-benefit has proven particularly useful to EPA's costly regulatory agenda. Estimated reductions of particulate matter ($PM_{2.5}$) and ozone have become a staple of EPA's regulation, with monetized benefits from $PM_{2.5}$ reduction representing the majority of all federal regulatory benefits (not just EPA's) for the past decade. As OMB reported to Congress in 2012, "It is important to emphasize that the large estimated benefits of EPA rules are mostly attributable to the reduction in public exposure to a single air pollutant: fine particulate matter." The vast majority of $PM_{2.5}$ co-benefits (about 98%) come from estimated reductions of premature mortality associated with $PM_{2.5}$ exposure based on EPA's estimated "value per statistical life," which takes no account of the age of the persons whose premature mortality is supposedly avoided. This metric is questionable in itself since, as OMB reported, "significant uncertainty remains" concerning "the reduction of premature deaths associated with reduction in particulate matter and . . . the monetary value of reducing mortality risk."

IV. EPA's Mercury Rule

For example, although no cost-benefit analysis was required, EPA's recent rule governing mercury emissions from power plants predicted benefits of up to $90 billion per year, including the avoidance of up 11,000 premature deaths annually, even though only a tiny proportion of those benefits came from reducing mercury emissions. More than 99% of the anticipated benefits were attributable to incidental reductions of $PM_{2.5}$.

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This stark imbalance prompted Chief Justice Roberts to suggest in oral argument that EPA was using its authority to regulate mercury "to get at the criteria pollutants [including $PM_{2.5}$] that you otherwise would have to go through a much more difficult process to regulate." The Chief Justice questioned whether EPA "ought to consider only the benefits of regulating that" targeted pollutant, rather than "bootstrapp[ing]" a "disproportionate amount of benefit that would normally be addressed under" a separate statutory authority.

V. EPA's Clean Power Plan

But despite these sensible questions, there is no end in sight for EPA's reliance on $PM_{2.5}$ and ozone co-benefits. Most of the projected benefits that EPA used to justify its proposed regulation of carbon emissions from power plants have nothing to do with climate change—the purported aim of the regulation. Out of $48 billion in total domestic benefits projected for 2030, for example, $45 billion (94%) are attributed to ancillary $PM_{2.5}$ and ozone reduction. Only $3 billion are associated with the climate change benefits of achieving the mandated carbon reductions—an amount far below the rule's annual compliance costs of $9 billion.

EPA's reliance on co-benefits to justify its new carbon rule is especially problematic because the statutory authority for that rule—section 111(d) of the Clean Air Act—*expressly prohibits* EPA from regulating $PM_{2.5}$, ozone, and other "criteria pollutants" under that provision. Because sources of air pollution inevitably emit multiple pollutants indiscriminately, air pollution regulations necessarily affect multiple pollutants. The only meaningful way to enforce the prohibition on regulating criteria pollutants through Section 111(d), therefore, is to prohibit EPA from counting $PM_{2.5}$, ozone, and other NAAQS pollutants as benefits of carbon regulation under that section.

VI. Double Counting

Particulate matter and ozone seem to offer EPA an inexhaustible well of regulatory co-benefits. But $PM_{2.5}$ and ozone are both already directly regulated by EPA's NAAQS to a level "requisite to protect the public health" with "an adequate margin of safety." Thus, whenever EPA counts $PM_{2.5}$ or ozone reductions in its cost-benefit analysis for other rules, it is double-counting reductions already mandated by the NAAQS.

For example, EPA admits that its proposed Clean Power Plan's benefit "estimates include health co-benefits from reducing fine particles in areas with varied concentrations of $PM_{2.5}$, including both areas that do not meet the fine particle standard and those areas that are in attainment, down to the lowest modeled concentrations." And it counts every ton of $PM_{2.5}$ reduction equally, regardless of where it is found.

This is double-counting, plain and simple. As Michael A. Livermore and Richard L. Revesz explained in the N.Y.U. Law Review last year, "[t]o guard against double counting the ancillary benefits, one needs to make sure that after each regulation is promulgated, a new baseline level of pollution is computed. Then, the further benefits from subsequent regulations need to be determined by reference to this baseline." EPA regularly flouts this basic principle of sound regulation by ignoring the $PM_{2.5}$ and ozone reductions it has already mandated, and counting those reductions again as benefits in new rules. The same ton of pollutant thus serves to justify multiple rules, even though the pollution can only be prevented once.

VII. Inflated Benefits

In regions that have already attained EPA's $PM_{2.5}$ and ozone NAAQS, counting reductions of those pollutants as co-benefits presents a different problem. EPA's NAAQS represent the level of pollution control that the Agency deems "requisite to protect the public health" with "an adequate margin of safety." Reducing $PM_{2.5}$ and ozone emission even further is not "requisite to protect the public health," and therefore cannot possibly produce the health benefits that the proposed rule claims. As a former Chairman of the Texas Commission on Environmental Quality has explained, "[i]f reducing particulate matter had the enormous benefits that EPA's analysis claims, it has a legal responsibility to lower the national ambient standard to a level that is actually protective of human health. The fact that it has not done so suggests that the EPA does not really believe its own numbers."

EPA can only accomplish this sleight of hand by jettisoning the very same evidence, assumptions, and models that it used to justify the $PM_{2.5}$ and ozone standards. In support of its proposed Clean Power Plan, EPA "assumes that the health impact function for fine particles is log-linear without a threshold" and counts $PM_{2.5}$ mortality benefits all the way down to the lowest measured level. But in its 2013 $PM_{2.5}$ NAAQS, EPA explicitly considered and rejected proposals to mandate a more stringent $PM_{2.5}$ standard, because such a standard "would not be warranted to provide requisite protection that is neither more nor less than needed to provide an adequate margin of safety." EPA declared that it was "not appropriate to focus on" the "uncertain" and "suggestive" evidence of health effects from $PM_{2.5}$ exposure below the mandated level. The proposed rule ignores these conclusions and treats all emissions reductions alike, whether or not they occur below the NAAQS level. Without any explanation for contradicting the assumptions on which it based its own $PM_{2.5}$ rule, EPA declares in the Clean Power Plan that it is "unable to estimate the percentage of premature mortality associated with the emission reductions at each $PM_{2.5}$ concentration, as we have done for previous rules with air quality modeling," and admits that it is "less confident in the risk we estimate from simulated $PM_{2.5}$ concentrations that fall below the bulk of the observed data in the [relevant] studies." Yet it is on the basis of these supposed benefits that EPA is justifying a path-breaking greenhouse gas regulation to the American people. The EPA's inflation of its purported regulated benefits appears to be a perfect example of what former OIRA Administrator Susan Dudley describes as the agencies' habit of "perpetuating puffery" in their benefit-cost analyses.

VIII. Nondelegation Implications

EPA's misuse of co-benefits to justify costly regulations is more than just bad policy; it violates the constitutional separation of powers. As I explained in an article in the George Mason Law Review earlier this year, the Supreme Court and D.C. Circuit have repeatedly recognized that statutes must not be construed to allow the agency to impose substantial regulations without evidence that such regulation is actually necessary to prevent "significant" risk of harm. To allow otherwise would be

to "make such a 'sweeping declaration of legislative power' that it might be unconstitutional under" the Court's nondelegation precedents, as Justice Stevens' plurality opinion in the *Benzene Cases* explained. "A construction of the statute that avoids this kind of open-ended grant should certainly be favored," he and his colleagues stressed.

The Court reiterated this approach in *Whitman v. American Trucking Associations*, where it narrowly construed the Clean Air Act's Section 109(b)(1). That statute provides for the establishment of air quality standards that are "requisite" to protect public health. The Court, at Solicitor General Waxman's urging, construed this as authorizing EPA to set standards that are "sufficient, but not more than necessary," to protect public health.

EPA utterly ignores such limits in its counting of $PM_{2.5}$ co-benefits in the Clean Power Plan. Just two years ago, when EPA updated its NAAQS for $PM_{2.5}$, the agency specifically found that the "requisite" level of protection was 12 micrograms per cubic meter; beyond that level, EPA could not show significant health impacts. But now, when calculating the supposed co-benefits that the Clean Power Plan would achieve by collaterally reducing $PM_{2.5}$, the EPA jettisons that conclusion without any justification, and simply claims co-benefits for any $PM_{2.5}$ reductions that might be obtained, even beyond the aforementioned 12 micrograms level, all the way down to the zero level. In other words, EPA now interprets the Clean Air Act as allowing it to regulate $PM_{2.5}$ emissions reductions beyond 12 micrograms, all the way down to zero, even though they have not shown any significant health risks being eliminated by such extreme reductions. EPA is treating the Clean Air Act as a completely open-ended grant of power, precisely as the Supreme Court forbids.

IX. Foreign Co-Benefits

Perhaps EPA's most egregious use of co-benefits is its reliance on the projected global benefits of its regulations. The cost-benefit analysis supporting EPA's Clean Power Plan and other carbon regulations is predicated on an apples-to-oranges comparison of domestic costs and global benefits. This will be a hallmark of all subsequent carbon regulation, thanks to the global "social cost of carbon" (SCC) at the heart of EPA's analysis. Although all of the costs of reducing carbon emissions will be borne by U.S. entities, EPA offsets those costs against a global valuation of the benefit of reducing a ton of carbon. Never mind that the United States' share is only 7 to 10 percent of the global SCC.

EPA's reliance on foreign benefits violates the Clean Air Act, whose purpose is "to protect and enhance the quality of the *Nation's* air resources so as to promote the public health and welfare and the productive capacity of *its* population." Despite EPA's past acknowledgement of "the [Clean Air Act's] stated purpose of protecting the health and welfare of *this* nation's population" in the context of the Agency's greenhouse gas endangerment finding, the Agency now gives equal weight to foreign benefits, without regard to whether they have any measurable impact on the United States.

EPA's use of a global social cost of carbon also violates OMB guidance, which requires a regulatory impact analysis to "focus on benefits and costs that accrue *to citizens and residents of the United States*." The Interagency Working Group that produced the SCC noted OMB's guidance, and acknowledged that using a global estimate "represents a departure from past practices, which tended to put greater emphasis on a domestic measure of SCC." Nevertheless, the Working Group—and EPA—expressly declined to follow OMB's instructions.

EPA attempts to justify its reliance on foreign benefits by the observation that "we expect other governments to consider the global consequences of their greenhouse gas emissions when setting their own domestic policies." But of course EPA has no power to control whether foreign countries regulate greenhouse gas emissions at all, much less how they calculate the benefits of their own regulation. As former Administrator of OIRA, Susan Dudley, has explained, "In the absence of . . . reciprocal action by other nations, . . . the global benefits in the SCC cannot be regarded as a legitimate entry in the benefit-cost ledger."

The global SCC has also been defended on the ground that climate change involves global externalities. But all significant U.S. regulations have international externalities, and the global benefits of adopting policies designed to benefit the world at large would invariably outweigh their cost to U.S. citizens. As economists Ted Gayer and Kip Viscusi have observed, the use of global benefits to justify domestic regulations "represents a dramatic shift in policy, and if applied broadly to all policies, would substantially shift the allocation of societal resources." Of course, if Congress wanted EPA to consider global benefits, it could pass a law requiring EPA to do so. But that is a policy judgment only Congress can make.

X. Guiding Principles for the Future

1. *Maintain Coherence Across Regulations.* In cost-benefit analysis of proposed regulations, EPA should not double-count pollution-related benefits that have already been used to justify prior regulations. Nor should agencies be allowed to count reductions of pollutants in areas where they appear below the national standard EPA has already set for those pollutants. EPA should use the best available data and models for calculating the health effects of reducing a given pollutant across all regulations.

2. *Compare Apples to Apples.* The costs of complying with a given regulation should be compared against the social goods that that regulation is authorized to achieve—not incidental co-benefits, especially the reduction of pollutants that are already regulated by separate rules. By the same token, domestic costs should be compared against domestic benefits.

3. *Justify Regulations Based on American—Not Global—Benefits.* Consistent with the Clean Air Act's purpose of improving national air quality and OMB's guidance requiring agencies to focus on domestic benefits, EPA should be prohibited from justifying costs to domestic industry with estimated benefits to the world at large.

Human Responsibility, Not Legal Personhood, For Nonhuman Animals

*By Richard L. Cupp, Jr.**

Introduction

We should focus on human legal accountability for responsible treatment of nonhuman animals rather than radically restructuring our legal system to make them legal persons.[1] This paper outlines a number of concerns about three ongoing related lawsuits seeking legal personhood for chimpanzees filed in New York state courts by the Nonhuman Rights Project (NhRP) in late 2013.

The lawsuits, *The Nonhuman Rights Project v. Lavery, The Nonhuman Rights Project v. Presti*, and *The Nonhuman Rights Project v. Stanley*, mostly overlap in terms of their legal theories.[2] They collectively involve four chimpanzees, two of which are kept by private individuals, and two of which were kept until recently for research on the evolution of bipedalism at Stony Brook University. The lawsuits each seek a common law writ of habeas corpus for the chimpanzees.[3] The lawsuits do not claim that any existing laws are being violated in the chimpanzees' treatment. Rather, the lawsuits argue that the chimpanzees are entitled to legal personhood under liberty and equality principles, asserting that each chimpanzee is "possessed of autonomy, self-determination, self-awareness, and the ability to choose how to live his life, as well as dozens of complex cognitive abilities that comprise and support his autonomy."[4] The lawsuits also assert that the chimpanzees are entitled to legal personhood under a New York statute allowing humans to create inter vivos trusts for the care of animals.[5] The lawsuits seek to have the chimpanzees moved to a sanctuary that confines chimpanzees, but in a manner the lawsuits argue is preferable to the chimpanzees' present living situations.[6]

As of the writing of this paper, the lawsuits have been unsuccessful. By the author's count, eighteen New York judges have ruled against the lawsuits thus far.[7] A unanimous intermediate appellate court rejecting *Lavery* emphasized that "collectively, human beings possess the unique ability to bear legal responsibility."[8] Another unanimous intermediate appellate court rejecting *Presti* raised an additional challenge without contradicting *Lavery*. The *Presti* court asserted that even if a chimpanzee were a person for purposes of habeas corpus (without addressing whether it actually is a person for this purpose), a habeas writ is only appropriate for immediate release from confinement, and being moved to a sanctuary is still a form of confinement.

The NhRP is seeking to appeal *Lavery* and *Presti* to the State of New York Court of Appeals. *Stanley* was most recently dismissed by a lower court judge, Justice Barbara Jaffe, in Manhattan in July 2015. The Manhattan *Stanley* ruling rejected the lawsuit because it found the *Lavery* appellate decision to be controlling under stare decisis, and because it believed the issue should be left to the legislature or to the State of New York Court of Appeals. Although the ruling emphasized that the law may evolve, and took a sympathetic tone with some of the NhRP's positions without highlighting some of the serious problems with the lawsuit, it did not advocate for animal legal personhood. Rather, the decision in rather vague dicta seemed to imply support more generally for further consideration of the issue without staking out a position. In further dicta, the decision expressly rejected using the past mistreatment of slaves, women, and other humans as an analogy for extending legal personhood to animals. The NhRP has announced that it will appeal the ruling to a New York intermediate appellate court.

Despite a lack of success thus far, these lawsuits are only at the beginning of a long-term struggle, and the issue's ultimate outcome is far from clear. Although the lawsuits are misguided in many ways, they should not be underestimated. The question of how we treat animals is exceptionally serious, both for animals and for human morality.[9] The emotional appeal of doing something very dramatic in an effort to help animals, especially the animals that are most like us, is understandably strong to many people. As expressed by Justice Jaffe in the lower court Manhattan *Stanley* ruling, "The similarities between chimpanzees and humans inspire the empathy felt for a beloved pet."[10]

This paper encourages greater empathy for animals, but introduces and briefly outlines several (although not all) problems with the lawsuits, and calls instead for a focus on evolving standards of human responsibility for animals' welfare as a means of protecting animals, rather than granting legal personhood to animals.

I. Animal Legal Personhood as Proposed in the Lawsuits Would Pose Threats to the Most Vulnerable Humans

One of the most serious concerns about legal personhood for intelligent animals is that it presents an unintended, long-

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term, and perhaps not immediately obvious threat to humans—particularly to the most vulnerable humans.

Among the most vulnerable humans are people with cognitive impairments[11] that may give them no capacity for autonomy or less capacity for autonomy than some animals, whether because of age (such as in infancy), intellectual disabilities, or other reasons.[12] To be clear, supporting personhood based on animals' intelligence does not imply that one *wants* to reduce the protections afforded humans with cognitive impairments. Indeed, my understanding is that the lawsuits seek to pull smart animals up in legal consideration, rather than to push humans with cognitive impairments down.[13]

However, despite these good intentions, there should be deep concern that, over a long horizon, allowing animal legal personhood based on cognitive abilities could unintentionally lead to gradual erosion of protections for these especially vulnerable humans. The sky would not immediately fall if courts started treating chimpanzees as persons. As noted above, that is part of the challenge in recognizing the danger. But over time, both the courts and society might be tempted to not only view the most intelligent animals more like we now view humans, but also to view the least intelligent humans more like we now view animals.[14]

Professor Laurence Tribe has expressed concern that the approach to legal personhood for intelligent animals set forth in a much-discussed book by Steven Wise, the president and lead attorney of the NhRP, might be harmful for humans with cognitive impairments. The book, *Rattling the Cage,* was published in 2000.[15] In 2001, Professor Tribe stated "enormous admiration for [Mr. Wise's] overall enterprise and approach," but cautioned that "[o]nce we have said that infants and very old people with advanced Alzheimer's and the comatose have no rights unless we choose to grant them, we must decide about people who are three-quarters of the way to such a condition. I needn't spell it out, but the possibilities are genocidal and horrific and reminiscent of slavery and the holocaust."[16]

Mr. Wise later responded in part: "I argue that a realistic or practical autonomy is a sufficient, not a necessary, condition for legal rights. Other grounds for entitlement to basic rights may exist."[17] But Mr. Wise also noted that in his view entitlements to rights cannot be based only on being human.[18] I did not find in the NhRP's briefs an explanation of why, despite Mr. Wise's apparent view that being part of the human community is not alone sufficient for personhood, he and the NhRP think courts should recognize personhood in someone like a permanently comatose infant. If the argument is that the permanently comatose infant has rights based on dignity interests, but that dignity is not grounded in being a part of the human community, why would this proposed alternative basis for personhood only apply to humans and to particularly intelligent animals? Would all animals capable of suffering, regardless of their level of intelligence, be entitled to personhood based on dignity? If a rights-bearing but permanently comatose infant is not capable of suffering, would even animals that are *not* capable of suffering be entitled to dignity-based personhood under this position?[19] The implications of some alternative non-cognitive approach to personhood that rejects drawing any lines related to humanity may be exceptionally expansive and problematic.

Further, good intentions do not prevent harmful consequences. Regardless of the NhRP's views and desires regarding the rights of cognitively impaired humans, going down the path of connecting individual cognitive abilities to personhood would encourage us as a society to think increasingly about individual cognitive ability when we think about personhood. Over the course of many years, this changed paradigm could gradually erode our enthusiasm for some of the protections provided to humans who would not fare well in a mental capacities analysis. Deciding chimpanzees are legal persons based on the cognitive abilities we have seen in them may open a door that swings in both directions regarding rights for humans as well as for animals, and later generations may well wish we had kept it closed.[20]

II. Applauding an Evolving Focus on Human Responsibility for Animal Welfare Rather than the Radical Approach of Animal Legal Personhood

When addressing animal legal personhood, the proper question is not whether our laws should evolve or remain stagnant. Our legal system *will* evolve regarding animals, and indeed is already in a period of significant change. One major reason for this evolution is our shift from an agrarian society to an urban and suburban society. Until well into the twentieth century, most Americans lived in rural areas. Most American families owned or encountered livestock and farm animals whose utility was economic. Now we are an urban and suburban society, and relatively few of us are directly involved in owning animals for economic utility. Rather, when most of us now encounter living animals, they are most frequently companion animals kept for emotional utility. Most of us view the animals in our lives in terms of affection rather than as financial assets. As law gradually reflects changes in society, transformation in our routine interactions with animals doubtless has influenced the trend toward providing them more protections in many respects.

A second major reason we are evolving in our legal treatment of animals is the advancement of scientific understanding about animals. We are continually learning more about animals' minds and capabilities. As we have gained more understanding of animals, we have generally evolved toward developing more compassion for them, and this increasing compassion has been to some extent and will continue to be increasingly reflected in our protection laws.

This evolution is a good thing, and it is probably still closer to its initial significant acceleration in the twentieth century than it is to a point where it will slow down. In other words, it seems quite probable that we will continue in a period of notable change in our treatment of animals for some time. We will continue evolving; the only question is *how* we should evolve. Two unsatisfactory positions and a centrist position may be identified in answering this question. One unsatisfactory position would be clinging to the past, and denying that we need any changes regarding how our laws treat animals. A second unsatisfactory position on the other extreme would be to radically reshape our understanding of legal personhood, with potentially dangerous consequences.

A centrist alternative to these extremes involves

maintaining our legal focus on human responsibility for how we treat animals, but applauding changes to provide additional protection where appropriate. As emphasized by the intermediate appellate court that unanimously dismissed the NhRP's *Lavery* appeal, "Our rejection of a rights paradigm for animals does not, however, leave them defenseless."[21] When our laws or their enforcement do not go far enough to prevent animals from being mistreated, we should change our laws or improve their enforcement rather than assert that animals are legal persons. The legislatures' role in legal evolution should be respected and embraced, and courts should refrain from adopting extreme legal theories that would not enhance justice and that would be contrary to the views of most citizens.

III. Among Beings of Which We Are Aware, Appropriate Legal Personhood is Anchored Only in the Human Community

As explained by the philosopher Carl Cohen, "Animals cannot be the bearers of rights because the concept of right is *essentially human*—it is rooted in the human moral world and has force and applicability only within that world."[22]

Our society and government are based on the ideal of moral agents coming together to create a system of rules that entail both rights and duties. Being generally subject to legal duties and bearing rights are foundations of our legal system because they are foundations of our entire form of government. We stand together with the ideal of a social compact, or one might call it a responsible community, to uphold all of our rights, including of course our inalienable rights.[23] As stated in the Declaration of Independence, "to secure these rights, Governments are instituted among Men, deriving their just powers from the consent of the governed."[24] One would be hard-pressed to convince most Americans that this is not important, as from childhood Americans learn it as a bedrock of our social structure. It is not surprising that the American Bar Association's section addressing civil liberties is called "The Section of Individual Rights and Responsibilities."[25]

This does not require viewing every specific protection of a right as corresponding to a specific duty imposed on an individual. The connection between rights and duties for personhood is in some aspects broader and more foundational than that. It comes first in the foundations of our society, rather than solely in analysis of specific obligations and rights for persons governed by our laws. As the norm, we insist that persons in our community of humans and human proxies be subjected to responsibilities along with holding rights, regardless of whether a specific right or limitation requires or does not require a specific duty to go along with it.

It misses the point to argue, as the NhRP seems to do in its *Lavery* brief seeking leave to appeal from the State of New York Court of Appeals, that personhood is unrelated to duties because we can call freedom from slavery a bodily liberty immunity right that does not require capacity.[26] First, as noted elsewhere in this section, this is too narrow a conceptualization of connections between rights and duties. Further, whether freedom from slavery requires capacity does not control the question of personhood, since cognitively impaired humans' personhood is anchored in the responsible community of humans, even if they cannot make responsible choices themselves. The NhRP's argument does not avoid the problem that a chimpanzee, although an impressive being we need to treat with exceptional thoughtfulness, should not be considered a *person* within our intrinsically human legal system, whereas humans with cognitive limitations should be recognized as persons.

Professor Wesley Hohfeld wrote about the form of rights and duties between persons in the early twentieth century, and the NhRP's brief seeking leave to appeal the intermediate appellate court's *Lavery* decision seeks to invoke his analysis to argue for chimpanzee legal personhood.[27] Perhaps the most basic problem with the NhRP's argument is that we are dealing with a question that must precede Hohfeldian analysis of the forms of rights granted to persons. Professor Hohfeld's description of rights assumed it was dealing with the rights of *persons*.[28] Our issue revolves around determining who is a member of society eligible for those rights and protections; in other words, who is a person. This is a foundational question that is not answered by Hohfeldian analysis.[29]

It is sometimes asserted that since we give corporations personhood, justice requires that we should give personhood to intelligent animals. But this ignores the fact that corporations are created by humans as a proxy for the rights and duties of their human stakeholders. They are simply a vehicle for addressing *human* interests and obligations.[30]

The NhRP argues that "*if* humans bereft of autonomy, self-determination, sentience, consciousness, even a brain, are entitled to legal rights, *then* this Court must either recognize Tommy's just equality claim to bodily liberty or reject equality entirely."[31] Although not described as such in the lawsuits, reasoning along these lines is often referred to by philosophers as "the argument from marginal cases."[32] The concept of an "argument from marginal cases" has an unsettling tone, because most of us do not want to think of *any* humans as being "marginal." The pervasive view that *all* humans have distinctive and intrinsic human dignity regardless of their capabilities may have cultural, religious, or even instinctual foundations.

All of these foundations would on their own present huge challenges for animal legal personhood arguments to overcome in the real world of law, but they are not the only reasons to reject the arguments. Humans with cognitive impairments are a part of the human community, even if their own agency is limited or nonexistent. Among the beings of which we are presently aware, humans are the only ones for whom the *norm* is capacity for moral agency sufficiently strong to fit within our society's system of rights and responsibilities. It may be added that no other beings of which we are presently aware living today (even, for example, the most intelligent of all chimpanzees) ever meet that norm. Recognizing personhood in our fellow humans regardless of whether they meet the norm is a pairing of like "kind"[33] where the "kind" category has special significance—the significance of the norm being the only creatures who can rationally participate as members of a society such as ours.

Morally autonomous humans have unique natural bonds with other humans who have cognitive impairments, and thus denying rights to them also harms the interests of society—we are all in *community* together. Infants are human infants, and adults with severe cognitive impairments are humans who are

other humans' parents, siblings, children, or spouses. We have all been children, and we relate to children in a special way. Further, we all know that we could develop cognitive impairments ourselves at some point in our lives, and this reminds us that humanity is the most defining characteristic of persons with cognitive impairments.

Thus, recognizing that personhood is anchored in the human moral world does not imply that humans with cognitive impairments are not persons or have no rights. As explained by Professor Cohen, "this criticism mistakenly treats the essentially moral feature of humanity as though it were a screening function for sorting humans, which it most certainly is not."[34] It would be a serious misperception to view the appellate court's decision in *Lavery* as actually threatening to infants and others with severe cognitive impairments in finding connections between rights and duties. This misperception would reflect an overly narrow view of how rights and duties are connected. Regarding personhood, they are connected with human society in general, rather than on an individual-by-individual capacities analysis.[35] Again, appropriate legal personhood is anchored in the human moral community, and we include humans with severe cognitive impairments in that community because they are first and foremost humans living in our society.[36] Indeed, the history of legal rights for children and for cognitively impaired humans is a history of increasing emphasis on their humanity.[37] The *Lavery* court noted that "some humans are less able to bear legal duties or responsibilities than others. These differences do not alter our analysis, as it is undeniable that, collectively, human beings possess the unique ability to bear legal responsibility."[38]

IV. How Far Might Animal Personhood and Rights Extend?

The NhRP has stated that a goal of using these lawsuits is to break through the legal wall between humans and animals.[39] But we have no idea how far things might go if the wall comes down. One might suspect that many advocates would push for things to go quite far.

In the real world, law does not fit perfectly with any single philosophical theory or other academic theory because judges must be intensely conscious of the practical, real world consequences of their decisions. One practical consequence courts should expect if they break through the legal wall between animals and humans is a broad and intense proliferation of expansive litigation without a meaningful standard for determining how many of the billions of animals in the world are intelligent enough to merit personhood. We should not fool ourselves into minimizing the implications of these lawsuits by thinking that they are, in the long run, only about the smartest animals.

How many species get legal personhood based on intelligence is just the start. Once the wall separating humans and nonhumans comes down, that could serve as a stepping stone for many who advocate a focus on the capacity to suffer as a basis for legal personhood. Animal legal rights activists do not all see eye to eye regarding whether they should focus on seeking legal standing for all animals who are capable of suffering or on legal personhood and rights for particularly smart animals like chimpanzees. However, these approaches may only be different beginning points with a similar possible end point.

The intelligent animal personhood approach that begins with the smartest animals is more pragmatic in the short term, because the immediate practical consequences of granting legal standing to all sentient animals could be immensely disruptive for society.[40] We do not have much economic reliance on chimpanzees, there are relatively few of them in captivity compared to many other animals, and we can recognize that they are particularly intelligent and more similar to humans than are other animals. Thus, perhaps a court could be tempted to believe that granting personhood to chimpanzees would be a limited and manageable change. If that were accepted as a starting position, there is no clear or even fuzzy view of the end position. It would at least progress to assertions that most animals utilized for human benefit have some level of autonomy interests sufficient to allow them to be legal persons who may have lawsuits filed on their behalf on that basis. Professor Richard Epstein has recognized the slipperiness of this slope, pointing out that, "unless an animal has some sense of self, it cannot hunt, and it cannot either defend himself or flee when subject to attack. Unless it has a desire to live, it will surely die. And unless it has some awareness of means and connections, it will fail in all it does."[41]

Once the personhood door opens to the more intelligent animals, it would also encourage efforts to extend personhood on the basis of sentience rather than autonomy. The implications of much broader potential expansion of legal personhood based on either autonomy definitions or sentience could be enormous, and society should carefully think through them. Any court that contemplates restructuring our legal system must also contemplate the practical consequences.

V. A Few Words about the Common Law Writ of Habeas Corpus

Professor Tribe has argued that the *Lavery* intermediate appellate court decision misunderstood the "crucial role" the common law writ of habeas corpus has historically played "in providing a forum to test the legality of someone's ongoing restraint or detention."[42] He also says it serves as "a crucial guarantor of liberty by providing a judicial forum to beings the law does not (yet) recognize as having legal rights and responsibilities on a footing equal to others."[43]

The common law writ of habeas corpus has indeed served as a vehicle for *humans* to test the legality of ongoing restraint. However, humans are not simply "beings," they are human beings, and their legal personhood is anchored in the human community. If habeas corpus jurisdiction were to be granted for any beings for whom an advocate wished to test the legality of restraint, would it be available for earthworms restrained in containers to be sold at gardening stores? If courts began to broadly allow habeas writs to test the legality of any nonhuman being's restraint, and then focused only on the scope of habeas corpus *relief* to limit boundaries, they could be opening themselves up to habeas corpus claims for countless animals.

The New York habeas corpus statute states that a "*person*" or one acting on the person's behalf may petition for the writ.[44] Thus, the jurisdiction question is related to the ultimate question of legal personhood under the statute's language. Boundaries

are needed for jurisdiction as well as for substantive relief, and, among the beings of which we are presently aware, habeas corpus should be grounded only in the human community.[45]

Conclusion

Recognizing that personhood is a fit for humans and not a fit for animals in our legal system does not limit us to considering animals as "*mere*" things with the same status as inanimate objects. "Mere" things such as inanimate objects do not have laws protecting them. This is not an argument that we have done enough for animals. Society is increasingly interested in protecting animals through law, and we must continue to develop our protections. As noted above, in some areas our laws have not yet caught up with our evolving views on the protection of animals, and quite a bit of evolution is likely still ahead even from an animal welfare perspective.[46]

Felony animal cruelty statutes provide a hopeful example of the kind of evolution that we have experienced and likely will continue to experience without restructuring our legal system to divorce personhood from humans and human proxies. Twenty-five years ago, few states made felony status available for serious animal cruelty.[47] A misdemeanor was the most serious charge available in most states. However, by 2014, our laws in this area had dramatically evolved. In that year South Dakota became the last of *all* states to make serious animal cruelty eligible for felony status.[48] We need to continue evolving our legal system like this to provide more protection to animals where appropriate, not because animals are legal persons, but because humans need to be responsible in their treatment of animals.

Endnotes

1 For the sake of brevity I will hereafter refer to nonhuman animals as "animals."

2 Because the lawsuits are so similar, this paper will cite to the NhRP's initial brief for one, *Nonhuman Rights Project v. Lavery*, as representative. *See* Petitioner's Memorandum of Law in Support of Order to Show Cause & Writ of Habeas Corpus and Order Granting the Immediate Release of Tommy, People ex. rel. The Nonhuman Rights Project, New York Supreme Court, Fulton County, Dec. 2nd, 2013 [hereafter "*Lavery* Brief], *available at* http://www.nonhumanrightsproject.org/wp-content/uploads/2013/12/Memorandum-of-Law-Tommy-Case.pdf. The *Lavery* lawsuit was rejected by a lower court and in a reported intermediate appellate decision, People ex. rel. Nonhuman Rights Project, Inc. v. Lavery, 124 A.D. 3d 148 (3rd Dept. 2015), and the NhRP is now seeking to appeal the case to the State of New York Court of Appeals. Another lawsuit involves a chimpanzee named Kiko kept by a private owner. This lawsuit was also rejected by a lower court and in a reported intermediate appellate decision, Matter of the Nonhuman Rights Project, Inc. v. Presti, 124 A.D. 3d 1334 (4th Dept. 2015), and the NhRP is also seeking to appeal this case to the State of New Court of Appeals. The third lawsuit, *Stanley*, involves two chimpanzees, named Hercules and Leo, who were until recently used in research at Stony Brook University. In July 2015, it was reported that the research project involving the chimpanzees had ended and that "the chimps will be leaving the university . . . soon." Associated Press, *Chimps Denied Legal Personhood will be Retired from Research*, New York Times, July 31st, 2015, *available at* http://www.nytimes.com/aponline/2015/07/31/us/ap-us-chimps-legal-rights.html?_r=0. *Stanley* was initially filed in Suffolk County, New York, but after being rejected by a lower court and by an intermediate appellate court, it was refiled in New York County. The New York County lower court judge, Justice Barbara Jaffe, ruled against the lawsuit in July 2015. The Nonhuman Rights Project v. Stanley, Supreme Court of the State of New York, New York County, Decision and Order, Index. No. 152736/15, July, 29, 2015, *available at* http://www.nonhumanrightsproject.org/wp-content/uploads/2015/07/Judge-Jaffes-Decision-7-30-15.pdf. The Nonhuman Rights Project has indicated that it plans to appeal this ruling as well.Many of the legal documents associated with the three lawsuits are available at http://www.nonhumanrightsproject.org/.

3 Although two of the lawsuits involve chimpanzees kept by private individuals rather than a government entity, the NhRP cites New York and other cases granting habeas corpus writs when a person was wrongfully imprisoned by a nongovernmental actor. The lawsuits' focus on common law habeas corpus rather than on constitutional arguments distinguishes them from *Tilikum v. Sea World Parks & Entertainment, Inc.*, 842 F. Supp. 2d 1259 (2012). In *Tilikum*, protection against slavery and involuntary servitude under the Constitution of the United States' 13th Amendment was asserted for five orcas owned by Sea World. *Id.* at 1260. In rejecting the lawsuit, the court held that the 13th Amendment applies only to "humans." *Id.* at 1262.

4 *Lavery* Brief, *supra* note 2, at 77.

5 *Id.* at 49-52.

6 *Id.* at 1.

7 This includes one lower court judge each for the *Lavery* and *Presti* lawsuits, two lower court judges for the *Stanley* lawsuit, five intermediate appellate judges each for the *Lavery* and *Presti* lawsuits, and four intermediate appellate judges for the *Stanley* lawsuit. *See supra* note 2.

8 *Lavery*, 124 A.D.3d at 152.

9 As recognized by Immanuel Kant, "He who is cruel to animals becomes hard also in his dealings with men." Immanuel Kant, Lectures on Ethics 240 (Louis Infield trans., Harper Torchbooks 1963) (1780).

10 The Nonhuman Rights Project v. Stanley, Supreme Court of the State of New York, New York County, Decision and Order, Index. No. 152736/15, July 29th, 2015, *available at* http://www.nonhumanrightsproject.org/wp-content/uploads/2015/07/Judge-Jaffes-Decision-7-30-15.pdf.

11 This paper will use the term "cognitive impairments" to refer to all human cognitive limitations, including those related to childhood and intellectual disabilities, as well as being comatose or being impaired due to an injury, illness or medical condition.

12 The implications of cognitive impairments for young children and for other humans are addressed at length in Richard L. Cupp Jr., *Cognitively Impaired Adults, Intelligent Animals, and Legal Personhood*, which will be made available at SSRN.com, and in Richard L. Cupp Jr., *Children, Chimps, and Rights Arguments from "Marginal" Cases*, 45 Az. St. L. J. 1 (2013) [hereinafter *Children & Chimps*].

13 The *Lavery* Brief states that "*Homo Sapiens* membership has been laudably designated a *sufficient* reason for legal personhood. Even the permanently comatose and anencephalic of our human species are entitled to fundamental legal rights under international and American law. However, 'the thesis that humans should be ascribed rights simply for being humans has received practically no support from philosophers.'" *Lavery* Brief, *supra* note 2, at 70 (emphasis in original) (citation omitted), *quoting* Daniel Wikler, *Concepts of Personhood: A Philosophical Perspective*, in Defining Human Life: Medical, Legal, and Ethical Implications 13, 19 (1983). The *Lavery* Brief later states "The NhRP agrees that humans who have never been sentient or conscious nor possessed of a brain *should* have basic legal rights. But *if* humans bereft of autonomy, self-determination, sentience, consciousness, even a brain, are entitled to legal rights, *then* this Court must either recognize Tommy's just equality claim to bodily liberty or reject equality entirely." *Lavery* Brief, *supra* note 2, at 73 (emphasis in original).

14 *See* Richard A. Posner, *Animal Rights*, 110 Yale L. J. 527, 535 (2000) (a secular argument for dichotomizing between humans and animals is that "if we fail to maintain a bright line between animals and human beings, we may end up by treating human beings as badly as we treat animals, rather than treating animals as well as we treat (or aspire to treat) human beings.").

15 Steven M. Wise, Rattling the Cage (2000).

16 Laurence H. Tribe, *Ten Lessons our Constitutional Experience Can Teach us About the Puzzle of Animal Rights: The Work of Steven M. Wise*, 7 Animal L. 1, 7 (2001). Thank you to Justin Beck for highlighting this passage to me in conversation and in his presently unpublished paper addressing animal

personhood issues. Justin Beck, *The Gradual Move Toward Nonhuman Personhood: Assessing the Moral and Legal Implications of the New Animal Rights Movement*, 28-29, 54 (copy on file with author).

17 Steven M. Wise, *Rattling the Cage Defended*, 43 B.C. L. Rev. 623, 650 (2002).

18 *Id.* at 650-51. I disagree with Mr. Wise, and believe that treating humans distinctively makes sense, because the human community is in fact distinctive in important aspects. *See infra* Section 3.

19 In his book Drawing the Line, Mr. Wise seems to argue that, under equality principles, granting rights to a "baby born into a permanent vegetative state" or to a man with an IQ of ten supports granting rights to what he describes as "Category 2" animals in terms of autonomy values (in addition to the animals who may be among the most intelligent, such as great apes). Steven M. Wise, Drawing the Line 237-38, 241 (2002). In Category 2 he includes animals such as dogs, African Elephants, and African Grey Parrots, which are known to probably have relatively strong intelligence. *Id.* at 241. He also asserts that, with animals that are lower on the scale of the probability of practical autonomy, at a point the disparities in autonomy between the animals and a man with very low intelligence "become small enough to allow a judge to distinguish rationally between that creature and a severely retarded man. At some point, the psychological and political barriers to equality for a nonhuman animal with a low autonomy value become insuperable." *Id.* at 238. But what if we consider the baby born into a permanent vegetative state instead of an adult with a severe cognitive disability (who may, despite his disability, have some abilities)? Would an equality argument based on individual autonomy, if accepted, suggest personhood for many, many more animal species that may have autonomy equal to or less than that of an adult with a severe cognitive disability, but more autonomy than that of an infant born into a permanently vegetative state? In light of our recognition of the legal personhood of an infant born into a permanently vegetative state, how many animals would *not* merit personhood if an equality argument based on individual autonomy were accepted?

20 Regarding a possible misconception that acknowledging personhood's foundation in a societal framework of rights and responsibilities could somehow be a threat to humans without the capacity for responsibility, *see infra* Section 3.

21 *Lavery*, 124 A.D.3d at 152.

22 Carl Cohen & Tom Regan, The Animal Rights Debate 30 (2001).

23 Of course, we have in some instances shamefully failed to follow this ideal, such as in allowing the odious institution of slavery. Because noncitizen humans, even noncitizen unlawful enemy combatants, are human, recognizing some rights for them is consistent with our foundational societal principles. We assert some responsibilities for noncitizen humans as they interact with our society in addition to recognizing that they have some rights as they interact with our society. *See also* note 45.

24 The Declaration of Independence (U.S. 1776).

25 American Bar Association Section of Individual Rights and Responsibilities, http://www.americanbar.org/groups/individual_rights.html (last visited June 3rd, 2015).

26 Memorandum of Law in Support of Appellant's Motion for Leave to Appeal to the Court of Appeals, Court of Appeals of the State of New York at 19-22, People ex. rel. The Nonhuman Rights Project v. Lavery, 124 A.D.3d 148 (N.Y.App. Div. Feb. 23, 2015) (No. 518336), http://www.nonhumanrightsproject.org/wp-content/uploads/2015/02/6.-Motion-for-Leave-to-Appeal-and-Affirmation-in-Support.pdf.

27 *Id.*

28 Professor Hohfeld stated, "[S]ince the purpose of the law is to regulate the conduct of human beings, all jural relations must, in order to be clear and direct in their meaning, be predicated of such human beings." Wesley Newcomb Hohfeld, *Fundamental Legal Conceptions as Applied in Judicial Reasoning*, 26 Yale L. J. 710, 721 (1917).

29 "[S]ince Hohfeld's theory is largely descriptive, it does not really tell us what grounds our duties and, thus, what ultimately grounds rights. While Hohfeld's theory may help us to identify and explicate legal issues, it is not a method for determining social and legal philosophical issues." Thomas G. Kelch, *The Role of the Rational and the Emotive in a Theory of Animal Rights*, 27 B.C. Envtl. Aff. L. Rev. 1, 9 (1999).

30 *See Lavery*, 124 A.D.3d at 152; Richard L. Cupp, Jr., *Moving Beyond Animal Rights: A Legal/Contractualist Critique*, 46 San Diego L. Rev. 27, 52-63 (2009).

31 *Lavery* Brief, *supra* note 2, at 73 (emphasis in original).

32 *See Children & Chimps*, *supra* note 12, at 22-28.

33 Regarding animals and humans, Professor Cohen asserts that "[t]he critical distinction is one of kind." Cohen & Regan, *supra* note 22, at 37.

34 *Id.*

35 Of course, individual capacities are relevant to some specific rights (for example, the right to vote). They are not relevant to humans' personhood.

36 Further, the status quo views humans as persons based on their humanity, and infants and other cognitively impaired persons are unquestionably included. It is rejecting this status quo in favor of an approach that denies membership in the human community as the foundation for personhood that would create risk for cognitively impaired humans, not maintaining the status quo.

37 *See, e.g.*, Richard Farson, Birthrights: A Bill of Rights for Children 1 (1978) (asserting that denying rights to children denies "their right to full humanity").

38 *Lavery*, 124 A.D.3d at 152. For a brief discussion of views about the conflicting academic philosophical concepts of "will theory" and "interest theory" for rights in the context of these lawsuits, see Richard L. Cupp Jr., *Focusing on Human Responsibility Rather than Legal Personhood for Nonhuman Animals*, 33 Pace Env. L. Rev. __ (forthcoming 2015).

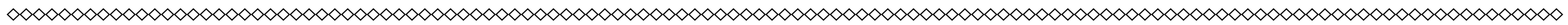
39 "Our goal is, very simply, to breach the legal wall that separates all humans from all nonhuman animals." Nonhuman Rights Project website, *Lawsuit Filed Today on Behalf of Chimpanzees Seeking Legal Personhood*, Dec. 3rd, 2013, *available at* http://www.nonhumanrightsproject.org/2013/12/02/lawsuit-filed-today-on-behalf-of-chimpanzee-seeking-legal-personhood/ (last visited June 5, 2015).

40 *See Children & Chimps*, *supra* note 12, at 21. The Manhattan *Stanley* ruling asserted in a footnote that "the floodgates argument is not a cogent reason for denying relief." The Nonhuman Rights Project v. Stanley, Supreme Court of the State of New York, New York County, Decision and Order, Index. No. 152736/15, July, 29th, 2015, *available at* http://www.nonhumanrightsproject.org/wp-content/uploads/2015/07/Judge-Jaffes-Decision-7-30-15.pdf. The judge cited Enright v. Eli Lilly & Co., 77 NY2d 377, 392-93 (1991), which involved a proposed tort law expansion. Although no pinpoint citation was provided, apparently the court was referencing the dissent in *Enright*. *Id.* at 392-93. (Hancock, J., dissenting). Interestingly, the majority opinion in *Enright* found it appropriate to consider what it viewed as "staggering implications" of the proposed expansion, and the difficulty, if the expansion were accepted, "of confining liability by other than artificial and arbitrary boundaries." *Id.* at 384. In the NhRP lawsuits, courts must consider that there is no basis for determining how far to extend legal personhood among the world's billions of animals if personhood is grounded in a vague intelligence standard.

41 Richard A. Epstein, *Animals as Objects, or Subjects, of Rights*, *in* Cass R. Sunstein & Martha C. Nussbaum, Animal Rights: Current Debates and New Directions 154 (2004).

42 *Letter Brief of Amicus Curiae Laurence H. Tribe in Support of Motion for Leave to Appeal* 3, People ex. rel. The Nonhuman Rights Project v. Lavery, Court of Appeals of the State of New York, Index No. 518336, May 8, 2015, *available at* http://www.nonhumanrightsproject.org/wp-content/uploads/2015/05/Tribe-Amicus-Curiae-Letter-Brief-FINAL.pdf.

43 *Id.* at 4.



44 N.Y. Code section 7002(a). Section 7003, addressing "When the writ shall be issued," also indicates it is for a "person." *Id.* at section 7003(a).

45 This is not inconsistent with allowing habeas corpus and personhood for detainees held by the United States at Guantanamo Bay. The detainees are human. Although American courts have in some situations not granted full personhood to some subsets of humans (such as when the odious practice of slavery was an American institution), because of personhood's focus on humanity American courts have never extended personhood beyond humans and human proxies. *See also supra* note 23.

46 *See supra* note 21 and accompanying text.

47 The Animal Legal Defense Fund has gathered information about the year each state adopted felony animal cruelty provisions. *See* Animal Legal Defense Fund, *U.S. Jurisdictions With and Without Felony Animal Cruelty Provisions*, http://aldf.org/resources/advocating-for-animals/u-s-jurisdictions-with-and-without-felony-animal-cruelty-provisions/ (last visited June 3, 2015). According to the website's list, as of 1990, only six states had adopted felony animal cruelty provisions. *Id.*

48 *South Dakota is Last State to Make Animal Cruelty a Felony*, J. of the Am. Vet. Med. Ass'n News, June 15, 2014, https://www.avma.org/News/JAVMANews/Pages/140615f.aspx, (last visited June 3, 2015).

Environmental Regulation and Natural Resource Management

*By James L. Huffman**

Although opinion polling generally indicates that the environment is low on the list of public concerns, environmental and natural resource policies have a very significant impact on the economy and therefore on the day to day lives of ordinary Americans. Any pro-growth agenda will benefit from attention to environmental regulations and federal natural resource management.

I. Challenges Facing Federal Departments and Agencies with Environmental Responsibilities

Numerous federal departments and agencies have regulatory and management responsibilities relating to the environment and natural resources including, but not limited to, the following: Council on Environmental Quality, Environmental Protection Agency, Department of Interior (Bureau of Land Management, Bureau of Reclamation, National Park Service, U.S. Fish and Wildlife Service), Department of Agriculture (Forest Service, Natural Resources Conservation Service, Office of Environmental Markets), Department of Energy, and Department of Commerce (National Oceanic and Atmospheric Administration).

Federal laws and administrative actions have created a complex array of environment-related regulations and directives that affect virtually every aspect of private and public life. While most environmental regulations have important and legitimate purposes, the monitoring and compliance costs often exceed the public benefits and, like all regulations, those relating to environmental protection and natural resources conservation can be manipulated for the benefit of special interests rather than the public welfare.

Two challenges facing every presidential administration are to achieve the maximum possible coordination and consistency among the many federal agencies and to assure that the private and public costs of regulatory compliance are justified by the resulting public benefits. Given the many agencies involved and the broad range of statutes they are responsible to administer, it is not possible to meet these challenges with top-down policy directives from the White House. Thus, the only realistic approach is to integrate a common set of basic policy principles across the full range of environmental and natural resources agencies–principles that can have application to the regulation of pollution from private industrial sources as well as to the management of publicly owned resources, the control of greenhouse gas emissions, and the preservation of endangered species and natural areas.

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II. The Most Important Environmental and Natural Resources Issues Facing the Next Administration

Several concrete issues are likely to provide the opportunity for a coordinated and coherent approach to environmental protection and natural resource conservation. Continued pressure from environmental groups combined with independent action by state and local governments will require the federal government to act where matters within the scope of federal responsibility are at issue. Foremost among those issues requiring federal action will be climate change, energy, water, federal public lands, and endangered species.

Climate change has become the dominant concern of most mainstream environmental groups, including those with relatively narrow missions like wildlife and wilderness protection. Their concern is that climate change has the potential to alter or destroy whatever environmental amenities and natural resources it is their mission to protect. Climate change has also surfaced as a top priority of the current administration. On June 1 of this year, the Environmental Protection Agency (EPA) promulgated rules implementing its Clean Power Plan. Those rules have been challenged as beyond EPA authority, but if upheld they will have dramatic consequences for the American economy.

Inextricably related to climate change policy is *energy*. Carbon dioxide constitutes over 80 percent of greenhouse gas (GHG) emissions, and nearly 80 percent of those emissions derive from electricity generation, transportation, and industry. Thus, significant reductions in GHG emissions are dependent on rapid and widespread substitution of low carbon for high carbon fuels and on the development of alternative energy sources. There has been growing pressure from environmental groups to close coal-fired generating facilities, and the recent history of subsidized alternative energy sources has created influential interest groups lobbying for the extension and expansion of those subsidies. A growing movement on college campuses is pressuring for disinvestment in companies engaged in carbon related industries.

Also linked to concerns over climate change is *water policy.* Environmental activists attribute the ongoing drought in California and the Southwest and flooding in other parts of the country to climate change. Whether or not climate change has anything to do with these and other weather patterns, the allocation of scarce water resources will be an ever more pressing challenge, and the next administration will be faced with defining the federal role and collaborating with the states in the allocation and management of the nation's water resources.

In the western states, the use and management of the vast *federal public lands*, which constitute on average 50 percent of the land between the Rocky Mountains and the Pacific Ocean, is likely to reemerge as an issue for the next administration. Agricultural and natural resource interests in much of the rural West are pressuring state legislatures to follow the state of Utah's lead and enact legislation calling on the federal government to

transfer control of federal lands to state governments. While there appears to be little likelihood that states will succeed in claiming legal title to federal lands, the effort does evidence a widespread concern in the rural West over the use and management of lands in federal ownership. Because these lands contain significant timber, mineral, water, and grazing resources, there are significant opportunities to stimulate rural economies through improved management.

Directly related to the water and public lands challenges are existing policies relating to the protection of *endangered species*. The Endangered Species Act (ESA) has proven to be a powerful tool for the imposition of constraints on land and resource use with obvious implications for economic development. Because the ESA increasingly constrains alternative energy development and curtails water diversions by large urban areas affecting millions of inhabitants, there are likely to be growing pressures to amend the ESA.

III. Discussion

Political debates over climate change policy usually degenerate into name-calling, with one side labeled extremists and the other deniers. The next administration will have the opportunity to elevate the discussion in the interest of developing a realistic and affordable set of policies to cope with whatever climate change may occur, without regard for whether it is human caused. To the extent reduced reliance on carbon-based fuels and a shift from more carbon-intensive to less carbon-intensive fuels will be cost-effective and beneficial to Americans, measures should be taken to encourage such actions. But it makes little sense to incur enormous taxpayer and social costs where the returns in mitigated climate change will be minimal. The better approach is to prepare for the possible impacts of climate change with strategies for adaptation if and when changes occur, and with an understanding that the predictions are based on models that necessarily simplify extremely complex natural processes.

Because most climate change mitigation strategies that have been proposed would dramatically affect the cost of energy, and because energy costs are a significant factor for virtually all businesses, climate change policies must account for economic effects including innovation, investment, employment, compensation, and the quality of goods and services. Recent innovations in the technology of petroleum extraction ('fracking' and directional drilling) demonstrate that private innovation can have significant environmental benefits (reduced carbon emissions from the substitution of natural gas for coal, for example) as well economic benefits (lower energy costs and new jobs, for example). Although the federal government can play an important role in energy innovation by providing support for basic research, experience suggests that direct federal intervention in the energy market with subsidies and tax breaks only serves to divert private investment into uneconomic energy development. It should also be clear that the best and perhaps only existing large-scale alternative to carbon-based energy fuels is nuclear. Modern nuclear technology has advanced dramatically over the past decade and now has enormous potential for safe electricity generation with minimal environmental harm and zero carbon emissions. Still, existing federal regulations make the costs of new nuclear development prohibitive.

Because water is essential to life and because water sources are usually parts of complex systems of transient and integrated ground and surface waters, the tendency over the last half-century has been to resort to public planning and management of water resources. This tendency has given rise in nearly every region of the country to political struggles over water and a diminished role for the private rights systems that have long existed in all of the states. While there is a necessary role for federal involvement in the allocation of interstate waters, it is important to recognize that historic government policies have contributed to some of the nation's most serious environmental problems, and that private water markets can make an important contribution to the efficient use of water resources.

Federal public land resources have also suffered from a lack of market discipline. Pursuant to various federal laws, vast areas of the public lands have been effectively withdrawn from productive use in favor of environmental preservation and species protection. The impact on rural communities of the West has been devastating. The 1964 Multiple Use Act and the subsequent planning legislation has had the perverse effect of removing economic considerations from management decisions while tying the hands of the government officials with management responsibilities. The Endangered Species Act further constrains land managers by functioning as an effective trump on all other considerations. Efficient use of whatever public land resources are made available for economic use does not require private title, but it does require private rights of use sufficient to justify investment and long-term management.

IV. Unifying Themes

Although the foregoing issues are related to one another (as explained above), they will also seem quite distinct from a political perspective. Different regions of the country will tend to see some issues as more important than others and each of the political interest groups active in these arenas will have a particular policy focus that views the problems and solutions in a given area as unique. But there are unifying themes that should be reflected in the environmental and natural resource policies of the next administration.

1. *Remember that resource scarcity requires trade-offs.* All of the foregoing issues rise to political significance because of resource scarcity. Whether we are talking about water for residents of Los Angeles, timber for mills in Idaho, coal not mined in Pennsylvania, or carbon pollution from New Jersey industries, the challenge exists because resources are limited. Water delivered to Los Angeles is water not available to farmers as distant as Colorado. Trees harvested on public lands to supply mills in Idaho are trees no longer providing habitat for birds and shade for hikers. Coal left in the ground in Pennsylvania denies employment to local miners and requires reliance on other energy sources. Carbon emitted in New Jersey is the byproduct of both jobs and useful products. There are tradeoffs everywhere because resources are scarce and therefore valuable. To the extent federal law requires federal officials to make resource allocation decisions, these tradeoffs must be taken into account. But government policy at all levels must also recognize that central planners cannot possibly account for all of the literally millions of factors affecting supply and demand.

2. *Rely on market forces to make needed trade-offs wherever possible.* Scarce resources could be allocated on a first come first served basis, but the result of that is what Garrett Hardin labeled the "tragedy of the commons"–everyone has incentives to consume what they can and no one has incentives to conserve and manage for the future. The alternatives to this tragedy are only two: we can allocate resources through a political process of some sort, or we can allocate them through market exchanges between willing buyers and sellers. The former requires a distribution of political power; the latter requires a system of private property and contract rights. Environmental harm is evidence that a purely market system will have unacceptable third party impacts. A half century of environmental regulation and over a century of public lands resource management demonstrate that public officials lack the information required for efficient resource allocation and that the processes put in place to acquire information end up creating obstacles to timely decision making. Thus, the allocation of scarce resources requires some combination of political and market approaches.

3. *Be aware of regulations' links to rent-seeking.* To the extent we rely on the political methods of regulation, subsidy (including tax breaks), and public management, rent-seeking will be a persistent reality. Private interests and self-proclaimed public interest advocates will seek political solutions that benefit them. All will insist that they have only the public interest in mind, but pursuit of private advantage is an inevitable aspect of public resource management. The same is true of the resource managers who have careers to think about and their own agendas. Measures can be taken to limit opportunities for private benefit, but the reality is that rent-seeking is pervasive, expensive, and often disruptive of the public purposes that justify public action in the first place.

4. *Focus on incentive effects.* Achieving the right balance between public action and private markets is difficult, to say the least, but a good guiding principle should be to get the incentives right in relation to our public objectives. Getting the most benefit from any given amount of a scarce resource is surely an objective that is widely shared. Markets are demonstrably superior for getting the incentives right in this respect. For markets to work, resources must be effectively owned and ownership must be transferable. To the extent that the resulting resource uses impose unacceptable costs on third parties (like air and water pollution), regulation is necessary and appropriate. But consistent with the theme of getting the incentives right, regulators should rely on market incentives like tradable emissions permits for pollution control, congestion pricing for traffic management, competitive bidding for the allocation of public land resources, and user fees for the provision of public goods and services.

Federalism & Separation of Powers

The Circuit Splits Are Out There—and the Court Should Resolve Them

*By Evan Bernick**

Note from the Editor:

This article argues that the U.S. Supreme Court should resolve a number of circuit splits in consequential cases. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. The Federalist Society seeks to foster further discussion and debate about the issues involved. To this end, we offer links below to briefs in opposition to certiorari in some of the past cases discussed by the author, and we invite responses from our audience. To join the debate, please e-mail us at info@fedsoc.org.

• Brief in Opposition to Petition for Writ of Certiorari, Kagan v. City of New Orleans, No. 14-585 (Jan 21. 2015): http://sblog.s3.amazonaws.com/wp-content/uploads/2015/01/Kagan-Brief-in-Opposition.pdf.

• Brief in Opposition to Petition for Writ of Certiorari, Powers v. Harris, No. 04-716 (2004): http://www.ij.org/images/pdf_folder/economic_liberty/ok_caskets/Respondents-Brief-in-Opposition.pdf.

• Brief in Opposition to Petition for Writ of Certiorari, Heffner v. Murphy, No. 14-53 (Aug. 18 2014): http://sblog.s3.amazonaws.com/wp-content/uploads/2014/09/14-53-Heffner-brief-in-opp.pdf.

Under the circumstances, Chief Justice John Roberts appeared to be in excellent spirits. On June 29, 2012, the morning after he announced a badly fractured decision upholding the Affordable Care Act's individual mandate,[1] the Chief Justice gave a talk at the District of Columbia Circuit judicial conference in which he covered various Court-related topics and took questions from the audience.[2] When asked about the fact that the number of cases argued before the Supreme Court has continued to decline even as the number of petitions for writs of certiorari has increased, Roberts responded that the Court could hear "100 cases without any stress or strain, but the cases just aren't there." He also emphasized that circuit splits are far and away the most important consideration in deciding whether to grant cert petitions.

Three years later, the number of argued cases remains low in comparison with the Court's peak years. In the early 1980s, the Supreme Court decided more than 150 cases per year. In its 2014-2015 term, the Court decided 76, continuing a trend that has long been under observation.[3] In 2009, the Supreme Court advocacy clinic at Yale Law School held a conference to explore the recent docket shrinkage. Professors and practitioners advanced various theories, but as Adam Liptak of the *New York Times* reported, "there emerged nothing like a definitive answer."[4]

And yet, there are a number of glaring (and judicially acknowledged) circuit splits with wide-ranging effects that stand in need of resolution. If the Court is indeed capable of hearing these cases "without any stress or strain," we need to seek to understand why it has not done so. As indicated by the partial survey below, the cases *are* there, and the Court should hear them.[5]

The Court's own Rule 10 sets out the considerations governing review on certiorari. The rule instructs that among "the reasons the Court considers" in deciding whether to grant or deny certiorari are whether a lower court of last resort (a federal court of appeals or a state court of last resort) (1) "has entered a decision in conflict with" another such court on "an important federal question"; (2) "has so far departed from the accepted and usual course of judicial proceedings, or sanctioned such a departure by a lower court, as to call for an exercise of this Court's supervisory power"; (3) "has decided an important question of federal law that has not been, but should be, settled by this Court"; or (4) "has decided an important federal question in a way that conflicts with relevant decisions of this Court."[6] There has been a great deal of research devoted to the question of which of these reasons is most influential, and the presence (or absence) of a circuit split has long been identified as a paramount consideration.[7] In this regard, the Chief Justice's focus on circuit splits was confirmatory rather than revelatory.

To hear Roberts tell it, the reason the Court's docket has shrunk so dramatically is not lack of capacity. His remarks suggest that the Court could and would hear more if it were presented with consequential circuit splits in need of resolution. Is it true that such splits "just aren't there"?

Earlier this year, the Institute for Justice sought review of a First Amendment challenge to a New Orleans law that made it illegal to give a paid tour of the city without first passing a history test and obtaining a license from the government. This law was upheld by the Fifth Circuit in *Kagan v. City of New Orleans*, which found that it did not restrict the tour guides' speech at all and thus applied the rational basis test rather than heightened scrutiny.[8] Subsequently, the D.C. Circuit in *Edwards v. District of Columbia* reached precisely the opposite conclusion about a nearly identical law and struck it down.[9] In *Edwards*, the court reasoned that a law which makes it illegal to speak about points of interest or the history of the city does, in fact, restrict speech and thus merits heightened scrutiny. In reaching this conclusion, Judge Janice Rogers Brown, writing for the panel, pointedly acknowledged and declined to follow

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Kagan.[10] The Fifth Circuit denied a petition for rehearing en banc following the decision in *Edwards*.

The split over whether occupational speech is in fact speech entitled to meaningful constitutional protection affects, not only tour guides, but everyone who speaks for a living—from comedians to consultants to interior designers to therapists.[11] As we move from an industrial to an information economy, more and more and more Americans will earn their livings in occupations that consist primarily in speaking.[12] And yet, on February 23rd, the Supreme Court denied certiorari in *Kagan*, taking a pass on the question of whether the government can effectively deny them the ability to do so.

Yet another example: In *Powers v. Harris*, the Tenth Circuit concluded that a state could impose irrelevant credentialing requirements on casket retailers for the sole purpose of protecting state-licensed funeral directors from competition.[13] Thanks to the so-called[14] rational basis test, the Supreme Court and lower courts have generally turned a blind eye to blatant examples of protectionism. But the Court has always required a "fig leaf" of legitimacy—some assertion, however implausible, of a public-spirited end, like the protection of public health and safety.[15]

In *Powers*, however, the Tenth Circuit welcomed a wolf that came as a wolf, holding that economic protectionism—apart from even a disingenuous public goal—constituted a legitimate government interest.[16] In *Craigmiles v. Giles*, the Sixth Circuit reached the opposite conclusion, holding that economic protectionism, standing alone, is not a legitimate government interest.[17] More recently, in *St. Joseph Abbey v. Castille*, the Fifth Circuit followed *Craigmiles*, holding that mere economic protection of a particular industry is not a legitimate governmental purpose, but rather a "naked transfer of wealth."[18] This is another circuit split, and it touches on an issue of fundamental importance to ordinary Americans across the nation—whether their right to earn an honest living can be extinguished on the basis of a naked governmental preference for entrenched incumbents whose lobbying power they cannot match.[19] And, again, the Supreme Court took a pass.[20]

The circuits also remain divided over how to evaluate laws that burden interstate commerce. So long as the laws do not overtly discriminate between interstate and intrastate commerce, courts apply the test set forth in *Pike v. Bruce Church*, which asks whether the burden imposed on interstate commerce is "clearly excessive in relation to putative local benefits."[21] The test contains an inherent tension—together, the terms "clearly" and "excessive" imply an evidence-based, quantitative analysis, whereas the word "putative"[22] connotes supposition. The (predictable) result is that two directly conflicting lines of authority have emerged. The Second, Third, Eighth, and Tenth Circuits require proof that purported local benefits are both genuine and "credibly advanced."[23] By contrast, the First, Fifth, Ninth, and District of Columbia Circuits require only the assertion of a local benefit by the state, however incredible.[24] The Supreme Court made plain in *Kassel v. Consol. Freightways Corp*. that "(t)he incantation of a purpose to promote the public health or safety does not insulate a state law from Commerce Clause attack."[25] In *Kassel*, the Court concluded that, while the state law restricting the length of tractor trailers was designed to benefit Iowa residents, it burdened interstate traffic too much and was therefore unconstitutional; in reaching that conclusion, the Court carefully scrutinized the evidence in the record.[26] And yet no less than four circuits have held that a bare assertion is sufficient to establish a local benefit. In declining to grant certiorari on this question in *Brown v. Hovatter*, a case involving funeral home regulations, the Court missed an opportunity to resolve this simple but fundamental conflict between multiple circuits—one that threatens to balkanize the unified national market that the Commerce Clause is designed to protect.[27]

Further, despite having heard over 150 rational basis cases since formalizing the test in *United States v. Carolene Products* in 1938, the Supreme Court has yet to decisively answer the question of whether a statute that is rational when passed can be challenged as irrational at a later date if circumstances change. In *Carolene Products*, the Court unambiguously stated that "the constitutionality of a statute predicated upon the existence of a particular state of facts may be challenged by showing to the Court that those facts have ceased to exist."[28] But the Supreme Court has not consistently affirmed that the rationality of the government's actions must be determined on the basis of presently existing facts in rational basis cases—indeed, it has implied that they do not. In *FCC v. Beach Communications*, for instance, the Court stated that "legislative choice is not subject to courtroom fact-finding" and that legislation should be upheld if any "conceivable state of facts" could justify it.[29] Lower courts are understandably confused—some circuits continue to follow the changed-circumstances doctrine articulated in *Carolene Products*,[30] while others look solely at whether the statute could be thought rational when it was passed.[31] If the rational basis test—the default rule in constitutional cases—is to be a meaningful test, the Court must clarify that facts matter in every constitutional case. Yet last year the Court declined to review *Heffner v. Murphy*, a decision in which the Third Circuit upheld archaic laws that force funeral directors to (among other things) spend tens of thousands of dollars building useless "preparation rooms" because those laws could have been thought rational in 1952.[32]

There are also several unresolved splits regarding the Second Amendment, including splits over whether the Second Amendment guarantees the right to carry a handgun outside the home;[33] whether states need to offer evidence in support of laws burdening the right to bear arms;[34] and whether consumers have standing to challenge federal restrictions on gun sales.[35] In *McDonald v. Chicago,* the Court affirmed that the Second Amendment protects a personal right to bear arms, and that that right is not a "second-class right," but is rather "among those fundamental rights necessary to our system of ordered liberty."[36] Law-abiding citizens seeking to exercise that right deserve better than this state of uncertainty.

There is also a fundamental disagreement over how carefully trial judges, acting in their capacity as "gatekeepers," should scrutinize expert testimony before admitting it. Federal Rule of Evidence 702 requires that judges determine both that the expert relied upon "reliable principles and methods" and that "the expert reliably applied the relevant principles and methods to the facts of the case." In *Daubert v. Merrell Dow Pharmaceuticals* (1993), the Supreme Court made plain that, as part of their gatekeeping function, judges must ensure that expert

testimony "both rests on a reliable foundation and is relevant to the task at hand."[37] But the Seventh, Eighth, and Ninth Circuits have adopted the view that faults in an expert's methodology generally go to the weight of the expert's opinions, not their admissibility—thus delegating the gatekeeping function to the jury.[38] In contrast, the Second, Third, Sixth, and Tenth Circuits have adopted the bright-line rule that "any step that renders the analysis unreliable under the *Daubert* factors renders the expert's testimony inadmissible, whether the step completely changes a reliable methodology or merely misstates that methodology."[39] This circuit split has resulted in the lack of any uniform rule when it comes to scrutinizing expert testimony in federal courts.

These are not obscure circuit splits of interest only to constitutional law aficionados. They leave the rights of millions hanging in the balance. Questions about whether naked wealth transfers merit more than a judicial rubber stamp or whether the price of pursuing a vocation is the abandonment of one's right to speak freely are pressing and fundamental, and certainly worthy of the attention of a Court that (to hear the Chief Justice tell it) could easily hear some thirty additional cases. While it is true that some issues benefit from percolating in the lower courts before the Supreme Court wades in, that is an insufficient explanation for the Supreme Court's refusal to resolve consequential issues that have long been ripe for review. After years of fruitless efforts to solve the mystery of docket decline, it is time to subject the Court's inaction to exacting scrutiny.

Endnotes

1 *See* Nat. Fedn. of Indep. Business v. Sebelius, 567 U.S. 1 (2012).

2 Del Quentin Wilber, *After the Health Care Ruling, Roberts Jokes But Declines to Talk About the Decision*, Washington Post (June 29, 2012), http://www.washingtonpost.com/local/crime/after-the-health-care-ruling-roberts-jokes-but-declines-to-talk-about-the-decision/2012/06/29/gJQAzOHfBW_story.html (last visited August 10, 2015).

3 *See* David R. Stras, The Supreme Court's Declining Plenary Docket: A Membership-Based Explanation, 27 Const. Comment. 151 (2009); Margaret Meriwether Cordray & Richard Cordray, The Supreme Court's Plenary Docket, 58 Wash. & Lee L. Rev. 737 (2001); Arthur D. Hellman, The Shrunken Docket of the Rehnquist
Court, 1996 Sup. Ct. Rev. 403 (1996).

4 Adam Liptak, *The Case of the Plummeting Supreme Court Docket*, New York Times, (September 28, 2009), http://www.nytimes.com/2009/09/29/us/29bar.html?_r=0 (last visited April 5, 2015).

5 To help focus attention on this seeming anomaly, the Institute for Justice's Center for Judicial Engagement is planning to hold a conference at which professors and practitioners will identify and discuss the existence of circuit splits that have been presented to the Court, but that it has refused to resolve.

6 Sup. Ct. R. 10.

7 *See* Gregory A. Caldiera & John R. Wright, The Discuss List: Agenda Building in the Supreme Court, 24 Law & Soc'y Rev. 807 (1990) (finding that the existence of an actual conflict between the lower courts or between the lower Court and a Supreme Court precedent is a potent determinant of whether the Court grants certiorari).

8 753 F.3d 560 (5th Cir. 2014).

9 755 F.3d 996 (D.C. Cir. 2014).

10 Id. at 1009 n.15 ("We are of course aware of the Fifth Circuit's contrary conclusion… We decline to follow that decision, however, because the opinion either did not discuss, or gave cursory treatment to, significant legal issues.").

11 The Third Circuit and the Ninth Circuit have also taken differing approaches in cases involving sexual orientation change efforts (SOCE) performed by licensed counselors. This "talk therapy" consists largely in speech. But in Pickup v. Brown, 728 F.3d 1042 (9th Cir. 2013), the Ninth Circuit applied rational basis review to a law which prohibited counselors from engaging in SOCE with clients under 18, reasoning that the ban regulates only "conduct," not speech. In King v. Governor of the State of New Jersey, 767 F.3d 216 (3d Cir. 2014), the Third Circuit considered a similar ban and expressly disagreed with the Ninth Circuit's analysis. Following the Supreme Court's lead in Holder v. Humanitarian Law Project, 561 U.S. 1 (2010), the Third Circuit in King rejected the proposition that verbal communications are transformed from speech into "conduct" when they are used to deliver professional services, applying intermediate scrutiny rather than the rational basis test. The Third Circuit went on to uphold the ban, finding that it directly advanced the important government interest of preventing harm to minors.

12 *See generally* Alvin Toffler, The Third Wave (1980).

13 *See* Powers v. Harris, 379 F.3d 1208 (10th Cir. 2004).

14 *See generally* Clark Neily, No Such Thing: Litigating Under the Rational Basis Test, 1 N.Y.U. J.L. & Liberty 898 (2005) (describing the history and present state of the rational basis test and contending that it is not a meaningful "test" at all).

15 The Court has upheld laws barring people who are not licensed optometrists or opthalmologists from replacing broken lenses; denying pilotage licenses to anyone who is not a friend or relative of an incumbent pilot; and banning all pushcart vendors from a popular tourist location except those who had been there for more than eight years. Williamson v. Lee Optical of Okla., Inc., 348 U.S. 483 (1955); Kotch v. Board of River Port Pilot Comm'rs for Port of New Orleans, 330 U.S. 552 (1947); New Orleans v. Dukes, 427 U.S. 297 (1976). In all of these cases, the Court took the government's profession of public-spirited ends at face value.

16 *See* Powers, 379 F.3d at 1220 (holding that "protecting or favoring one particular intrastate industry… is a legitimate state interest").

17 *See* Craigmiles v. Giles, 312 F.3d 220 (6th Cir. 2002).

18 *See* St. Joseph Abbey v. Castille, 712 F.3d 215, 223 (5th Cir. 2013).

19 *See generally* Cass R. Sunstein, Naked Preferences and the Constitution, 84 Colum. L. Rev. 1689 (1985) (discussing how many of the most important clauses of the Constitution focus on a single underlying evil: "the distribution of resources or opportunities to one group rather than another solely on the ground that those favored have exercised the raw political power to obtain what they want.").

20 This split has since deepened. In April 2015, the Second Circuit Court of Appeals upheld a patently anticompetitive restriction on non-dentist teeth-whiteners in Connecticut. Writing for himself and another judge on the panel, Judge Guido Calabresi claimed that a "simple preference for dentists over teeth-whiteners" would constitute a legitimate state interest, even if the challenged rule did not—and was not designed to—promote public health. *See* Sensational Smiles v. Mullen, No. 14–1381–CV, 2015 WL 4385295 (2nd Cir. April 15, 2015).

21 Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970).

22 *See* Bryan A. Garner, A Dictionary of Modern Legal Usage 721 (2d ed. 1995) (defining putative as "supposed, believed, reputed").

23 Southhold v. E. Hampton, 477 F.3d 38 (2d Cir. 2007); Lebanon Farms Disposal, Inc. v. County of Lebanon, 538 F.3d 241 (3d Cir. 2008); R & M Oil & Supply, Inc. v. Saunders, 307 F.3d 731 (8th Cir. 2002); Blue Circle Cement, Inc. v. Saunders, 27 F.3d 1499 (10th Cir. 1994).

24 Pharm. Care Mgmt. Ass'n v. Rowe, 429 F.3d 294 (1st Cir. 2005); All State

Ins. Co. v. Abbott, 495 F.3d 151 (5th Cir. 2007); Spoklie v. Mont., 411 F.3d 1051 (9th Cir. 2005); Electrolert Corp. v. Barry, 737 F.2d 110 (D.C. Cir. 1984).

25 Kassel v. Consol. Freightways Corp., 450 U.S. 662, 670 (1981) (plurality opinion).

26 Id. at 672.

27 Brown v. Hovatter, 561 F.3d 357 (4th Cir. 2009), *cert. denied* 130 S. Ct. 741 (2009).

28 United States v. Carolene Products, 304 U.S. 144, 152 (1938). *See also* Borden's Farm Prods. Co. v. Baldwin, 293 U.S. 194, 210 (1934) (holding that where a statute is challenged under the rational basis test, the validity of that statute is "properly the subject of evidence and of findings").

29 508 U.S. at 315. *See also* Heller v. Doe, 509 U.S. 312, 320-1 (1993) (stating that rational basis does not require "foundation in the record").

30 *See* Long v. Robinson, 316 F. Supp. 22, 27-28 (D. Md. 1970), *aff 'd*,436 F.2d 1116 (4th Cir. 1971); Seaboard Air Line R.R. Co. v. City of West Palm Beach, 373 F.2d 328 (5th Cir. 1967); United States v. Moore, 644 F.3d 553 (7th Cir. 2011); Dias v. City & Cnty. of Denver, 567 F.3d 1169 (10th Cir. 2009).

31 *See* United States v. Then, 56 F.3d 464 (2d Cir. 1995); Burlington N. R.R. Co. v. Dep't of Pub. Serv. Regulation, 763 F.2d 1106 (9th Cir. 1985).

32 Heffner v. Murphy, 745 F.3d 56 (3d Cir. 2014), *cert. denied* 135 S.Ct. 220 (2014).

33 The Second, Fourth, Fifth, and Seventh Circuits have held or assumed that the Second Amendment encompasses the right to carry handguns outside the home for self-defense. Kachalsky v. Cnty. of Westchester, 701 F.3d 81, 93 (2d Cir. 2012); Woollard v. Gallagher, 712 F.3d 865, 876 (4th Cir. 2013); Nat'l Rifle Ass'n of Am., Inc. v. McCraw, 719 F.3d 338 (5th Cir. 2013); Moore v. Madigan, 702 F.3d 933 (7th Cir. 2012). The Third Circuit has refused to recognize this right. Drake v. Filko, 724 F.3d 426 (3d Cir. 2013), *cert. denied* 134 S.Ct. 2134 (2014).

34 The First, Second, Fourth, Seventh, and District of Columbia Circuits require evidence. United States v. Booker, 644 F.3d 12, 25 (1st Cir. 2011); Kachalsky v. Cnty. of Westchester, 701 F.3d 81 (2d Cir. 2012); United States v. Chester, 628 F.3d 673 (4th Cir. 2010); Ezell v. City of Chicago, 651 F.3d 684 (7th Cir. 2011); [DC Cir. cite]. While the Fifth, Ninth, and Tenth Circuits have not explicitly held that the government may only meet its burden with actual evidence, their decisions leave little doubt that at least some supportive evidence is expected. Nat'l Rifle Ass'n of Am., Inc. v. Bureau of Alcohol, Tobacco, Firearms & Explosives, 700 F.3d 185 (5th Cir. 2012); United States v. Chovan, 735 F.3d 1127 (9th Cir. 2013); United States v. Reese, 627 F.3d 792 (10th Cir. 2010). The Third Circuit does not require evidence. Drake, 724 F.3d. at 438.

35 The Fifth and District of Columbia Circuits have held that consumers do have standing. NRA of Am. v. BATFE, 700 F.3d 185 (5th Cir. 2012); Dearth v. Holder, 641 F.3d 499 (D.C. Cir. 2011). The Fourth Circuit has held that they do not. Lane v. Holder, 703 F.3d 668 (4th Cir. 2012), *cert. denied* 134 S.Ct. 1273 (2014).

36 McDonald v. City of Chicago, 561 U.S. 742, 780, 778 (2010).

37 Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579, 596 (1993).

38 Manpower, Inc. v. Ins. Co. of Penn., 732 F.3d 796 (7th Cir. 2013); Johnson v. Mead Johnson & Co., 754 F.3d 557 (8th Cir. 2014); SQM N. Am. Corp. v. City of Pomona, 750 F.3d 1036 (9th Cir. 2014).

39 Amorgianos v. Nat'l R.R. Passenger Corp., 303 F.3d 256, 265-270 (2d Cir. 2002); In re Paoli R.R. Yard PCB Litig., 35 F.3d 717 (3d Cir. 1994); Tamraz v. Lincoln Electric Co., 620 F.3d 665, 670 (6th Cir. 2010); Attorney General of Oklahoma v. Tyson Foods, Inc., 565 F.3d 769 (10th Cir. 2009).

Financial Services & E-Commerce

The Consumer Financial Protection Bureau and the Return of Paternalistic Command-and-Control Regulation

By Todd J. Zywicki

Note from the Editor:

This article examines and critiques the regulatory strategies employed by the Consumer Financial Protection Bureau. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. However, when we do, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• Danny Vinik, *Payday Loans Are Bleeding American Workers Dry. Finally, the Obama Administration Is Cracking Down.*, The New Republic (February 11, 2015), http://www.newrepublic.com/article/121034/consumer-financial-protection-bureau-will-soon-regulate-payday-lending.

• John Wasik, *The CFPB: Main Street's Best Friend in Government*, Forbes (March 14, 2013), http://www.forbes.com/sites/johnwasik/2013/03/14/the-cfpb-main-streets-best-friend-in-government/.

• Lydia Wheeler, *Small Payday Lenders Appeal to Lawmakers for Help with CFPB*, The Hill (August 17, 2015), http://thehill.com/regulation/finance/251290-small-payday-lenders-appeal-to-lawmakers-for-help-with-cfpb.

• *CFPB*, Mercatus Center, http://mercatus.org/tags/cfpb.

I. The Return of Command-and-Control Regulation at the Consumer Financial Protection Bureau

A centerpiece of the Dodd-Frank financial reform legislation was the establishment of the Consumer Financial Protection Bureau (CFPB), a new consumer protection super-regulator with the power to control the terms and offerings of every consumer financial product in America, from expensive complex mortgages offered by trillion-dollar international banks to short-term small-dollar loans by local payday lenders and routine debt collection. Moreover, because many small and start-up businesses are funded by the entrepreneur's personal credit, the CFPB has effectively become the regulator of much of the economy's small business credit as well. The White House press release issued contemporaneously with the CFPB's March 2015 announcement of plans for new stringent regulations on payday lending summed up: "One of the most critical components of the Wall Street Reform bill passed by Congress in 2010 and signed by the President was the creation of the Consumer Financial Protection Bureau (CFPB), a dedicated, independent cop on the beat with the single goal of protecting consumers from threats like abusive practices of unscrupulous lenders or the fraudulent practices of debt collectors."[1]

II. Agency Rules and Approach

According to its own materials, the CFPB touts itself as a "21st century, data-driven agency,"[2] and its proponents argue that it will take a "market-based approach" to regulation, seeking to make markets work better instead of replacing markets, through product bans, substantive regulation of specific terms of contracts, and the like.[3] In practice, however, the CFPB has quickly evolved into an old-fashioned command-and-control paternalistic regulator. Moreover, as a result of the combination of the CFPB's extremely broad authority and a lack of accountability from traditional oversight by the President or Congress, the CFPB's archaic regulatory approach holds potential for extreme harm to consumers and the economy. Its adoption of discredited command-and-control regulatory strategies is especially tragic in that, prior to Dodd-Frank, the federal system of consumer financial protection was in dire need of reform. Consumer financial regulation should have been systematized and modernized in light of sound economics and a more institutionally streamlined and coherent regulatory approach that could not only unify federal consumer financial protection policy, but also encourage federal and state policies to work together more effectively for the benefit of consumers. Instead, the CFPB's approach resembles a Nixon-era regulatory dinosaur frozen in ice and thawed out to try to regulate our 21st century economy.

III. Context: Consumer Financial Protection Regulation: Old and New Approaches

While legal rules governing the U.S. economy broadly support freedom of contract, the CFPB's command-and-control approach is more consistent with the historical approach of consumer financial protection law, which was defined by substantive regulation of terms and conditions of consumer financial products. Most notably, regulators around much of the world long regulated the maximum allowable interest rates for consumer credit products under "usury" laws that prohibited rates of interest regulators deemed excessive, purportedly to protect low-income and improvident borrowers from excessive costs and use of credit.[4] Following Jeremy Bentham's criticism of price controls on interest rates in the eighteenth century, however, a consensus emerged among economists that price controls on interest rates harmed consumers by forcing lenders

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to adjust other terms of the contract (such as requiring larger down-payments or larger loan amounts), by distorting the consumer credit market (favoring retailers that could increase prices of goods to offset credit losses), and by reducing credit availability to higher-risk borrowers (which increased their dependence on loan sharks and lower-quality credit products such as pawn shops). Apart from their inefficiency, usury ceilings' ill effects fall hardest on their supposed beneficiaries—low-income consumers—who are the first to lose credit choices when regulation tightens access to credit. Economic analysis has stressed that the distorting effects of command-and-control regulation of terms applies not just to regulation of interest rates but to restraints on any freely-bargained term of a consumer credit contract.

This recognition of the failure of command-and-control regulation led to a movement in the 1960s and 1970s toward disclosure requirements in place of substantive restrictions on products and terms, best exemplified by the enactment of the Truth in Lending Act. Disclosure regulation rests on the presumption that, rather than dictating terms and conditions of credit, regulators should try to work within the market structure by providing standardized disclosure formats and similar tools that will enable consumers to comparison shop among different providers of credit. This vision of disclosure regulation, however, fell victim to litigation, regulatory excess, and a preference for disclosure rules intended to shape consumer behavior rather than disclosure requirements that enable informed consumer choice.

The CFPB's resuscitation of a command-and-control approach to regulation is a self-conscious return to the regulatory approach of the past. The CFPB, as proposed by now-Senator Elizabeth Warren and others, was modeled on the Consumer Products Safety Commission, which has the power to ban and recall consumer products deemed to be "unsafe." Indeed, in advocating for the new agency, Warren once expressly analogized the regulation of subprime mortgages to unsafe toasters that explode when used, oblivious to the obvious differences between the products.[5]

Although the CFPB is expressly barred by Dodd-Frank from setting interest rate ceilings, its archaic approach to consumer financial protection is seen in a variety of other substantive areas. For example, its "Qualified Mortgages" and "Ability-To-Repay" rules essentially dictate the mortgage terms and borrower conditions which it deems to be "safe" mortgages for consumers. Yet at the same time, the rules do nothing to address the primary cause of the foreclosure crisis—the prevalence of underwater mortgages that provided consumers with an incentive to default when their homes fell in price—such as by requiring larger down payments, limiting cash-out refinancing, or recognizing the effects of state anti-deficiency laws that limit a borrower's personal liability upon mortgage default. The CFPB is also proposing rules on payday loans, auto title loans, installment loans, and other products that would force lenders to assess a borrower's ability to repay small-dollar loans before extending them, essentially eliminating (or sharply curtailing) those products from the marketplace.[6] With respect to auto loans issued by auto dealers, the CFPB is using its leverage over banks to try to restrict the opportunity for borrowers to negotiate over loan terms, because bargaining ability may result in pricing differences that have disparate impact on borrowers. Although enacted prior to Dodd-Frank, the Credit CARD Act of 2009 similarly regulates the terms of credit card accounts, such as limiting the size and incidence of certain behavior-based fees and limiting the ability of issuers to reprice interest rates when consumers' credit risks change.

The CFPB also appears prepared to take steps that would nullify pre-dispute arbitration clauses in consumer credit contracts, thereby opening the market to increased class action litigation. The "Durbin Amendment" to the Dodd-Frank financial reform legislation places price controls on the interchange fees of debit cards issued by banks with over $10 billion in assets, cutting those fees approximately in half and reducing bank revenues by an estimated $6-$8 billion annually. Finally, although the CFPB is barred from fixing interest rate ceilings, the Department of Defense has been authorized to do so with respect to members of the military, and it has extended the terms of the Military Lending Act to apply its 36% interest rate ceiling to virtually every consumer credit product used by military members.

IV. Effects of Command-and-Control Regulation for American Consumers

The effects of the command-and-control approach to consumer financial protection have been disastrous for consumers. For example, studies have found that implementation of the CARD Act accelerated interest rate increases on all credit card accounts and reduced access to credit cards (which has since fallen by 11 percent among low-income households). The Qualified Mortgages rule slowed recovery of the housing market by creating a massive layer of regulatory red-tape and liability risk for banks. And, despite the CFPB's pledge to examine the cost and availability of alternative sources of short-term credit for consumers before imposing new restrictions on payday loans, the CFPB appears ready to force these products out of the market without any evident replacement for the millions of Americans who rely on them to make ends meet. The problems visited on consumers are not entirely attributable to administrative decisions; for instance, large banks facing massive revenue losses from the Durbin Amendment have compensated with more and higher bank fees on consumers—free checking accounts have shrunk from 76% of all bank accounts to only 38%, and fees on bank accounts, such as monthly fees and overdraft fees, have risen substantially. This loss of access to free checking has been particularly problematic for low-income consumers who cannot afford the higher fees or the higher minimum balances necessary to avoid those fees. According to the FDIC, the number of unbanked American consumers rose by 1 million from 2009-2011, and the number of underbanked consumers rose even more, in part because of their loss of access to mainstream financial products as a result of the Durbin Amendment, the CARD Act, and various regulations.

In addition, the regulatory weight of the CFPB has tilted retail banking markets against smaller banks that cannot afford the new regulatory compliance costs associated with its many regulations and litigation risk. A study by the Mercatus Center at George Mason University found that 71% of small banks stated that the CFPB has affected their business activities.[7] Sixty-

four percent of small banks reported that they were making changes to their mortgage offerings because of Dodd-Frank, and 15% said that they had either exited or were considering exiting residential mortgage markets entirely. Nearly 60% of small banks reported that the CFPB and/or the Qualified Mortgages rule had a "significant negative impact" on their mortgage operations. More than 60% said that changes in mortgage regulations had a significant negative effect on bank earnings. Driving smaller banks from the market reduces competition and consumer choice, hurting all consumers; moreover, community banks serve a particularly crucial role in smaller, rural communities, making their loss particularly painful for those consumers and small businesses.

This kind of regulation also stifles innovation and creativity. For example, the Qualified Mortgages rule forces all mortgages into a one-size-fits-all set of underwriting criteria. In so doing, the rule has deprived community banks of their one competitive advantage against megabanks: their intimate familiarity with their customers and their ability to engage in relationship lending with their customers and to tailor loans to the needs of their customers. Similarly, the Durbin Amendment applies to prepaid cards issued by covered banks if those cards provide a level of functionality comparable to bank accounts; this shadow of the Durbin Amendment has deterred the largest banks from developing low-cost, no-frills prepaid and mobile bank products that could provide an alternative to expensive bank accounts for lower-income consumers.

V. What Should Be Done

America's consumer financial protection regime was in need of an overhaul prior to Dodd-Frank. Instead of updating the regime, the CFPB is attempting to impose 19th century regulatory approaches on a 21st century consumer credit economy. Consumers today have unprecedented choice, flexibility, and information about the products and services that they use. Consumer credit is no exception.

A modern regulatory strategy would begin with understanding the success of market economies, especially that of the United States, identifying the particular market failure the regulator seeks to address, and then designing crisply tailored regulation that addresses the problem with a minimum of unintended consequences. Many prior bases for regulation have been obviated or reduced in the modern world. For example, there are multiple credit card comparison websites (such as cardhub.com) that compile and assess the various terms of credit card offers and enable consumers to shop for cards according to the terms that they find most valuable, including interest rates, rewards, and even particular terms like fees on foreign transactions. Credit card issuers recognize the vast heterogeneity of credit card customers and tailor their products to the needs of consumers. These comparison websites have arisen to help consumers find the particular card offerings that they want. In this context, heavy-handed regulation is both unnecessary and detrimental.

For products such as payday loans, concern about vulnerable consumers with limited options are understandable, but regulatory solutions that further deprive these consumers of choices often harm those consumers that the regulations are purportedly intended to help. Surveys of payday loan customers reveal that they fully understand the terms and price of their choices; there is no compelling evidence that users of these products would be better off without such loans. Although the evidence is mixed, studies suggest that banning payday loans leads to more bounced checks and greater use of overdraft protection (which is often more expensive than payday loans) and may lead to more evictions and utility terminations.

The centerpiece of a modern consumer financial protection regime should be focused on encouraging competition, consumer choice, and innovation. Command-and-control regulation of consumer financial products, from the Durbin Amendment to new proposed regulations on payday loans, will have the opposite effect—reducing choice, competition, and innovation. Perhaps most tragically, these regulations typically fall hardest on the most vulnerable American consumers, taking away choices from those consumers who already face limited choices as a result of their situations in life. Ill-considered regulations are driving mainstream financial products such as credit cards and bank accounts out of the reach of low-income consumers, pushing those consumers into the alternative financial sector of check cashers, pawn shops, and payday lenders. As has happened so often in the past, paternalistic regulations intended to help consumers end up hurting them.

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Intellectual Property

The Costs of Patent Reform: Early Data and Abuses in the Uneven Playing Field of Post-Issuance Review

By Greg Dolin[*]

Note from the Editor:

This article is a critical examination of patent reform. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. However, when we do, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

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Introduction

Mark Twain once wrote "that a country without a patent office and good patent laws was just a crab, and couldn't travel any way but sideways or backways."[1] This attitude was shared by our country's founders and generations since, and it is not surprising that throughout our history Congress has tried various approaches to improve our patent laws. In recent years there has been much discussion about patent quality, and the 2011 Leahy-Smith America Invents Act ("AIA") included several provisions ostensibly geared toward improving patent quality.[2]

With the AIA, Congress attempted to improve patent quality by increasing the opportunities for the United States Patent & Trademark Office (PTO) to reevaluate its own patent grants. Specifically, Congress created new administrative post-issuance review programs at the PTO that could be used to invalidate previously-granted patents. Unfortunately, in establishing these new programs, Congress focused almost exclusively on the purported quality benefits of the "second look" to weed out "bad" patents, but failed to fully appreciate the costs of these new programs. Making matters worse, what Congress created was not just a "second look" but also a "third," "fourth," "fifth," etc., look. As we increase the number of chances to invalidate potentially improperly-granted patents, we also increase the corresponding danger of invalidating legitimate patents and create costly uncertainty.[3] The AIA was supposed to give the PTO a "toolbox" of new proceedings to weed out "low quality patents," but in doing so, it impaired the rights of legitimate patent holders by substantially increasing the costs of defending properly-issued patents, and by creating opportunities for abuse.

At the outset, it is worth noting that today's clamor over "low quality patents" is by no means a new complaint. Indeed, allegations that the Patent Office issues "useless patents" that result in "onerous litigation" have been with us for over 200 years.[4] And while it is true that the PTO can make mistakes or be defrauded by unscrupulous applicants, there is no evidence that "low quality" patents are overly-prevalent today or that they cause any significant economic problems.[5] Indeed, there is not even a settled definition of what constitutes a "low quality" patent (as opposed to "high" or "medium quality" one).[6] To be sure, there are plenty of anecdotes and popular press stories about silly patents, such as patents claiming a "Method for Exercising a Cat" or a "Method for Swinging on a Swing." What is absent is any reliable empirical evidence that low quality patents actually present a significant problem in our patent system.

All of this means that when Congress created the AIA's post-issuance review mechanisms to solve the "problem" of "low quality patents," it was far from clear that there was actually a problem in need of solving. Even assuming that there was a problem, and that it was serious enough to warrant a legislative solution, the solution offered ended up imposing costs on legitimate patent holders that appear way out of proportion to the alleged problem of bad patents. Moreover, the AIA's post-issuance review mechanisms have significantly amplified

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opportunities for patent challengers to abuse the system to the detriment of legitimate patent holders. To understand why, it helps to first look at the arsenal of weapons that are available to invalidate a patent.

I. Avenues for Patent Invalidation

a. Ex Parte Reexamination

Historically, when the government issued a patent, the patent had a presumption of validity and only a court could invalidate it.[7] In 1981, after decades of debating the issue, Congress created a new system that allowed patents to be invalidated in administrative proceedings–the ex parte reexamination process ("reexamination").[8] Congress' primary goals in creating the reexamination process were (1) providing more certainty about patent validity, and (2) creating a cheaper substitute for litigation.[9]

In many ways, the reexamination process resembles the procedure used to obtain a patent in the first place. Once the PTO orders the patent into reexamination, the process proceeds ex parte and the patent holder is put in the same position as a patent applicant, which includes the ability to amend the claims.[10] The only major difference between reexamination and the original process for obtaining a patent is the limits placed on reexamination. Whereas an initial patent application can be rejected for failure to comply with any of the Patent Act's requirements, reexamination can only address questions of novelty and obviousness (Sections 102 and 103 of the Patent Act, respectively).[11] This limitation has generated significant criticism over the years. As soon as reexamination was created, a leading patent practitioner argued that "reexamination will come up short, and actually fail to perform its intended function of 'improv[ing] the reliability of reexamined patents.'"[12] Importantly, because of its limited nature, reexamination is not a full substitute for litigation. At the same time, the reexamination procedure can be, and frequently is, used to impose significant costs and delays on patent holders.[13]

The reexamination process begins with a patent challenger submitting a petition to the PTO that outlines why the patent in question is invalid in light of prior patents or publications (the "prior art"). The PTO then evaluates the petition and grants reexamination if there appears to exist a "substantial new question of patentability" with respect to any of the patent claims identified in the petition. While on the surface, the "substantial new question of patentability" seems like a significant bar, in reality it is not. The PTO grants more than 90% of all reexamination petitions.[14]

Once a reexamination petition is granted, the process is conducted without participation by the third-party requester. That means that the cost to the requester of the examination is simply the fee for the request plus the cost of the prior art search and the opinion letter explaining why the claims are invalid in view of the discovered prior art.[15] The cost to the patent holder, on the other hand, is much more significant. Not only will the patent holder have to respond to the initial reexamination filing, he will also have to spend significant resources to essentially re-prosecute the claims in the Patent Office.[16]

Furthermore, even if the patent holder successfully defends against a reexamination challenge, that does not insulate him from subsequent challenges. Indeed, some attorneys have advised their clients to withhold a handful of prior art references during the initial reexamination request so that they can request additional reexaminations (at substantial cost to the patent holder) should the first proceeding be resolved in the patent holder's favor.[17] The marginal cost to the challenger for these piecemeal submissions is minimal (beyond another reexamination request fee), but the cost to the patent holder is roughly the same for each individual proceeding. This reexamination "stacking" allows challengers to keep patents in limbo for indefinite periods of time. And while a patent in the midst of a reexamination does remain enforceable, in practice most judges will stay litigation while reexamination is pending. All of these factors result in reexamination being an *adjunct* rather than an *alternative* to litigation.[18]

The upshot is that reexamination failed to achieve Congress's goals. Because of its limited nature, it failed to provide a substitute to litigation. As a result, it *increased*, rather than decreased the costs and duration of disputes,[19] in direct contradiction of Congress' intent in creating the system. It also failed to provide more certainty about the validity of issued patents. Surviving reexamination does not insulate a patent holder against litigation, nor does winning a judgment of validity in litigation insulate against reexamination.[20] Indeed, on average, a patent that is subject to reexamination is reexamined twice, with some being reexamined as often as four, five, or even six times.[21] All of these shortcomings stemmed from the following flaws in the patent reexamination system: 1) the lack of a meaningful threshold to initiate the process; 2) the lack of estoppel provisions either in civil suits or in subsequent proceedings at the PTO; which in turn results in 3) the lack of certainty about the validity of the patent following reexamination; 4) disproportionate costs on the patent holders; and 5) excessive length of the process itself.

b. The AIA's New Administrative Review Procedures

Congress sought to address each of these shortcomings in the new administrative review procedures it created under the AIA. The AIA was supposed to give the Patent Office a "toolbox" of new proceedings to "weed out low quality patents . . . includ[ing] post-grant review, *inter partes* review, supplemental examination, and derivation proceedings, as well as a transitional post-grant review program for certain business methods patents."[22] Each of these procedures provided new avenues for patent challengers to attack issued patents, and did so without closing the option of an ex parte reexamination. As of 2014, the two most used proceedings are the inter partes review ("IPR") and the covered business method review ("CMBR") program. The new post-grant review ("PGR") program is only applicable to patents with a filing date of March 16, 2013 or later.[23] Given that very few patents filed on or after that date have issued already, PGR is not yet prevalent. Nonetheless, as more and more patents filed after that date are issued, all of the criticisms identified below may well be applicable to the PGR procedure as well.

Both IPR and CBMR sought to address the complaints about reexamination while creating low-cost alternatives to litigation.[24] To that end, both mechanisms created estoppel

provisions and deadlines for resolving disputes.[25] Unfortunately, the estoppel provisions are proving to be easily avoidable, and the new review mechanisms are exacerbating rather than solving pre-existing problems.

i. Inter Partes Review (IPR)

Inter partes review can be filed by any person (other than the patent holder) and can be used to challenge any claim of an issued patent.[26] IPR cannot be requested if the petitioner has previously filed a suit in federal court challenging the validity of the patent, but it is permissible to file an IPR request first and then subsequently file suit in federal court.[27] While an IPR is pending, the federal court action is automatically stayed unless the patent holder either waives a stay or brings his own infringement counterclaims.[28] After a challenger requests an IPR, the patent holder has a right to file a preliminary response to explain why the IPR petition ought to be rejected, and the Patent Office then must decide whether to grant the petition, which it may only do if the petition "demonstrate[s] that it is more likely than not that at least one of the claims challenged in the petition is unpatentable."[29] No appeal (save for a motion for reconsideration) lies from the decision to either grant or deny the petition. If a petition is *denied*, however, a new one can be filed by the same (or different challenger) at any time during the patent's enforceability period.[30] If the Patent Office grants the petition and institutes an IPR proceeding, the matter goes to trial before the Patent Trials and Appeals Board ("PTAB" or the "Board"), which must render its final decision within twelve months of the decision to institute the proceedings.[31]

It is worth noting that the seemingly quick turnaround time required by statute is actually not that quick. Taking into account the time for filing an IPR request, the time allowed for opposition, and the time the PTO has to decide whether to grant the petition, the total time that a patent can spend in limbo waiting for resolution of an IPR proceeding is up to 27 months (or 33 months if the deadline for rendering the decision is extended). The 27-33 month timeframe is roughly equivalent to a district court litigation timeframe. Thus, though IPR may be cheaper and more streamlined, it is not necessarily faster, especially if one considers the time spent in additional litigation resolving issues of infringement and invalidity that were not addressed in the IPR process.

From the challenger's perspective, the key difference between trials at the PTAB and trials in district court is the compressed schedule and lower burden of proof. Whereas district court proceedings require "clear and convincing evidence" to invalidate a patent,[32] PTAB proceedings apply a "preponderance of evidence" standard.[33] Much like ex parte reexamination, the potential bases for invalidity in IPR proceedings are limited to lack of novelty under Section 102 and obviousness under Section 103 of the Patent Act.[34]

IPR proceedings have estoppel consequences. A petitioner who requests an IPR is estopped from subsequently asserting claims and theories which the PTAB rejects. The estoppel applies both to federal court litigation and future administrative proceedings (such as other PTO review proceedings), and includes issues that "reasonably could have been raised" before the Board. The parties covered by the estoppel include not only the petitioner, but also the real party in interest (that must be identified in every petition) and anyone in privity with the petitioner.[35] Importantly, other third parties are not estopped from challenging the same claims on the same theories that have already been addressed before the PTAB, either through additional PTAB proceedings or in litigation. Nor is the initial petitioner estopped from seeking additional rounds of administrative review or litigation with respect to *different* claims in the patent.

ii. Covered Business Method Review (CBMR)

CBMR is in many respects similar to IPR, but it applies to a narrower range of patents and allows for consideration of a broader set of issues. Unlike IPR, CBMR validity challenges can be based on any section of the Patent Act, not just Sections 102 and 103.[36] CBMR grew out of lawmakers' frustration with "business method" patents, in particular patents that covered the method for electronically processing and clearing personal checks. It is noteworthy that although proponents of CBMR have claimed that business method patents are "anathema to the protection the patent system provides" and that they only exist to target innocent companies in frivolous lawsuits, the patents that initially animated the push for the CBMR provision have been repeatedly upheld in litigation and reexamination.[37] Despite this record, Congress decided to subject "business method" patents to a more scrutinizing post-issuance review.

Given the difficulty in defining with any level of precision what constitutes a "business method" (a problem that the Supreme Court recognized in *Bilski v. Kappos*), Congress settled for a seemingly narrow definition of patents eligible for CBMR. Under the statute, challengers can use CMBR against patents that "claim[] a method or corresponding apparatus for performing data processing or other operations used in the practice, administration, or management of a financial product or service, except that the term does not include patents for technological inventions."[38] Unfortunately, "financial services" is left undefined. The PTO has stated that it will interpret this section broadly to "activities that are financial in nature, incidental to a financial activity or complementary to a financial activity."[39] Likewise, the AIA does not define "technological innovations." For this term, the PTO has concluded that it will proceed on a "case by case basis" and consider "whether the claimed subject matter as a whole recites a technological feature that is novel and unobvious over the prior art; and solves a technical problem using a technical solution."[40] This tautological definition has resulted in further litigation over the PTO's authority to order certain patents into CBMR and has cast a cloud of uncertainty over a broad range of patents.

Procedurally, CBMR is similar to IPR, with some important exceptions. First, unlike IPR, where any person can challenge a patent claim, CBMR challengers must satisfy standing requirements identical to those that would be applicable in federal court. Second, although CBMR does have estoppel provisions, they are much less far-reaching. Most importantly, estoppel does not attach to arguments that "could have been raised" in CBMR proceedings; rather it only attaches to arguments actually raised.[41]

The creation of these new procedures (along with PGR)

did not disturb the existing ex parte reexamination. Thus, reexamination co-exists with the new AIA procedures. What is worse is that the AIA estoppel provisions are a one-way street. They apply to reexaminations that have been instituted after a decision has been rendered in an IPR or CBMR, but they do not apply in reverse. A challenger can thus request a reexamination and then an IPR or CMBR without fear of estoppel. Indeed, challengers can request multiple reexaminations and then follow them up with an IPR or CBMR. In that way, a determined challenger can keep a patent, and consequently the patent holder's ability to enforce or license it, in perpetual limbo.

II. Early Data

As of November 20, 2014, just over 2,000 petitions for IPR have been filed. The Patent Office has preliminarily evaluated just over half of the filed petitions to decide whether or not to institute a trial. Of the ones that were preliminarily evaluated, 78% were ordered into trial.[42] The PTAB has issued 135 final determinations in 166 cases covering just under 2,000 separate patent claims. (Some cases were joined for a single decision, which is why there are fewer decisions than cases). One hundred and three of the cases considered (77% of adjudications) resulted in *every* challenged claim being cancelled.[43] An additional 10.5% of cases resulted in *some* claims being cancelled. Only 12% of the cases resulted in all of the challenged claims being upheld.

Another way of looking at the data is to consider the percentage of challenged claims that have been invalidated by the PTAB. Out of a total of 1,962 claims before the Board, 1,572 or 81% were found to be invalid. This is a staggering rate, especially considering that the *only* issues the Board is allowed to consider are novelty and obviousness. By comparison, in district court litigation, claims are invalidated for obviousness or lack of novelty about one third of the time, (i.e., at less than half the PTAB rate).[44] Similarly, academic studies suggest that when properly examined, only about 30% of issued patents are actually invalid for reasons of obviousness or lack of novelty.[45] That the PTAB invalidates patents at more than double these rates may indicate that it is giving short shrift to the vested patent rights of inventors.

The CBMR data is even less encouraging for patent holders. Admittedly, the data is significantly more sparse, because only a small subset of patents are eligible for CBMR. Nonetheless, the trends are fairly evident. As of November 2014, the PTO received 255 CBMR petitions, and processed 149 of them to determine whether to institute a full-blown trial. The Board chose to institute trial in 76% of all cases it considered. Of the cases that have gone to trial, the Board issued a final decision in 17 cases covering over 339 claims.[46] In *no case* did the Board uphold all challenged claims, and in only two cases did the PTAB find any of the challenged claims to be valid. The total claim invalidation rate in CBMR tops 96%.

Making matters worse still is the fact that IPR and CBMR are often not the first "bite at the apple" for patent challengers. A number of the AIA challenges were brought against patents that had been re-affirmed in previous litigation or ex parte reexamination proceedings. Despite the patent holders' repeated success in confirming their patent rights, the Board invalidated those patents at the same rate as every other patent that came before it. Nor is the PTAB solicitous of motions to amend claims. Indeed, the PTAB denied *every* contested motion to amend claims that were subject to an IPR or CBMR. Considering the data as a whole, it is not a surprise that former Chief Judge Rader of the U.S. Court of Appeals for the Federal Circuit recently remarked that the new administrative post-issuance review procedures are "acting as death squads, killing property rights."[47]

III. Abuses in the System

The ex parte reexamination system and the new AIA post-issuance review proceedings are rife with opportunities for abuse against patent holders. In enacting the AIA, instead of fixing existing problems of abuse against patent holders, Congress actually increased the opportunities for challengers to abuse the system. While the statistics above tell part of the story, a few specific examples of abuse are illustrative. The stories of abuse are necessarily anecdotal, but they shed light on the weaknesses in the system overall and suggest avenues to ameliorate the problems created by the AIA.

a. Rent-Seeking

Some patent challengers have used the system as a pure rent-seeking mechanism. Recognizing the high likelihood that a petition for review will be successful (both at the initial grant stage and at the merits stages), these challengers use the threat of filing a petition for review as a way to make patent holders pay them large sums of money in exchange for not filing the petition.

A clear case of such behavior involved four patents owned by VirnetX. After VirnetX won a substantial infringement suit against Apple[48] (and while an appeal was pending at the Federal Circuit), an unrelated entity called New Bay Capital, LLC filed an IPR request against the patents VirnetX had asserted against Apple.[49] Prior to filing the IPR request, however, New Bay made an offer to VirnetX – for 10% of VirnetX's jury verdict against Apple, it was willing to forego filing the IPR petition. Neither New Bay nor its parent company were ever involved in any litigation with VirnetX, nor was New Bay ever threatened with any patent enforcement actions by VirnetX. Yet, because of the lack of any standing requirement to file an IPR petition, New Bay was able to engage the PTO's machinery in its quest to extort money from VirnetX. Although VirnetX refused New Bay's demand for a payoff, it paid a high price when New Bay carried through on its threat. Within a week of the IPR petition being filed, VirnetX's stock price fell by 25%, a $250 million loss in market capitalization.[50]

Whatever the reason for New Bay's payoff demand and subsequent IPR request, it illustrates that the system can be used to destroy not just the value of a patent, but the value of a patent holder's entire enterprise. Furthermore, this damage can be accomplished at the low cost of an IPR filing. Because the cost of filing an IPR request to the patent challenger is modest, the threat of going through with it is almost always credible.[51] Given the potentially high costs imposed on the patent holder, the patent holder is in a lose-lose situation–either submit to the challenger's demands, or risk suffering losses on the market. The

challenger, on the other hand, is in a win-win situation. It need not even prosecute the challenge to completion (indeed, New Bay abandoned its challenge before the PTAB even decided whether to institute an IPR, and it is likely that it profited from taking a short position on VirnetX's stock).[52]

Machinations like these defeat the purposes of having post-issuance review proceedings in the first place. Abandoned challenges do not weed out "low quality" patents, nor do they provide certainty about the validity of "high quality" patents, and given that nothing is resolved in the process, it is impossible to talk about increased speed or decreased cost for dispute resolution. Unfortunately, the setup of the AIA's post-issuance proceedings almost ensures that more "New Bays" will come about. The opportunity to make money by shorting the market or by extracting rents from patent holders is simply too great to pass up. And because it is the most valuable patents that are preferentially subject to such requests, it is the value of the truly innovative companies that will likely suffer at the hands of this rent-seeking behavior.

b. Evasion of Estoppel and Time Bars

The AIA ostensibly sought to rein in seriatim requests for post-issuance review by patent challengers by requiring that request be brought within one year of the challenger being sued for infringement and by forbidding relitigation of issues that were or could have been raised in the first PTO proceeding that resulted in a final judgment.[53] As it turns out, however, these bars can be evaded with relative ease.

The most prominent case of attempts to evade such strictures also stems from the VirnetX's patents. While New Bay's IPR petitions were pending, Apple–the losing party in District Court litigation–filed its own IPR petition. As it happens, however, Apple's petition was not timely because VirnetX sued Apple more than one year prior to Apple's IPR request. The PTAB dismissed it, and that should have been the end of the story. But it was not.

As soon as New Bay's IPR petitions were withdrawn, seven additional IPR requests were filed by RPX Corporation.[54] RPX "is the leading provider of patent risk solutions, offering defensive buying, acquisition syndication, patent intelligence, insurance services, and advisory services."[55] It is a membership-based organization that provides the aforementioned services to its members. One of the services it provides is participation in post-issuance review in an attempt to invalidate patents. Although such attempts are clearly meant to benefit RPX's member-clients, ostensibly, RPX files petitions in its own name. By using this approach, RPX attempted to evade the time bars applicable to one of its clients–Apple.

In its petition for IPR of VirnetX's patents, RPX asserted that it was the real party in interest and was therefore not bound by any time bars or estoppel provisions that may be applicable against Apple.[56] After receiving half a million dollars from Apple and engaging the same law firm Apple used to defend itself against VirnetX's infringement claims, RPX decided, supposedly in the exercise of its "sole discretion," that VirnetX's patents were "of questionable validity" and should be challenged before the PTO.[57] The PTAB eventually held that on the very specific facts of RPX's petition, the real party in interest was Apple. However, that holding was predicated on a particularly strong intertwining of Apple's work and needs with RPX's actions. It is not clear from the Board's opinion that the mere fact of Apple's membership in RPX would have been sufficient to bind RPX with Apple's deadlines.[58] And if so, that raises opportunities for multiple rounds of reviews initiated not just by RPX itself, but by any of its members. In other words, the mere fact that RPX's member-client may benefit from RPX's decision to seek post-issuance review will likely be insufficient to conclude that such a member-client is the true "real party in interest."

RPX's actions, however, are not limited to evading estoppel and time bars to post-issuance proceedings. They also serve to enable each of their members (who happen not to be subject to any bars) to share costs and information on the potential lines of attack against a patent. That information can then be deployed piecemeal against a patent holder, keeping the patent under a constant and continuous IPR threat. A company like RPX can pool the resources of its members in order to compile a dossier on a patent that the members wish to invalidate. Then that dossier can be made available to all members who can proceed in piecemeal fashion against a patent holder. That is precisely what happened to at least some of VirnetX's patents, and it is likely that such a system will flourish going forward.

c. Seriatim Attempts at Invalidation

Patents that are subject to a post-issuance review request often face more than one such request. When these requests are filed simultaneously, the burden on the patent holder is somewhat alleviated because the PTAB tends to consolidate multiple pending requests into a single adjudicatory proceeding (although even in these circumstances, the challenger is in a better position because it can stagger its filings in such a way as to keep the patent holder's attorneys busy drafting responses to numerous post-issuance review petitions). The larger problem occurs when, after having failed in one post-issuance review proceeding, the challenger is able to trigger yet another one. One way to do that is to ask for an ex parte reexamination first, followed by the AIA-created procedures. Another way is to seek IPR first, followed by CBMR. This approach is not precluded by the estoppel provisions because certain lines of attack that are available in CBMR are not available in IPR, meaning that they are not issues that "could have been raised" in the previous proceeding. Yet another tactic is to challenge different *claims* in separate IPR or CBMR proceedings. This too does not trigger any estoppel provisions, because the estoppel provisions are applied on a *per claim* rather than per patent basis.

A good example of this behavior involved a patent owned by Zillow, an online real estate database directed to property valuation. In October 2012, Microstrategy, Inc., a business that has little apparent connection with real estate, filed an IPR request with respect to all 40 claims in Zillow's patent.[59] The Board granted the request in part, instituting review with respect to 29 out of the 40 claims.[60] In March 2014, the Board cancelled 25 of the 29 claims and upheld the remaining four. Zillow retained 19 total claims following the conclusion of the IPR.[61] That should have allowed Zillow to breathe at least a partial sigh of relief. Instead, almost immediately following this partial victory, Zillow was dragged back before the PTO

by Trulia–a competitor in the online real estate valuation market. In April 2014, a mere two weeks after Zillow managed to retain 19 out of 40 claims challenged by Microstrategy, Trulia filed a CBMR petition asking for a review of 15 of the claims in Zillow's patent. Furthermore, nine of the identified claims were ones that the PTAB declined to even institute a trial on in the previous IPR proceedings.[62]

Despite having prevailed previously on the issue (albeit against a different petitioner), Zillow had to defend its right to the claims at issue all over again. The PTAB promptly instituted trial on all but one of the challenged claims.[63] Zillow's patent has thus been under a consistent cloud since October 2012, (nearly two years as of this writing), and will spend additional time in limbo until the Board issues its final decision on Trulia's CBMR petitions. Of course, these petitions could be followed with yet other ones challenging any remaining claims. In that way, Zillow's patent could be kept in limbo for significantly longer than it would take to resolve district court litigation.

Unfortunately, Zillow is not the only victim of such tactics.[64] Furthermore, even though patents in the midst of IPR or CBMR continue to be enforceable, judges may stay any infringement actions while IPR or CBMR proceedings are ongoing.[65] As a result, while PTO review and any appeals therefrom are ongoing, patent holders may be de facto barred from actually enforcing their patents. In this environment, challengers have every incentive to "stack" their IPR and CBMR petitions so as to make life harder for patent owners and potentially deprive them of their ability to fully and consistently enforce their patent rights. Given the structure of the IPR and CBMR review processes, there is little to nothing that patent holders can do to prevent such abuse.

d. Retaliation and Leverage

Post-issuance review proceedings can also be used to settle scores with patent owners or to strong-arm companies into more favorable licensing deals. The Zillow patent discussed in the preceding subsection is an example of such "score-settling." Recall that Microstrategy, the first challenger to the Zillow patent, was a company with no relationship to Zillow or the technology protected by its patent. Nor was the challenger an RPX-type company that has patent invalidation as one of its stated goals. As it turns out, Microstrategy was involved in another, entirely unrelated patent litigation against an unrelated third party on an unrelated patent. The only thing that connected that litigation to Zillow was the fact that Zillow's attorneys (the large law firm Susman Godfrey) also happened to represent Microstrategy's opponents–Vasudevan Software, Inc, also known as VSi. During the course of negotiations between VSi and Microstrategy, Microstrategy threatened that unless VSi dropped their infringement lawsuit, not only would they seek PTO review of all of VSi's patents, they would also retaliate against Susman Godfrey by going after their other clients. When VSi's lawsuit was not dropped, Microstrategy followed through on its threat and filed an IPR petition against Zillow.[66] This behavior exemplifies how the system can be used for improper purposes and as a tool to browbeat patent owners, even ones who have nothing to do with whatever has raised the petitioner's ire.

Another egregious example is the case of ImmunoGen, a company that works "to develop innovative, effective anticancer therapies that meaningfully improve the lives of patients with cancer."[67] Several patents on antibodies that are useful in cancer therapies resulted from ImmunoGen's work and were licensed to Genentech (a large biotechnology company), which in turn practiced the patents. The relationship between ImmunoGen and Genentech was quite productive. Separately, Genentech was sued by Phigenix, Inc., a company that holds a patent on a method of treating certain type of breast cancer. In its suit, Phigenix claimed that the sale and use of the drug marketed by Genentech (and covered by ImmunoGen's patent) infringed its method patents.[68] However, in addition to suing Genentech, Phigenix also filed an IPR request against ImmunoGen's patents.[69] ImmonoGen does not appear to have ever asserted its patents against Phigenix. This makes sense, as Phigenix does not manufacture any pharmaceutical products, and therefore invalidating ImmunoGen's patents in and of itself would not benefit Phigenix. Instead, by threatening ImmunoGen's assets, it looks like Phigenix was simply hoping to obtain more favorable licensing terms in its unrelated negotiation with Genentech.

These examples illustrate how the post-issuance review system can be used as a tool for retaliation and leverage. When such abuse occurs, instead of reducing litigation and associated costs, the system actually increases costs by allowing companies like ImmunoGen to be dragged into the fray by companies like Phigenix (who have no actual complaint against them and who would be unable to file suit against them in district court). This behavior also imposes additional costs on the public. Instead of spending its time, money, and other resources developing "innovative, effective anticancer therapies that meaningfully improve the lives of patients," ImmunoGen was forced to spend time defending its patents before the PTAB. (The PTAB has now instituted trial, thus creating litigation costs where none would have existed in the absence of the IPR process).[70] It would be one thing if such costs were offset by the possibility that invalidation would lead the challenger to enter the market with a competing, cheaper product, but Phigenix doesn't compete with ImmunoGen and had no intentions of developing an alternative to ImmunoGen's patented antibodies. Thus, win or lose at the PTO, society will be left with an innovative company that will have less money to dedicate to further research and development of cancer treatment. It is hard to fathom that that is what was intended by the patent "reformers."

IV. Lessons To Be Drawn

Almost immediately after the AIA was signed into law, we started hearing calls for an additional round of patent reform. President Obama announced his support for patent reform in the 2014 State of the Union Address, and the House of Representatives passed a reform bill by an overwhelming margin.[71] The stated purpose of this next round of reform is to make it harder to enforce patents, which will supposedly strengthen the patent system by reducing frivolous litigation.[72] But while the stated goal is laudable, the proposed reforms are deeply flawed.

As discussed above, the latest round of patent reform (the AIA) has already tilted the playing field significantly against patent holders by permitting patent challengers multiple and sequential avenues at patent invalidation, often under very

permissive standards. Additionally, in the interim we have seen several Supreme Court decisions, PTO guidelines and initiatives, as well as actions by the Judicial Conference and the FTC, all of which tilt the playing field even further against patent holders. Piling on legislative intervention at this point would further unbalance the patent system and provide added avenues for abusive practices by infringers.

The broad lessons to be drawn here are that no reform is cost-free, and that while the benefits of certain reform measures may be real, they should be weighed against the true costs of those reforms. The early data on the AIA shows that the current system of post-issuance review is susceptible to abuse in ways that Congress did not anticipate. Creating additional and ever-more expansive mechanisms to eradicate supposedly "low quality" patents is a dubious approach because it may end up imposing unnecessary and exceedingly high costs on legitimate patents and patent holders. It is a lesson that Congress would be well-advised to heed as it proceeds to debate yet another round of patent reform.

Endnotes

1 Mark Twain, A Connecticut Yankee in King Arthur's Court 107 (1st ed. 1889).

2 Pub. L. No. 112-29, 125 Stat. 284 (2011) (codified in scattered sections of 28 and 35 U.S.C.).

3 *See generally* Timothy G. Pepper, *Beyond Inherent Powers: A Constitutional Basis for in Re Tutu Wells Contamination Litigation*, 59 Ohio St. L.J. 1777 (1998) (noting that an increase in pretrial procedures has led to delay and abuses); Judith Resnik, *Precluding Appeals*, 70 Cornell L. Rev. 603, 613 (1985)("The potential for misuse of procedure exists at all times and in all procedural models.").

4 *See* Edward C. Walterscheid, *Patents and Manufacturing in the Early Republic*, 80 J. Pat. & Trademark Off. Soc'y 855, 888 (1998) (quoting Letter, William Thornton to Amos Eaton, May 5, 1809); Edward C. Walterscheid, *The Winged Gudgeon - an Early Patent Controversy*, 79 J. Pat. & Trademark Off. Soc'y 533 (1997); Thompson v. Haight, 23 F. Cas. 1040, 1041 (C.C.S.D.N.Y. 1826); S. Misc. Doc. No. 50, at 123 (1878) (additional argument of J.H. Raymond).

5 *See* Matthew Sag & Kurt Rohde, Patent Reform and Differential Impact, 8 Minn. J.L. Sci. & Tech. 1, 8 (2007)(noting that "patents such as the Tarzan Swing Method, the Beerbrella, a Method for Exercising Your Cat (with a laser pointer), the Hair Comb-Over Patent, and the Peanut Butter & Jelly Sandwich … are silly, but they are typically of little consequence …."); Mark A. Lemley & Carl Shapiro, *Probabilistic Patents*, 19 J. Econ. Persp. 75, 79-83 (2005).

6 *See* Christi J. Guerrini, *Defining Patent Quality*, 82 Fordham L. Rev. 3091 (2014).

7 Microsoft Corp. v. i4i Ltd. Partnership, 131 S.Ct. 2238 (2011); 35 U.S.C. § 282.

8 Act of December 12, 1980, Pub. L. No. 96-517, 94 Stat. 3015 (1980).

9 H.R. Rep. No. 96-1307 pt. 1 at 3-4 (1980).

10 35 U.S.C. § 305; MPEP § 2254 (8th ed. Rev. 8, July 2010).

11 35 U.S.C. § 301 (2010); 37 C.F.R. § 1.552 (2010); MPEP § 2258 (8th ed. Rev. 8, July 2010).

12 Kenneth R. Adamo, *Reexamination--To What Avail? An Overview*, 63 J. Pat. Off. Soc'y 616, 617 (1981).

13 *See* Raymond A. Mercado, *The Use and Abuse of Patent Reexamination: Sham Petitioning Before the USPTO*, 12 Colum. Sci. & Tech. L. Rev. 93 (2011).

14 U.S. Patent & Trademark Off., Ex Parte Reexamination Filing Data - September 30, 2013 at 1, *available at* http://www.uspto.gov/patents/stats/ex_parte_historical_stats_roll_up_EOY2013.pdf.

15 Nellie A. Fisher, The Licensee's Choice: Mechanics of Successfully Challenging A Patent Under License, 6 Tex. Intell. Prop. L.J. 1, 46 (1997).

16 N. Thane Bauz, *Reanimating U.S. Patent Reexamination: Recommendations for Change Based Upon A Comparative Study of German Law*, 27 Creighton L. Rev. 945, 955-56 (1994); Mercado, *supra* note 12 at 133-34.

17 S. Rep. 111-18 at 56 (2009); Robert Greene Sterne, *et al.*, *Reexamination Practice with Concurrent District Court Litigation or Section 337 USITC Investigations*, 11 Sedona Conf. J. 1, 45 (2010).

18 *See* Randall R. Rader, *Addressing The Elephant: The Potential Effects of the Patent Cases Pilot Program and Leahy-Smith America Invents Act*, 62 Am. U. L. Rev. 1105, 1109 (2013); James L. Wamsley, *A View of Proposed Amendments to Patent Reexamination Through the Eyes of A Litigator*, 36 IDEA 589 (1996).

19 For example, the duration of an average *ex parte* reexamination proceedings is about 26 months, .S. Patent & Trademark Off., *Reexaminations - FY 2014* at 2, *available at* http://www.uspto.gov/patents/stats/Reexamination_operational_statistic_F_14_Q1.pdf, while average litigation lasts 27 months. Am. Intellectual Prop. Ass'n, *2011 Patent Litigation Study: Patent Litigation Trends as the "America Invents Act" Becomes Law* at 27-28 (reporting that average time to trial is 2.28 years (or 27.36 months), *available at* http://www.aipla.org/resources2/intlip/Documents/Other-International-Events/US-Bar-JPO-Liaison-Council-2012/2011-patent-litigation-study.pdf.

20 Patlex Corp. v. Mossinghoff, 758 F.2d 594, 604, *on reh'g*, 771 F.2d 480 (Fed. Cir. 1985); Allen M. Leung , *Legal Judo: Strategic Applications of Reexamination Versus an Aggressive Adversary (Part I)*, 84 J. Pat. & Trademark Off. Soc'y 471, 483 (2002).

21 Sterne, *supra* note 16 at 14-15.

22 Sarah Tran, *Policy Tailors and the Patent Office*, 46 U.C. Davis L. Rev. 487, 498-99 (2012).

23 Pub. L. No. 112-29, § 6(f)(2)(A), 125 Stat. 284, 311(2011).

24 *See* 57 Cong. Rec. S5428 (daily ed. Sept. 8, 2011) (statement of Sen. Patrick Leahy); 157 Cong. Rec. S1363 (daily ed. Mar. 8, 2011) (statement of Sen. Patrick Leahy); 157 Cong. Rec. S1375 (Mar. 8, 2011) (statement of Sen. Kyl); 155 Cong. Rec. S2715 (March 3, 2009) (statement of Sen. Hatch).

25 35 U.S.C. § 316(a)(11); Pub. L. No. 112-29, § 18, 125 Stat. 283, 330.

26 35 U.S.C. § 311.

27 *Id.* § 315(a)(1).

28 *Id.* § 315(a)(2).

29 *Id.* § 314(a).

30 *Id.* § 314(d).

31 *Id.* § 316(a)(11).

32 *See* Microsoft Corp. v. i4i Ltd. Partnership, 131 S.Ct. 2238 (2011).

33 35 U.S.C. § 316(e). On the other hand, from the patent holder's perspective, the key difference, at least in theory, is the ability to amend his claims in PTAB proceedings, but not in district court. In practice, however, this opportunity is merely illusory, as the PTAB thus far has denied every contested motion to amend a patent holder's claims.

34 *Id.* § 311(b); 42 C.F.R. § 42.104(b)(2).

35 35 U.S.C. § 315(e).

36 Pub. L. No. 112-29, § 18, 125 Stat. 283, 330.

37 157 Cong. Rec. S1053 (daily ed. Mar. 1, 2011) (statement of Sen. Schumer); Both of the patents that gave rise to this provision were subject to reexamination and litigation *See* U.S. Patent No. 6,032,137 (issued Feb. 29, 2000), *reexamination certificate* 6,063rd (issued Dec. 12, 2007); U.S. Patent No. 5,910,988 (issued June 8, 1999), *reexamination certificate* 5,957th (issued Oct. 23, 2007); DataTreasury Corp. v. WellsFargo & Co., No. 2:06-cv-72 (E.D. Tex., Aug. 1, 2011)(final judgment order).

38 Pub. L. No. 112-29, § 18(d)(1), 125 Stat. 283, 331.

39 77 Fed. Reg. 48,734, 48,735 (Aug. 14, 2012).

40 37 C.F.R. § 42.301(b).

41 Pub. L. No. 112-29, § 18(a)(1)(D), 125 Stat. 283, 330.

42 *See* U.S. Patent & Trademark Off., *AIA Progress as of November 20, 2014*, *available at* http://www.uspto.gov/ip/boards/bpai/stats/112014_aia_stat_graph.pdf. The 78% overall grant rate for IPR is appreciably lower than the 93% grant for *ex parte* reexamination, suggesting that Congress did succeed in raising the threshold for instituting post-issuance review proceedings. That said, and though the current trend is favorable, the data on reexamination is richer than that for IPR so the numbers may yet equalize, especially considering that after a drop to 77% grant rate in FY2014, the FY2015 rate is back up to 86%.

43 One case was submitted only for the purposes of an unopposed amendment, and therefore is not counted in the total.

44 John R. Allison & Mark A. Lemley, *Empirical Evidence on the Validity of Litigated Patents*, 26 AIPLA Q.J. 185, 209 (1998).

45 Shawn P. Miller, *Where's the Innovation: An Analysis of the Quantity and Qualities of Anticipated and Obvious Patents*, 18 Va. J.L. & Tech. 1, 6 (2013).

46 *AIA Progress as of November 20, 2014*, *supra* note 42.

47 Tony Dutra, *Rader Regrets CLS Bank Impasse, Comments on Latest Patent Reform Bill*, Bloomberg BNA (Oct. 29, 2013), *available at* http://www.bna.com/rader-regrets-cls-n17179879684/.

48 VirnetX Inc. v. Apple Inc., 925 F. Supp. 2d 816, 825 (E.D. Tex. 2013).

49 IPR2013-00375, 00376, 00377, and 00378 (all filed June 23, 2014).

50 Michelle Carniaux & Michael E.Sander, The Curious Case of New Bay Capital LLC and VirnetX Inc., IPR Blog (Nov. 22, 2013), *available at* http://interpartesreviewblog.com/curious-case-new-bay-capital-llc-virnetx-inc/.

51 American Intellectual Property Law Association estimates that the "all-in" cost for an IPR is somewhere between $300,000 and $500,000. *See* Am. Intellectual Prop. Ass'n, *Comparison of Federal Court, ITC, and USPTO Proceedings in IP Disputes* (Jan. 2014), *available at* http://www.aipla.org/committees/committee_pages/IP-Practice-in-Japan/Committee%20Documents/2014%20MWI%20Presentations/Tom%20Engellenner%20-%20IP%20Dispute%20Cost%20Comparison.ppt.

52 Tom Shaughnessy, *VirnetX: New Bay Capital LLC's And Apple's Contrived IPRs - Part 2: New Bay Retraces*, Seeking Alpha (Oct. 25, 2013), *available at* http://seekingalpha.com/article/1772542-virnetx-new-bay-capital-llcs-and-apples-contrived-iprs-part-2-new-bay-retraces.

53 *See* H.R. Rep. No. 112-98, at 48 (2011).

54 IPR2014-00171; -00172; -00173; -00174; -00175; -00176; and -00177 (all filed Nov. 20, 2013).

55 http://www.rpxcorp.com/about-rpx/.

56 IPR2014-00177 (Petition for Review at 2-4).

57 IPR2014-00171; -00172; -00173; -00174; -00175; -00176; and -00177 (order denying IPR at 4-6, filed June 5, 2014), *available at* http://cdn.arstechnica.net/wp-content/uploads/2014/06/RPX-IPR-denied.pdf.

58 *Id.*

59 IPR2013-00034 (filed Oct. 26, 2014).

60 *Id.* (order granting IPR in part and denying in part) (filed Apr. 2, 2013).

61 *Id.* (final judgment order) (filed Mar. 27, 2014).

62 CBM2014-00115 (filed Apr. 10, 2014).

63 *Id.* (order instituting CBMR) (filed Mar. 10, 2014).

64 For a full discussion of the abuses in the system, *see* Gregory Dolin, *Dubious Patent Reform*, 56 B.C.L. Rev. ___ (forthcoming 2015), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2488220.

65 Indeed, recent Federal Circuit decision has hinted that stays *must* be granted absent compelling reasons to the contrary. *See* VirtualAgility Inc. v. Salesforce.com, Inc., 759 F.3d 1307 (Fed. Cir. 2014).

66 Vasudevan Software, Inc. v. Microstrategy, Inc., 3:11-CV-0663, D.E. 172 (N.D. Cal. Mar. 11, 2013) (order denying sanctions).

67 ImmunoGen, Inc., Our Mission, *available at* http://www.immunogen.com/about-immunogen/mission-and-vision/.

68 Phigenix, Inc. v. Genetech, Inc., 14-cv-00287 D.E. 1 (N.D. Ga. Jan. 31, 2014) (Phigenix's complaint alleging patent infringement at 5-9).

69 IPR2014-00676 (filed Apr. 22, 2014) and IPR2014-00842 (filed May 29, 2014).

70 IPR2014-00676 (decision instituting IPR) (Oct. 29, 2014). The other petition remains pending.

71 *See* H.R. 3309, Innovation Act (113th Cong, 2013). Kate Tummarello, *President calls for patent reform in SOTU*, The Hill, Jan. 28, 2014, *available at* http://thehill.com/policy/technology/196754-obama-calls-for-patent-reform.

72 H. Rept. 113-279 at 16-44 (2013).

International Design Patent Filing Considerations After U.S. Entry into the Hague Agreement

By Trevor K. Copeland & Daniel A. Parrish***

Effective May 13, 2015, applicants can file international design patent applications in a single, standardized application via the United States Patent and Trademark Office (USPTO) designating any of more than 62 territories, including the U.S. and European Union (EU), and can receive the same effective filing date in each jurisdiction. Design patents protect the ornamental designs of functional items, such as the shape of a Coca-Cola bottle or the icon for an app. This important opportunity comes as the U.S. accedes to the Geneva Act of the Hague Agreement, details of which are set forth in the USPTO's recently published Final Rule implementing changes to the agency's relevant design patent Regulations.[1]

The Hague Agreement is directed to uniform filing and registration procedures, not substantive law. The U.S. is a relative latecomer to the Agreement, which was first enacted in 1925 and has been amended several times since. Several countries, including the U.S., did not ascribe to early versions of the Agreement because it did not adequately provide for the substantive examination by national offices of all design applications.

The Geneva Act of 1999 amended the Hague Agreement to attract countries such as the U.S. that conduct substantive examination by extending the notification of refusal period to 12 months and by allowing contracting states to set higher fees. These changes provided national offices with time and money to conduct substantive examination, while maintaining a uniform right of priority worldwide. In view of these modifications, Japan also joined the Hague Agreement on May 13, 2015.

Noteworthy Effects of the Hague Agreement on Applications Designating the U.S.

- Applicants may submit up to 100 industrial designs per application, as long as all designs are in the same Locarno Class. This streamlined approach should result in increased filing efficiencies and cost savings for applicants, who may file through the USPTO or directly with the International Bureau of the World Intellectual Property Organization (WIPO). However, only persons who are nationals of the U.S. or who have a domicile, a habitual residence, or a real and effective industrial or commercial establishment in the territory of the U.S. may file international design applications through the USPTO as the direct office of filing.
- U.S. design patents resulting from international or national applications filed on or after May 13, 2015, will be enforceable for a 15 year term from grant, an extra year compared to the previous statute.
- International design applications designating the U.S. will undergo substantive examination based on U.S. law, including the written description and duty of disclosure requirements.
- Although the Hague Agreement permits up to 100 designs per application, those designating the U.S. must still be directed to a single invention. The USPTO may issue a restriction requirement if "distinct inventions" are submitted, requiring divisional applications to protect those inventions.
- For design patent applications, color drawings and photographs will no longer require a special USPTO petition.
- WIPO will publish Hague Agreement design applications, including those designating the U.S., following its formalities examination (typically six months after registration), but U.S.-only design applications still will not be published by the USPTO unless and until they issue.
- The U.S. will grant provisional patent rights for published international applications that designate the U.S. These provisional rights may be especially valuable (compared to utility patents) because design patent claim scope typically is not substantively changed during prosecution.[2]
- Ownership in the U.S. of Hague Agreement design applications remains subject to the assignment recordal procedures of the USPTO.
- Each Contracting State can impose requirements for whether or not an agent or attorney is required during "national phase." Design applications designating the U.S. will require a USPTO registered patent agent, patent attorney, or person operating under a "limited recognition number," each of which requires U.S. residency or U.S. citizenship/immigrant status.

Optimizing an international filing strategy requires weighing the pros and cons of various filing systems, including the Hague Agreement, Registered Community Designs (EU), and USPTO design patents, or other "home country" registrations or applications.

One-Stop Shopping

A major advantage of the Hague Agreement is "one-stop shopping." It uses a single form and deposit for registering up to 100 designs in 62 member countries. There is no need for

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This article is a general summary and does not provide legal advice upon which a reader should act. The views and opinions expressed in this article are those of the authors and do not necessarily represent views of Brinks, Gilson, & Lione, PC, or any of its clients.

a national agent in many countries since each country sets its own requirements, and countries that treat each application as a registration do not require local counsel for prosecution/examination. Although it is available, there is no need for an earlier national priority filing, because one application provides the same effective date in all countries. Furthermore, refusal (or invalidation) in one member country based on local substantive examination (or litigation) does not directly affect parallel registrations/applications in other member countries. It should be noted that substantive examination in other jurisdictions may identify items that are material to prosecution of a U.S. design case, triggering the applicant's duty of candor under 37 CFR §1.56.

The flip-side of this coin is that each country has different standards and requirements of which applicants must be aware. Thus, although certain countries may not require a local agent during the "national phase," applicants are encouraged to review the substantive laws of each designated state prior to filing, especially the drawing requirements and requirements for claiming and describing the design for which protection is sought. The ability to file up to 100 designs per application may provide strategic options for addressing and complying with different jurisdictions' distinctive drawing requirements, and not just for seeking to protect different embodiments of similar designs. Drawings not compatible with a particular jurisdiction's requirements can be canceled upon entry thereto, and divisional applications can be used to pursue multiple designs/embodiments in jurisdictions like the U.S. that permit only one "invention" per application/patent.

Another drawback is the large number of countries that are not contracting parties to the Hague Agreement; protection in those countries still requires a separate application. Notably absent members include Canada, Mexico, Brazil, Russia, China, India, and Australia. With the U.S. and Japan's accession to the Hague Agreement, however, more countries may soon follow.

Registered Community Design

A Registered Community Design (RCD) is another avenue of protection available for industrial design applicants seeking protection in the European Union. RCDs are administered by the Office for Harmonization in the Internal Market (OHIM). Inventors can apply for an RCD via designation in a Hague Agreement application, or by a separate application. One advantage of the RCD is that registration applies in all EU countries, barring any unauthorized person from making, importing, exporting, using, or otherwise dealing products embodying the covered design. Another advantage is that the OHIM grants up to 25 years of protection for RCDs, whereas design patents designating the U.S. are only eligible for 15 years. Although the Hague Agreement is limited to 100 designs in the same Locarno class, RCD applicants may submit an unlimited number of designs in a "multiple application."

The RCD system also has fewer grounds for invalidation of design patents than the U.S. system and others like it, providing another potential advantage to applicants; obviousness, for example, is not a ground for invalidation of an RCD. Although a Community Design must have "individual character," this is measured relative to other public designs individually, and there are no provisions to combine references (as in a U.S. obviousness analysis). Other defenses that are unavailable in the RCD system include indefiniteness, inequitable conduct, and potentially prior-user rights (under AIA §273). Thus, a Community Design may survive a challenge even if the counterpart U.S. design patent does not.

The major downside to the RCD system is that nullification or invalidation in one country applies to all EU member countries. This creates an incentive for competitors to challenge RCDs in less patent-friendly jurisdictions because a single successful challenge opens up the entire EU (28 countries) to commercialization. Another downside is the relative dearth of case law. The European Court of Justice (ECJ) rendered the first substantive decision in an industrial design case in 2011, whereas the U.S. Supreme Court has nearly 150 years of design patent precedent.

Home Country Registration

Some applicants may choose to file in the U.S. or another "home country" registration or application system. This also has advantages, including a single regime for standards of allowance and a mature body of case law for enforcement. For example, a design patent in the U.S. bars any unauthorized person from making, importing, exporting, using, selling or offering for sale products embodying the covered design. This is a powerful tool for enforcement against copycats, and includes a unique special damages provision that provides for disgorgement of the infringer's profits based on the entire product value, not just the portion of value attributable to product features embodied in the design patent. This was one reason why the famed $1 billion damages awarded in *Apple v. Samsung* was so large — because damages were calculated based on the entire saleable devices, not just the patented features.[3]

One downside to filing in a home country system is the need to navigate country-specific laws. For example, the U.S. requires "unity of invention," meaning only one inventive design is allowed per application. Another U.S.-specific potential pitfall is that applicants could inadvertently forfeit foreign filing rights if they do not plan carefully and make certain that any and all design and precedent utility patents are timely filed. For example, under the Paris Convention rules and U.S. law, any design patent application claiming subject matter disclosed in a provisional application must be filed within six months of the provisional filing date, even though a design patent cannot claim priority to the provisional application and any utility application claiming priority to that provisional can be filed within 12 months. Also, unlike the U.S., at least some jurisdictions do not allow a design patent to make a priority claim to a utility patent (e.g., the EU).

As discussed above, many potential infringement defenses in the U.S. are unavailable in some regimes, including obviousness, indefiniteness, and inequitable conduct. Applicants should consult with a registered practitioner so as to avoid these potential pitfalls. The U.S. accession to the Hague Agreement creates a new standardized application that should simplify international filing for industrial design patents for many inventors. Applicants should weigh the pros and cons of the Hague Agreement against other filing systems, including

RCDs and "home country" systems, to generate an optimized international filing strategy.[4]

Endnotes

1 *See* Changes to Implement the Hague Agreement Concerning International Registration of Industrial Designs, Final Rule, 80 Fed. Reg. 17,918.

2 *See* 35 USC §154(d).

3 Damages in this case were later reduced for other reasons.

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International & National Security Law

International Trade: New Initiatives

By Ronald A. Cass & C. Boyden Gray***

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This article discusses regulation in the context of international trade. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the authors. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. However, when we do, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• James McBride, *CFR Backgrounder: The Future of U.S. Trade Policy*, Council on Foreign Relations (June 25, 2015), http://www.cfr.org/trade/future-us-trade-policy/p36422.

• Joshua Meltzer, *Pass Trade Promotion Authority and Enable Conclusion of the Trans-Pacific Partnership Negotiations*, Brookings (April 9, 2015), http://www.brookings.edu/research/opinions/2015/04/09-trade-promotion-authority-trans-pacific-partnership-negotiations-meltzer.

I. International Trade

International trade is not often thought of in the context of regulatory overreach—which is the primary focus of the series that includes this paper—but the sort of trade agreements that nations enter into, the manner in which trade accords are arrived at and made binding on signatory nations, and the ways in which they are implemented have enormous implications for national economies and also for the scope and impact of domestic regulation in each nation. Trade agreements can bolster inefficient regulatory approaches by "harmonizing" regulations in ways that reduce some inputs to competition among firms' production in different nations. Conversely, trade agreements can reduce barriers to competition across borders, at least indirectly increasing pressure on regulators to adopt more efficient approaches. Choosing the right approach can make a significant difference to domestic economies and to the degree of liberty enjoyed in trading nations.

II. New Trade Initiatives: TPP and TTIP

After a series of global trade initiatives from the 1940s to the 1990s lowered trade barriers, especially tariffs on traded goods, efforts to advance further global multi-lateral agreements—notably, the World Trade Organization's (WTO) Doha Round—have stalled. Many nations (including the U.S.) have turned to arrangements between smaller groups of nations as vehicles for reducing trade barriers and expanding trade.

The two initiatives currently at the forefront of trade expansion hopes and fears are the Trans-Pacific Partnership agreement (TPP) and the Transatlantic Trade and Investment Partnership agreement (TTIP); both are still being negotiated, though they are substantially far along in the process. The TPP would provide lower trade barriers and agreed rules on trade-related issues for 12 Pacific Rim nations, while the TTIP would do similar (but not identical) things for the U.S. and the 28-nation European Union (EU).

Opponents complain that the agreements would reduce U.S. ability to secure American consumers' and workers' interests and to protect taxpayers against claims from foreign companies that feel disadvantaged, and that both agreements ultimately would hurt the U.S. economy and its most vulnerable workers—almost exactly the opposite of arguments made in favor of the accords. While our interest is primarily in the relationship between these potential agreements and regulation, we will touch on other arguments as well.

III. The New Trade Agreements: What is at Stake?

TPP negotiations have concentrated mostly on relatively traditional forms of trade opening, particularly lowering tariffs and reducing non-tariff barriers, although the negotiations also have included protections for investment and intellectual property rights as well as other issues that are either directly affected by trade or can be most efficiently addressed in the trade context. *Regulatory coherence*—a term used to connote promotion of more effective and transparent mechanisms for scrutinizing regulatory initiatives and for preventing regulations that (by design or not) unduly restrict trade—has not been a primary focus, but it has been added to the negotiating agenda.

Much of the work done by promotion of regulatory coherence also can be done within the TPP framework by restricting non-tariff barriers. Concerns over such barriers have been on the negotiating table under the rubric of agreements over *technical barriers to trade* and *sanitary and phytosanitary (health and food related) measures*. The goal for each of those parts of the agreement is to design rules that constrain protectionist

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regulations that lack substantial scientific support (for instance, a documented connection between a product and a health risk) and that especially limit competition by imports.

In comparison, a greater part of the TTIP negotiation aims at *regulatory cooperation*—coordination of different regulatory approaches to assure that the U.S. and EU regulations, even if different, do not pose cumulative hurdles to product development and sales—as well as *regulatory coherence*. TTIP also endeavors to lower tariff and other trade barriers (including on agricultural products, a long-running source of U.S.-EU trade frictions), but the greater focus on regulatory impediments reflects the fact that other barriers to U.S.-EU trade are already lower.

Further, as both the U.S. and EU have highly developed regulatory structures with extensive sanitary and phytosanitary rules, as well as technical regulations covering almost every imaginable industry and product class, it is likely that differences in approach or in standards may pose trade barriers that serve no significant public interest. In other words, differences may exist simply by virtue of the fact that different bodies have adopted the rules, even though there are many equally good approaches to protecting public interests and rules used on both sides of the Atlantic will be effective. While good faith differences will exist, there also is substantial opportunity for manipulation of the rule-creation and rule-administration processes to achieve protectionist ends—not all differences will be the result strictly of separate, good faith efforts.

At the simplest level, different rules and regulations, specifying different inputs to products or different certification procedures to assure compliance with regulators' concerns, frequently pose substantial, and unproductive, impediments to business. Two researchers looking at issues to be addressed in the TTIP negotiations gave one example that aptly illustrates the problem:

> According to one U.S. trade association, a U.S.-based producer of light trucks found that a popular U.S. model the manufacturer wanted to sell in Europe required 100 unique parts, an additional $42 million in design and development costs, incremental testing of 33 vehicle systems, and 133 additional people to develop—all without any performance differences in terms of safety or emissions. EU manufacturers face similar issues in reverse when selling an EU-designed model in the United States.[1]

The problems of regulatory differences between the U.S. and EU also have been brought up by representatives of numerous other industries, each with its own horror story about needless costs and delays in selling into countries that have comparable protections for the public but incompatible regulatory standards.

While these complaints generally are advanced by businesses that face barriers to competition in other markets, the barriers to trade also affect broader national interests. Estimates of gains to GDP in the U.S. and EU from eliminating such barriers range from just under 1 percent of GDP to as much as 13 percent of GDP (an estimate taking account of dynamic gains in the economy from greater freedom to compete in many markets more efficiently, as well as from the direct gains from eliminating special design changes and redundant regulatory permitting). Given the combined GDPs of the U.S. and EU, even at the lower end of the spectrum, gains would amount to tens of billions of dollars of gain annually, and higher estimates would equate to 3-4 trillion dollars of benefit each year.

IV. Analyzing, Forging, and Implementing Trade Accords

One set of arguments about trade policy has to do with international relations, including security concerns; a second set, which tends to dominate domestic debates in the U.S., focuses on economic issues. The short version of the international relations argument is that trade agreements help knit countries together: global trade accords facilitate and encourage trade across all borders, making nations more interdependent and less antagonistic, more likely to cooperate, less likely to fight.

There is doubtless some truth to this proposition (famously captured in the assertion that nations with Starbucks and McDonald's do not go to war against each other). But the evidence is less than compelling that the proportion of business done in trade is directly related to peaceful relations. Nations that fought in the first World War had economies far more integrated with fellow combatants than many that were on the sidelines. Still, at times conclusion of a preferential trade agreement signals—especially to those in less powerful, less populous, and less economically advanced nations—a degree of affiliation among the parties that can encourage better relations, facilitate more helpful accommodation on non-economic issues, and even tilt political debates in some of the partner-nations in a more favorable direction.

While national security and international political effects are important considerations, and increasing bonds are important likely byproducts of preferential trade agreements in particular (agreements of less than global reach, including TPP and TTIP), our focus is primarily on the economic effects of these accords, most of all on regulatory matters. Academic theorists for decades have developed analyses showing that reducing trade barriers does not always yield a "first best" economic result for each nation. This is true in special cases, but it almost always produces the best practical result, providing more goods and services of more quality options at better prices than more trade-restrictive alternatives. That insight is the same reason that we don't all make our own clothes, grow our own food, or build our own homes—or limit our effective options to products made by our friends and neighbors. Competition is economically beneficial, and competition among more potential creators and producers tends to expand the benefits to consumers and to nations.

Regulations can also be beneficial. They can limit opportunities for self-interested behavior that generates negative spillover effects, such as pollution that harms neighbors, acid rain that falls downwind, or water pollution that harms fish and ecosystems downstream. At the same time, regulations can be inefficient or ineffective; they can impose costs enormously in excess of their benefits; they can frustrate competition and reduce the range, quality, and affordability of products. Regulatory coherence should improve the way in which regulations are adopted, scrutinized, and justified. And regulatory cooperation should provide means of eliminating needless frictions among

regulations that ostensibly serve the same ends.

To the extent that happens, competitive forces will push jurisdictions to reduce regulatory costs, as these will make products from jurisdictions with higher regulatory costs (from rules that fail to produce better outcomes) less competitive. And lower regulatory drag also will increase the freedom of individuals and enterprises to research, design, produce, and distribute goods in the ways they think most conducive to success. Some observers worry that regulatory cooperation will reduce protections for consumers and punish producers in jurisdictions that are more responsible—those that police against harmful spillover effects, for example. The key consideration in treaties like TTIP is to reduce needless friction while keeping mutually agreed recognition of standards that enhance public health, safety, and well-being—without making it easy for less competitive businesses to use standards that advantage them (that rely on inputs others wouldn't use or specific product configurations that are peculiar to a particular location) as means of raising barriers to more globally successful rivals. Concentration on mutual recognition, rather than a single, agreed rule generally will better serve that end.

V. Guiding Principles for the Future

1. Support Expanding Open Trade. Because open trade tends to be politically, economically, and philosophically beneficial, administrations should start with the presumption that trade accords encouraging lower trade barriers should be favored.

2. Reduce Regulatory Frictions. Nations such as the U.S. and those comprising at least the core of the EU share broad commitments to similar goals, such as protection of the public against products that are dangerous for health and safety in ways that make it particularly efficient for well-conceived regulations to protect public interests rather than relying on individuals to protect themselves. Yet different regulatory approaches aimed at the same broad ends reduce competition, raise costs, and frequently make little or no difference in public health or safety. Input specifications and related standards should be eliminated where possible or their competition-reducing effects addressed. Primary attention should be devoted to this end.

3. Support Mutual Recognition. Administrations should prefer accords that allow different approaches to exist but that rely on agreed testing for compliance with standards by other national authorities or on mutually recognized certifications of compliance with similar regulatory requirements as sufficient. These approaches allow regulatory cooperation without the need for costly and often fruitless efforts to arrive at a single, jointly-approved regulatory approach.

4. Favor Dynamic Gains Over Static Gains. Approaches that generate more freedom over time for businesses to innovate, to find new and better ways of meeting concerns about public health and safety, and to compete as openly as possible—in as many markets and settings with as little risk of multiple, overlapping administrative requirements to gain entry into markets—should be favored over narrower agreements focused on approval of a specific, limited set of mutually accepted requirements. Narrower agreements may provide necessary starting points, but broader arrangements that allow reduced regulatory cost and more competitive engagement over time should be preferred. These will tend to promote newer and better ways of accomplishing agreed-on ends, more efficient and effective regulatory regimes, and greater welfare for all partner-nations over the longer term.

Endnotes

1 Shayerah Akhtar & Vivian Jones, *Proposed Transatlantic Trade and Investment Partnership (T-TIP): In Brief,* at 8 (Congressional Research Service, June 2014).

Labor & Employment

The OFCCP Continues to Add to Its Regulatory Arsenal

*By Lynn White**

Note from the Editor:

This article is about the Office of Federal Contract Compliance Programs' new sex discrimination regulations. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. However, when we do, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• ACLU, *ACLU Comments in Support of OFCCP's Proposed Regulations Prohibiting Discrimination on the Basis of Sex*, aclu.org, (April 13, 2015), https://www.aclu.org/sites/default/files/field_document/aclu_comments_ofccp_sex_discrimination_nprm-final_4-13-15.pdf.

• The Leadership Conference on Civil and Human Rights, *Discrimination on the Basis of Sex*, civilrights.org, (April 2, 2015), http://www.civilrights.org/advocacy/letters/2015/sex-discrimination-comments.html.

Federal contractors are reeling trying to keep up with the steady stream of regulations from the U.S. Department of Labor's Office of Federal Contract Compliance Programs (OFCCP). Although it is a relatively small office, the OFCCP has jurisdiction over approximately 500,000 employer establishments with millions of employees. The agency has made no secret of the fact that it is trying to add more "teeth" to existing regulations in order to more effectively root out employment discrimination and enforce the requirements of Executive Order 11,246. This 1965 order prohibits federal contractors and subcontractors and federally assisted construction contractors from discriminating on the basis of race, color, religion, sex, or national origin and requires them to take affirmative action to prevent discrimination based on these protected categories.[1]

The OFCCP recently issued final rules strengthening the nondiscrimination and affirmative action regulations for protected veterans and individuals with disabilities. The agency also issued final rules implementing the requirements of Executive Order 13,672, which added "sexual orientation" and "gender identity" to the list of protected classes under the Executive Order 11,246 regulations.[2] The OFCCP has several more regulations slated to come out in the coming year, including a requirement for federal contractors to report summary data on employee compensation to the agency.

One of the OFCCP's most recent proposed rules would eliminate the Sex Discrimination Guidelines (Guidelines) and replace them with regulations outlining the agency's current sex discrimination enforcement principles.[3] Rather than being "guidelines," the proposed regulations would have the force and effect of law.[4] The OFCCP suggested that this action was long overdue as there have been significant changes to sex discrimination statutory and case law under Title VII of the Civil Rights Act of 1964, and that revisions are needed to more accurately reflect current sex discrimination jurisprudence.[5] With little quantifiable benefit, this proposal will likely be much more costly than the agency estimated and create a significant amount of confusion for the federal contractor community.

a. Costs likely underestimated

The OFCCP asserted that since the proposal would only bring its regulations in line with existing requirements, it would impose minimal costs. Specifically, the OFCCP only assigned costs for becoming familiar with the rule's requirements and minimal costs for new pregnancy accommodation requests that may result from the rule. The estimated costs identified by the OFCCP are likely at the low end of potential costs in a number of respects. For example, the agency estimated that it would essentially cost less than $100 for an Equal Employment Opportunity Manager of a federal contractor establishment to familiarize herself with the rule. Given the complexity of the proposed rule, and its intersection with related laws, this estimate is unrealistically low. This estimate also does not take into account the cost and amount of time it will take to train managers and other employees to inform them of their rights and responsibilities under the new rule.

Similarly, the OFCCP's cost estimates regarding the proposed rule's requirements for providing pregnancy accommodation were off the mark in many respects. These estimates assumed, first, that only women who are working in laborer positions would request pregnancy accommodations, and also that accommodations would cost approximately $500 each. This estimate does not reflect the realities that women in any job category can request a pregnancy accommodation and that those accommodations will often cost much more than $500. It also fails to take into account that pregnant women may request light duty, telework, or medical leave as an accommodation, requests that could last anywhere from a few weeks to the full duration of the pregnancy.

The OFCCP also neglected to assign any costs to the new provisions regarding gender-neutral bathroom facilities in contractor establishments. The proposed rule would make it unlawful sex discrimination to deny a transgender employee

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"access to bathrooms used by the gender with which they identify."[6] These requirements prompted the White House to add gender-neutral restroom facilities "in keeping with the administration's guidance on this issue and consistent with what is required by the executive order that took effect [April 8, 2015] for federal contractors."[7] Rather than being costless, as the OFCCP assumes, this requirement could lead to millions of dollars in construction costs for each contractor, particularly those who may have multiple buildings at one establishment.

b. Creating more confusion

The OFCCP asserted that regulation was necessary to save federal contractors the effort of trying to reconcile the existing Guidelines with more recent Title VII jurisprudence and avoid a "vacuum of guidance for contractors."[8] However, it is highly unlikely that contractors even consult the Guidelines any more since they have been outdated for decades. The OFCCP also admitted that the proposal did not even include the full scope of Title VII sex discrimination principles, leaving a vacuum of guidance regarding the principles that the agency chose not to address in this rulemaking.[9] As a result, the proposed rule would not create the authoritative source for Title VII compliance as it relates to sex discrimination, which is the primary justification that the agency offers.

The OFCCP also made the interesting decision to base parts of the proposed rule on areas of law that were not only unsettled, but also under review by the U.S. Supreme Court. The proposed rule relied heavily on the Equal Employment Opportunity Commission's (EEOC) *Enforcement Guidance: Pregnancy Related Discrimination and Related Issues,* despite the fact that the Court had not yet issued its *Young v. UPS* decision (which was later issued in March 2015).[10] The EEOC acknowledged that portions of this guidance may need to be updated in light of the Court's decision.[11] While the OFCCP stated that the final rule would be consistent with the Supreme Court's ruling in *Young v. UPS*, the agency did not address precisely how the final rule may be different, nor did it provide opportunity for notice and comment on such changes. The EEOC subsequently revised the Pregnancy Discrimination Guidance in June 2015, two months after the comment period closed for OFCCP's proposed rule. Given the complex and ever-changing nature of Title VII case law, it is foreseeable that other landmark rulings may impact the validity of these rules, thus creating more confusion.

Preventing sex discrimination in the workplace is a critical mandate. However, as in some of its previous rulemakings, the OFCCP's sex discrimination proposed rule would heap costs on employers while providing little quantifiable benefit. The agency seems content to create myriad technical requirements that sound good, but do little to get at the root of employment discrimination. What they will do is make the jobs of those who have dedicated their careers to this pursuit a paperwork nightmare. Hopefully the OFCCP will more fully explore the true cost of these proposals in the final rule and attempt to quantify the benefit consistent with standard rulemaking practice.

Endnotes

1 Exec. Order No. 11,246, as amended (September 24, 1965).

2 Exec. Order No. 13,672 (July 21, 2014).

3 Discrimination on the Basis of Sex, 80 Fed. Reg. 5,246 (January 30, 2015).

4 *Id.* at 5,252.

5 *Id.* at 5,247.

6 80 Fed. Reg. at 5,277.

7 Sara Wheaton, *Latest White House Feature: Gender-Neutral Restroom*, Politico, April 8, 2015, *available at* http://www.politico.com/story/2015/04/white-house-gender-neutral-bathroom-116779.html; *see also* David McCabe, *White House Adds Gender-Neutral Bathroom to Office Building*, The Hill, April 9, 2015, *available at* http://thehill.com/blogs/blog-briefing-room/news/238342-administration-adds-gender-neutral-bathroom.

8 80 Fed. Reg. at 5,264.

9 *Id.* at 5,248.

10 *Young v. UPS*, No. 12-1226 (March 25, 2015).

11 Questions and Answer About the EEOC's Enforcement Guidance on Pregnancy Discrimination and Related Issues (http://www.eeoc.gov/laws/guidance/pregnancy_qa.cfm) (last visited April 6, 2015).

Labor Rules: Union Walk Around Rule and Broadened Joint Employer Standard

*By Karen Harned**

Note from the Editor:

This article is about new labor rules, including the so-called union walk around rule and the broadened joint employer standard. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the author. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. However, when we do, as here, we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

• Abigail Rubenstein, *OSHA Inspections Could Become New Union Organizing Tool*, Law360 (May 10, 2013), http://www.law360.com/articles/440624/osha-inspections-could-become-new-union-organizing-tool.

• Jeff Spross, *How McDonald's Puts the Squeeze on Both Franchise Owners and Workers*, The Week (August 31, 2015), http://theweek.com/articles/574355/how-mcdonalds-puts-squeeze-both-franchise-owners-workers.

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I. Labor Regulation by the Occupational Safety and Health Administration and the National Labor Relations Board

One cabinet level agency and two independent agencies regulate the majority of issues relating to the American worker. The Department of Labor houses various administrations, including the Wage and Hour Administration, which ensures that workers are paid a fair wage, and the Occupational Safety and Health Administration (OSHA), which ensures that working conditions are safe. The National Labor Relations Board (NLRB) serves as the arbiter of conflicts between labor and management and protects workers' right to organize. Finally, the Equal Employment and Opportunity Administration protects workers against illegal discrimination.

Examples of executive overreach can be found within each of these agencies, but two recent examples stand out as especially egregious. OSHA's "Union Walk Around Rule" and NLRB's pursuit of a much broader "joint employer standard" have the potential to impact a great number of employers and workers, along with the vitality of the American economy.

Both OSHA and NLRB are arguably acting outside the scope of their statutory authority in pursuing these policies. In addition, neither agency provided an opportunity for public comment as envisioned under the Administrative Procedure Act prior to proposing or implementing these changes.

II. OSHA's Underground "Union Walk Around Rule"

a. OSHA's Rule

On Feburary 21, 2013, Former Deputy Assistant Secretary for OSHA, Richard Fairfax, announced OSHA's "union walk around rule" in a controversial opinion letter responding to a union official.[1] The so-called "Fairfax Memo" concludes that an employee may ask that a union official accompany OSHA officials during safety inspections of a worksite, regardless of whether the company is unionized or has a collective bargaining agreement in place. Accordingly, the Fairfax Memo provides that a union representative may accompany an OSHA inspector as an employee's "personal representative," provided that the employee has requested the union official's presence and the OSHA inspector agrees to allow it.[2] The employer has no say in the arrangement. Under the Fairfax Memo, employers must allow union officials to walk around the worksite with OSHA inspectors.

b. The Rule's Context

Under the Occupational Safety and Health Administration Act, employees are permitted to have a "personal representative" present during OSHA inspections.[3] But the "union walk around rule" stretches the text of the Act quite liberally. A plain reading of the pertinent statutory language would not suggest that a non-employee union official should be considered a personal representative:

> The representative(s) authorized by employees shall be an employee(s) of the employer. However, if in the judgment of the Compliance Safety and Health Officer, good cause has been shown why accompaniment by a third party who is not an employee of the employer . . . is reasonably necessary to the conduct of an effective and thorough physical inspection of the workplace, such third party may accompany the Compliance Safety and Health Officer during the inspection.[4]

This seems to require a showing of "good cause" on an individualized basis for any third party to be present in an OSHA inspection.[5] The Fairfax Memo's blanket conclusion that union representatives may be present without such a showing runs contrary to the text of the regulation and OSHA's interpretation of the statute, regulations, and Field Manual.[6] Indeed, it makes little sense to assume that the presence of a union official will necessarily do anything to facilitate a proper inspection or be deemed "necessary" for "an effective and thorough physical

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inspection." Furthermore, this significant change of longstanding OSHA policy was implemented without any notice to the public or opportunity to comment, both of which are required by the Administrative Procedure Act. Finally, the Fairfax Memo raises constitutional concerns since it requires business owners to allow physical invasions of their property by parties who are not essential to an administrative inspection.[7]

III. NLRB's Proposed Change to the Joint Employer Standard

a. NLRB's Proposed Change

On August 27, 2015, in *Browning-Ferris Industries of California, Inc.*, NLRB overturned the existing joint employer standard, which had been in place since 1984.[8] Under the old standard, an entity was a joint employer if it exercised *direct and immediate control* over another business' employees by, for example, having the ability to hire, fire, discipline, supervise, or direct individual employees. Entities were joint employers only when they shared that *direct control* over the terms and conditions of employment for the same employees. Under the previous standard, franchisors, franchisees (independent businesses), and subcontractors operate as separate businesses.

In May 2014, NLRB announced that it would treat McDonald's USA LLC (McDonald's) and its franchisees as joint employers.[9] Then, in December 2014, NLRB filed 13 complaints asserting that McDonald's and its franchisees should be held jointly liable for numerous alleged violations of labor law stemming from alleged misconduct on the part of McDonald's franchisees.[10] There is a serious question as to whether McDonald's may be held liable, as a franchisor, for the actions of its franchisees.

The decision to treat McDonald's as a joint employer is highly controversial. With this move, NLRB effectively announced new rules that will have far-reaching implications for businesses working with independent companies. As one business owner put it, NLRB's newly announced rule throws "a hand-grenade in the middle of the [franchising] business model."[11] NLRB's new approach treats franchisors as joint employers with franchisees, or other independent contracting firms, so long as they exert "significant control" over the same employees—a standard that NLRB now argues can be satisfied simply by demonstrating that a franchisor has exerted signifiant control over every-day business operations, without regard to whether the franchisor has exercised any control over personnel decisions.[12] This not only jeopardizes the entire franchisor-franchisee model, but it contravenes 30 years of case law establishing that a franchisor is not a joint employer unless the franchisor actively exerts control over employment decisions, such as by setting wages or administering discipline.[13]

b. The Change in Context

NLRB first advanced this new rule in an amicus brief filing before an Administrative Law Judge (ALJ) in June 2014.[14] In the case of *Browning-Ferris Industries of California, Inc.*, NLRB argued that the ALJ should change the 30-year-old joint employer rule because today's franchising practices demonstrate the need for a change in order to promote "meaningful collective bargaining . . . [because] . . . some franchisors effectively control [] wages 'by controlling every other variable in the business except wages . . . .'"[15] Accordingly, *Browning-Ferris* may well pave the way for NLRB's enforcement actions against McDonald's. The case also could result in other "fishered" industries—like staffing companies—to be considered joint employers under the new rule.

The new rule imposes regulatory burdens, including expanded liabilities, on businesses throughout the country. In addition, NLRB's position would cause major disruptions for thousands of companies across the nation, as franchisors would be forced to take a more hands-on role in the franchisee's employment decisions, and an independent business would need permission from the franchisor to hire, fire, or discipline its employees.

IV. Discussion of OSHA's and NLRB's Rationales for the Rules

There has been a precipitous decline in union membership over the last thirty years. Many believe that the practical effect of both of these rules will be to help increase union membership. The OSHA rule could incentivize unions to use OSHA complaints as an organizing tactic. Through an OSHA inspection, union officials could gain access to non-union employees and begin laying the groundwork for a unionization campaign.[16]

The NLRB rule also promises a significant increase in union membership. The new broader standard will make it easier for unions to gain access to a larger company. By organizing a subcontractor first, the union can say that the company who uses the subcontractor should also be unionized. Similarly, in the franchising model, unions will no longer need to fight unionization campaigns on a piecemeal basis in every franchisee location. Instead, unions can seek to unionize all non-corporate franchisees in one election.[17]

V. Guiding Principles Going Forward

OSHA's union walk around rule and NLRB's recent decision to broaden the joint employer standard completely overturn decades of labor and employment law upon which businesses and workers have relied. Absent significant evidence that such fundamental legal changes are necessary, the executive should not change the law. If evidence suggests that such legal changes should be made, Congress—not unelected agency officials—should propose and consider them. Executive agencies should not be permitted to change decades of law for millions of businesses and workers through a memorandum or enforcement position. That is the constitutional system America's founders envisioned and upon which America's job creators rely.

Endnotes

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4 *Id.*

5 Brennan W. Bolt, OSHA Says Nonunion Employees Can Select Union Representatives to Participate in OSHA Inspections, Labor Relations Today, McKenna Long & Aldridge LLP (Apr. 19, 2013), *available at* http://www.laborrelationstoday.com/2013/04/articles/unions/osha-says-nonunion-employees-can-select-union-representatives-to-participate-in-osha-inspections/ (last visited Feb. 11, 2015) ("This OSHA Interpretation is significant to labor relations because it appears to dilute OSHA's own regulations requiring that the employee representative be employed by the employer being inspected except in limited circumstances.").

6 Testimony of Maury Baskin on behalf of the National Association of Manufactures and Associated Builders and Contractors, Inc., before the U.S. House of Representatives Committee on Education and The Workforce, Subcommittee on Workforce Protections on "OSHA's Regulatory Agenda: Changing Long-Standing Policies Outside the Public Rulemaking Process" (Feb. 4, 2014).

7 *See* Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982).

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Telecommunications & Electronic Media

Net Neutrality and the Rule of Law

By Richard Wiley & Brett Shumate***

Note from the Editor:

This article is about the Federal Communications Commission's net neutrality rules. As always, the Federalist Society takes no position on particular legal or public policy initiatives. Any expressions of opinion are those of the authors. Generally, the Federalist Society refrains from publishing pieces that advocate for or against particular policies. However, in some cases, such as with this article, we will do so because of some aspect of the specific issue. In the spirit of debate, whenever we do that we will offer links to other perspectives on the issue, including ones in opposition to the arguments put forth in the article. We also invite responses from our readers. To join the debate, please e-mail us at info@fedsoc.org.

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I. Internet Regulation by the FCC

The Federal Communications Commission (FCC) was created for "the purpose of regulating interstate and foreign commerce in communication by wire and radio." While Congress has expanded the FCC's regulatory mandate over time to embrace new communications technologies, it has never granted the FCC open-ended regulatory authority over communications. Instead, the Commission has been given express regulatory power with respect to specific types of communications. In the Communications Act of 1934, as amended by the Telecommunications Act of 1996, Congress charged the FCC with regulating telecommunications services in Title II of the Act; broadcast television, radio, and commercial mobile radio service in Title III; and cable television in Title VI. The degree to which the FCC can stretch the bounds of its statutory mandate has critical implications for federal power to control communications.

II. Net Neutrality Rules

Probably the most controversial issue in the communications arena today is the FCC's ongoing effort to regulate the Internet to promote "net neutrality." Despite the absence of express authority to regulate the Internet, the FCC has sought for nearly a decade to impose "net neutrality" requirements on Internet service providers (ISPs)—companies like AT&T, Verizon, and Comcast as well as small and rural providers. The FCC's previous two regulatory attempts in this regard were overturned in court. Earlier this year, the Commission imposed strict net neutrality rules and, in the process, classified broadband Internet access service as a telecommunications service subject to the requirements of Title II of the Act.

III. Net Neutrality in Context

Net neutrality represents the concept that ISPs should treat all Internet traffic equally—not blocking or degrading some content and not speeding up or slowing down content based on its source. Net neutrality supporters fear that ISPs will use their control over the Internet connection they provide to their customers to extract fees from content providers or otherwise disadvantage unaffiliated content. For this reason, public interest groups and many Internet content companies (sometimes referred to as "edge providers") favor net neutrality rules. On the other hand, ISPs believe that they should be able to control their own networks and that the competitive marketplace will prevent them from engaging in misconduct of the sort net neutrality advocates invoke, noting also that other laws already exist (including antitrust laws) to address such misconduct in the unlikely event of a market failure.

Nearly everyone supports the central ideal at the core of net neutrality, including the ISPs. The heart of the debate is whether the FCC has the authority to impose net neutrality requirements through regulation. From 1998 to 2015, the FCC—under both Republican and Democrat administrations—treated Internet access as an unregulated information service under Title I of the Communications Act. The Supreme Court upheld this policy in *NCTA v. Brand X Internet Services*.[1]

After *Brand X*, the FCC issued an Internet Policy Statement adopting four principles that, according to the Commission, would "encourage broadband deployment, preserve and promote the open and interconnected nature of the public Internet," and entitle consumers to: (1) access lawful Internet

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content of their choice; (2) run applications and use services as desired, subject to the needs of law enforcement; (3) connect their choice of legal devices that do not harm the network; and (4) enjoy the benefit of "competition among network providers, application and service providers, and content providers." While not legally binding, these principles were endorsed by the largest ISPs.

The debate about net neutrality has been largely theoretical. There has been little evidence that ISPs have unfairly blocked access to websites or online services. The most high-profile incident to date involved allegations that Comcast was using network management techniques to address congestion from file sharing services such as BitTorrent, which can use up to 60 percent of the bandwidth of an ISP's network. The FCC found that Comcast's network management practices violated federal Internet policy. Comcast appealed, and the D.C. Circuit held that the Commission had not demonstrated statutory authority to regulate ISPs' network management practices.[2]

The FCC responded in 2010 by adopting net neutrality regulations under several statutory provisions, including Section 706 of the Telecommunications Act, which directs the Commission to encourage the deployment of broadband infrastructure.[3] Specifically, the FCC adopted: (1) a transparency rule requiring broadband providers to disclose their network management practices; (2) rules prohibiting wireline broadband providers from blocking access to lawful content and wireless providers from blocking access to lawful websites and competing applications; and (3) a nondiscrimination rule prohibiting wireline broadband providers from taking steps to slow or degrade Internet traffic.

The D.C. Circuit indicated that Section 706 authorized the FCC to adopt some net neutrality rules.[4] However, the court held that the no-blocking and nondiscrimination rules in particular were unlawful because they treated ISPs as common carriers in violation of the Communications Act. Because Title II common carrier regulation is reserved for telecommunications carriers, the Communications Act prohibits the FCC from regulating information service providers as common carriers. The court concluded that the no blocking and nondiscrimination rules required ISPs to give all content providers nondiscriminatory access to their subscribers—the same duty applicable to common carriers under Title II of the Act.

In response to the Verizon case, the Commission initially proposed to adopt new net neutrality rules under Section 706. However, net neutrality supporters urged the FCC to instead change the regulatory treatment of Internet access service. Specifically, they argued that the Commission should classify Internet access as a telecommunications service under Title II—the same regulatory classification of basic telephone service, which traditionally has been heavily regulated—rather than an unregulated information service under Title I. According to these advocates, treating Internet access as a telecommunications service would provide the most defensible legal foundation for net neutrality rules, allow the FCC to prohibit any "discrimination" against Internet content, and thereby prevent broadband providers from prioritizing certain content. In November 2014, President Obama weighed in on the net neutrality debate, urging the agency to adopt strict rules and reclassify Internet access as a telecommunications service subject to regulation under Title II of the Act.

On February 26, 2015, the FCC adopted President Obama's plan to regulate the Internet, reversing more than a decade of precedent treating Internet access as an unregulated information service. The Commission adopted new net neutrality rules applicable to both fixed and mobile ISPs that prohibit blocking, throttling, and paid prioritization, and require enhanced transparency. In addition, the FCC adopted a catch-all prohibition against practices that "unreasonably interfere with or unreasonably disadvantage the ability of consumers to reach the Internet content, services, and applications of their choosing or of edge providers to access consumers using the Internet." The FCC also reclassified Internet access as a telecommunications service under Title II of the Act and further declared mobile Internet access to be a commercial mobile service. Although the FCC granted forbearance from certain provisions of Title II, ISPs will be subject to various Title II obligations, the precise scope of which the agency has yet to define.

IV. Discussion of the FCC's Approach to Net Neutrality

According to the FCC, net neutrality rules are necessary to promote a "virtuous cycle" of edge provider innovation, end user demand, and ISP investment. As the Commission has explained, net neutrality rules will spur content providers to innovate, which will incent end user demand and which, in turn, will motivate ISPs to invest in their networks. Thus, in the FCC's view, net neutrality rules encourage broadband deployment as directed by Congress in Section 706 of the Telecommunications Act of 1996. And by classifying broadband Internet access as a telecommunications service under Title II of the Act, the agency believes it can ground net neutrality rules in the strongest legal authority.

The main criticism of the FCC's approach is that net neutrality is a solution in search of a problem. As indicated, nearly all ISPs openly support the concept of net neutrality, and there is no real record of ISPs blocking or degrading Internet traffic. Although the FCC found that ISPs have the incentive and ability to interfere with the Internet's openness, it has been able to identify only a handful of supposed instances of bad behavior. Instead of examining whether ISPs have market power, the Commission has acted on the belief that ISPs are gatekeepers to edge providers seeking to reach end users, and the agency has discounted evidence that subscribers are ready and willing to switch ISPs in the unlikely event they engage in misconduct.

The FCC's decision to regulate ISPs under Title II has drawn a firestorm of criticism. Title II was designed to regulate the monopoly-era telephone companies of the 1930s. By classifying broadband Internet access as a Title II telecommunications service, the FCC attempted to unlock the power to regulate the Internet in the same way it regulated telephone wires in the past. Title II gives the FCC the authority to control nearly every aspect of a telecommunications carrier's business, including the rates that the company can charge its customers. It also authorizes the Commission to impose new taxes on customer bills to support universal service. Title II regulation has long been the goal of net neutrality supporters because it

puts the Internet on par with such public utilities as water and electricity, providing a rationale for broad regulatory oversight.

Many fear that regulating the Internet under Title II will harm the vitality of the Internet. ISPs spend billions of dollars to build and maintain the broadband facilities that consumers use to access the World Wide Web. The concern is that these companies may be less inclined to invest in expanding capacity and reaching unserved areas if they are subjected to extensive government oversight under Title II. And if ISPs choose not to continue such investment—or if their sources of private capital diminish because of excessive regulation—broadband deployment in this country might stagnate and the future growth of the Internet could be threatened.

V. Guiding Principles for the Future

1. Ensuring Political Accountability. The political branches of our government must decide whether—and to what extent—the Internet should be regulated. This is a question of overriding national importance that should not be decided by an administrative agency. Delegating such a key issue to a single regulatory body undermines political accountability.

2. Promoting Investment. The Internet has flourished because the FCC's deregulatory policies heretofore have encouraged ISPs to expend billions of dollars to build ubiquitous networks throughout the country. These providers may not invest at the same pace if their services are subject to excessive government regulation. A light-touch regulatory framework will incentivize continued investment by ISPs in faster and more ubiquitous networks to the benefit of all Americans.

3. Maintaining Government Impartiality. The government should not pick winners and losers on the Internet. Using a heavy bureaucratic hand to skew the competitive playing field in favor of one preferred group over another entrenches existing business models and suppresses innovation. Instead, the market should decide which businesses succeed and which new services develop without the government tipping the scales in one direction.

4. Encouraging Innovation. The Internet has been one of the greatest developments of our time. Innovation, which is occurring both on the network and at its edges, is highly desirable and essential to maximize consumer choice. Government policy should seek to promote such innovation through continuing bipartisan support of a deregulatory approach to the Internet.

Endnotes

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Net Neutrality Meets Regulatory Economics 101

*By Joshua D. Wright**

I. Introduction

I want to thank the Federalist Society's Telecommunications and Media Practice Group and its George Washington University Law School Student Chapter for the invitation to speak with you today.**

Today's conference occurs at a fortuitous time, as the FCC Chairman has indicated the Commission will be voting on new net neutrality regulations tomorrow. The connection between net neutrality and media is so obvious it hardly needs to be stated. An increasing number of consumers use broadband internet access to consume an increasingly large amount of media. This media includes not only that which used to be consumed on the printed page, but also that which used to be consumed on television, and that which used to be consumed in a movie theater, and that which used to be consumed not at all–like, for instance, cat videos.

Once we are able to review the FCC's specific proposed regulations tomorrow, I suspect the debate surrounding the FCC's new approach will quickly delve into the details of the 332-page plan to regulate the internet. This debate will no doubt be very interesting and I expect will ultimately be resolved by the courts after a few years of lawsuits. Today, however, we have available to us the advantage of exploring net neutrality regulation the day *before* we have specific regulations to examine. Today, we can take an approach that focuses upon first principles.

Today I plan to discuss the economics of regulation more generally, with the hope of placing the broadband industry in that broader context. Rather than focus upon *how* we regulate broadband, I want to focus upon *why* and *whether* we even need to regulate broadband. My thesis is that the two major reasons for regulating an industry–the presence of natural monopoly conditions or significant externalities–are not present in the broadband industry. For that reason, we do not need to develop a new regulatory regime for broadband. Rather, we can use existing law and regulation to handle problems as they arise. In particular, I think antitrust is particularly well suited to protect consumer welfare from any issues that arise from priority contracting in the broadband industry, the prohibition of which is the major target of Chairman Wheeler's soon-to-be proposed regulations. Further, at least until tomorrow, existing consumer protection law authorizes the FTC to prosecute deceptive and unfair acts or practices in broadband markets that harm consumers.

II. State of Play in Net Neutrality Regulation

The FCC has a long and sordid history in attempting to enact net neutrality regulations. I do not think it would be a good use of our time here to recount the entire struggle. However I will note that my esteemed sister agency has taken several bites at the net neutrality apple only to have it swatted away just as many times by the D.C. Circuit.[1] The court's last swat occurred just over a year ago.[2] I, for one, have been waiting to see how the FCC would respond, especially after President Obama threw his hat into the ring in favor Title II regulation late last year.[3] Shortly after the President's pronouncement, we learned earlier this month from the Chairman of the FCC Tom Wheeler that the FCC plans to use its authority under Title II of the Communications Act of 1934 to regulate broadband providers as common carriers.[4] Regardless of whether you think prospective regulation is a good way to ensure an "open" internet–and I do not, as I will explain more in a minute–the FCC using its authority under Title II of an 81 year old statute to regulate competition in the broadband market is sort of like Intel using a hammer and a sickle to manufacture semiconductors. As I noted just a minute ago, we will get to see the particulars of the FCC's latest attempt tomorrow.

III. A Quick Primer on the Economic Theory of Regulation

Before I discuss net neutrality specifically, I think it is worthwhile to ask a threshold question that I feel too often gets ignored in policy debates about net neutrality: what is the economic problem that net neutrality is supposed to solve? In other words, what is the economic basis for *any* regulation in the broadband market? To do this properly, it is worthwhile first to consider the theoretical bases for economic regulation generally. In other words, what can we say generally about why regulation may be necessary in certain industries?

The standard economic answer is that a market failure is necessary, but not sufficient, for regulation. Market failure–that is, an identifiable reason an unfettered free market may result in the misallocation of resources–is necessary but not sufficient because there are multiple ways to solve problems involving market failure. If market failure exists, an important second question arises concerning the relative efficiency of alternative solutions, including regulation. However, well-understood principles of the economics of regulation require a solid understanding of the market failure to be solved before moving on to evaluating the costs and benefits of regulatory alternatives. In short, it makes little sense to subject consumers–in this case internet users–to a medical treatment or procedure without knowing whether they are sick in the first place.

We can generally describe four types of markets in which regulation may be necessary to correct a market failure.

The first is a natural monopoly in which fixed costs are

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The views stated here are my own and do not necessarily reflect the views of the Commission or other Commissioners. I am grateful to my advisor, Derek Moore, for his invaluable assistance in preparing this speech.

large relative to the marginal costs of production. If this occurs, then it may be more efficient from a production standpoint for a single firm to produce all the output in an industry. In such a market there is a theoretical conflict between the free market–where output is produced by a single supplier–and allocative efficiency. Allocative efficiency occurs when the market-wide output equilibrates the marginal revenue associated with the sale of an additional unit of output with the marginal cost of producing it. In a competitive industry in which sellers are price-takers, the marginal revenue is simply the market-clearing price. When a market is characterized by having only a single seller, the seller decides to produce a quantity that equilibrates marginal revenue and marginal cost. The difference is that a monopoly firm is not a price-taker; the marginal revenue of producing an additional unit is not simply the market price. Assuming the monopolist faces a downward-sloping demand curve and cannot price discriminate, producing an additional unit forces the monopolist to lower his price, and he must accordingly lower the price he charges for all units of output. For this reason, the slope of the monopolist's marginal revenue curve is steeper than the monopolist's demand curve, and equilibrating marginal revenue and marginal cost results in the monopolist producing a lower output than under competitive conditions, which is properly viewed as a misallocation of societal resources. Under natural monopoly conditions, however, economies of scale are such that it is efficient from a production standpoint for a single seller to produce all the output in an industry. When this occurs, there is an economic basis for government regulation to resolve the conflict between the allocative inefficiencies associated with monopoly pricing on the one hand, and the productive efficiencies associated with a natural monopoly cost structure on the other. Regulation in this context often involves price oversight and entry regulation by a government body designed to resolve the monopolist's incentive to raise price above the socially optimal level. Indeed, this mode of analysis was used to justify much of the rate regulation in the electric power industry.

A second category of market failure, related to natural monopoly, is the more general phenomenon of monopoly power. Firms can acquire monopoly power without natural monopoly conditions in some circumstances. Although a firm's acquisition of monopoly power and corresponding enjoyment of monopoly profits is often temporary because new firms enter the market over time reducing the incumbent's power, economic welfare nevertheless suffers when a firm or firms exercise market power and increase the market price beyond what would obtain in a competitive market. Multiple firms may collude to exercise market power; or in some cases, a single firm might do so unilaterally. Government action and imposition of regulatory barriers to entry are also an important source of market power.[5] For example, state and local governments often impose restrictions to exclude new competitors, like UBER in the taxi market or state laws preventing the interstate shipment of wine.[6] Antitrust law prohibits the unlawful acquisition of market power that harms consumers.

The third type of market in which regulation may be necessary is a market plagued by externalities. An externality occurs when the parties to a market transaction do not internalize all the costs and benefits associated with their transaction. In other words, an externality occurs when the activities of one party impose uncompensated benefits or costs on other parties. When negative externalities are present, a free market results in too much production. When positive externalities are present, a free market results in too little production. When we think of externalities we typically think of negative externalities such as pollution, but it is important to remember that positive externalities exist as well. A good example is education. A teacher and a student, the seller and the buyer in the market for education, both benefit when a student buys education from the teacher. However, society at large benefits from a more educated populace and those benefits are difficult to capture in a private market exchange between teacher and student. Accordingly, there is some rational economic basis for government intervention to encourage more education transactions between teachers and students. Some markets that feature externalities might require taxes or subsidies to induce parties to internalize costs or benefits imposed on society from their activities. Of course, externalities are ubiquitous in the modern economy. Most do not require any sort of regulation at all because private actors can internalize the externalities at relatively low cost.[7]

The fourth category involves market failures associated with the market for information. For example, market failures might arise because sellers have more information than buyers.[8] The efficient level of information is not necessarily perfect or "total" information because information is costly to supply. In markets for goods and services, failures associated with inadequate or asymmetric information are often handled without government intervention–for example, through firms' strategies to credibly signal information to consumers, the rise of review sites that collect information about the quality of goods and services firms provide (think Yelp or Angie's List), and firms' own investments in reputation. Consumer protection law also prohibits deceptive statements and omissions that induce transactions that would not have occurred in the absence of market failure.

IV. Net Neutrality and the Economic Theory of Regulation

Against this backdrop, the natural question is: where does the market for broadband internet access fit into the economic theory of regulation, broadly defined? What market failure, if any, is the FCC trying to solve with net neutrality regulations? Statements from the FCC Chairman are of little help. In a recent article, Chairman Wheeler said that net neutrality regulations are necessary "to preserve the internet as an open platform for innovation and free expression." It is hard to glean from this statement exactly what economic forces are at work today in the broadband market preventing the internet from being an open platform for innovation and free expression.

The Chairman also says "the fundamental problem [is] with allowing networks to act as gatekeepers."[9] The word "gatekeeper" could have some relevant economic meaning. It is important, however, to pin down exactly what we

think the Chairman means by the term. There are gatekeepers everywhere. McDonald's is the gatekeeper of Coca-Cola beverages sold inside McDonald's restaurants. Starbucks is the gatekeeper to my morning cup of coffee and the supermarket is the gatekeeper to your access to Cheerios breakfast cereal in the supermarket aisle.[10] A gatekeeper becomes an economic problem potentially worthy of regulation only when the gatekeeper stands between consumers and the *only* source of a desirable good or service. If consumers are able to get Coca-Cola or other similar beverages from sources other than McDonald's, then McDonald's will be unable to manipulate consumers' access to Coca-Cola in a way that makes consumers worse off because if it does, consumers are able to buy Coca-Cola from other sources. In short, it is *competition* that ensures that firms supply consumers access to the goods or services they want.

In other words, the "gatekeeper" issue identified by Chairman Wheeler is a problem worthy of regulation only insofar as the broadband industry is a natural monopoly or otherwise exhibits meaningful monopoly power–that is, the power to artificially increase market prices and decrease market output. The simple fact that there are multiple suppliers of both wired and wireless broadband internet renders this justification of regulation totally unpersuasive.[11] As I will explain a bit later, we have a legal regime specifically designed to address those sorts of problems: antitrust law. My point at this time is simply that the "gatekeeper" justification for broad-sweeping net neutrality regulation cannot possibly justify those regulations because no broadband provider can be viewed as a gatekeeper to anything when there is viable competition from other broadband providers.

Being charitable to Chairman Wheeler, it could be that the desire "to preserve the internet as an open platform for innovation and free expression" reflects a concern about externalities rather than natural monopoly or monopoly power more generally.[12] Indeed, Chairman Wheeler has touted that the latest net neutrality regulation will "ban paid prioritization, and the blocking and throttling of lawful content and services."[13] Perhaps the concern is that the broadband provider and the content provider do not internalize all the costs associated with a contractual arrangement through which the content provider pays the broadband provider for priority use of the network. The argument would seem to be that there is some social interest in egalitarian access to all broadband providers' networks–in effect a one-size-fits-all contract between broadband providers and content providers–and that we cannot trust the marketplace to reach this outcome without regulatory intervention.

An argument that the broadband market ought to be regulated because of externalities not captured in the bargains between broadband providers and content companies may be economically coherent, but it lacks any basis in fact. At this point, the problems associated with giving certain content providers preferential access to the network–and by extension providing certain content providers with degraded access–are purely theoretical. And as I will explain, both economic theory and empirical evidence give substantial reason to believe that restrained distribution arrangements between broadband providers and content providers are actually more likely to result in efficient outcomes for consumers. Furthermore, even if there is some evidence of an externality problem with contracts providing for priority access to certain content providers–and I have not seen such evidence–the FCC has numerous regulatory options to address the problem short of outright prohibition. Indeed, the EPA does not ban coal production notwithstanding the fact that we have much stronger evidence supporting the conclusion that an unfettered market for coal production results in pollution externalities.

V. Net Neutrality and Vertical Restraints

I would now like to transition from discussing net neutrality in the context of the economics of regulatory policy writ large to discussing net neutrality in the context of the economics of vertical restraints. Broadband providers and content providers occupy different positions in the supply chain. The Netflix customer needs both content–supplied through Netflix–and broadband access–supplied through one of any number of broadband providers–in order to enjoy Netflix's video streaming product. An arrangement between Netflix and one broadband provider that ensures a certain level of speed for customers using the broadband provider's network to access Netflix is simply a vertical contractual arrangement between two entities operating as two links in the same supply chain. The world is full of these vertical contracts in all sorts of different industries. And industrial organization economists have been studying these types of contractual arrangements for decades, so we know quite a bit about their marketplace effects generally.

Although it is well-accepted that vertical contracts occasionally can lead to anticompetitive foreclosure under certain specific conditions,[14] it is equally clear and has long been understood that such arrangements often are part of the regular competitive process and can generate significant efficiencies that enhance consumer welfare.[15] For instance, such arrangements can create efficiencies by reducing double marginalization, preventing free riding on manufacturer-supplied investments, and aligning incentives of manufacturers and distributors.[16] In fact, vertical contracts are frequently observed between firms lacking any meaningful market power, implying that there must be efficiency justifications for these practices. These efficiencies are at least partially passed on to consumers in the form of lower prices, increased output, higher quality, and greater innovation. In other words, the monopoly explanation–that a monopolist uses vertical contracts to foreclose rivals from access to a critical input or a critical set of customers thereby raising the rivals' costs[17]–cannot be the reason for most instances of these types of contracts.

Indeed, there is considerable empirical evidence that strongly supports the view that vertical contracts are more often than not procompetitive. I have summarized this body of literature elsewhere[18] and will not do so again now, but as one study puts it, "with few exceptions, the literature does not support the view that these practices are used for anticompetitive reasons," which supports "a fairly strong prior belief that these practices are unlikely to be anticompetitive in most cases."[19]

Although we do not have the sort of rigorous empirical examination of the effects of vertical restraints in the broad-

band market specifically–the empirical studies I have pointed to relate to all sorts of different industries–anecdotal evidence demonstrates that "non-neutral" business models deployed by broadband providers have often proved highly efficient. In the mid-1990s, when most web content appealed to mass-market consumers, AOL paid brand name media companies, such as Time Magazine and the New York Times, to launch a new business model that offered custom content exclusively to AOL subscribers. This fueled competition with rival internet service providers and gave AOL the incentive to market its services aggressively to new customers, ultimately resulting in the distribution of some 250 million discs with AOL software, thus rapidly increasing consumers' access to the internet. In 2002, a then-upstart Google was able to achieve economies of scale in search by beating out its competition in a bid to become the default search engine on AOL, then the country's leading internet service provider, by offering a substantial financial guarantee.

VI. The Antitrust Approach

Chairman Wheeler's forthcoming proposal to place an outright ban on "paid prioritization" and "the blocking and throttling of lawful content" is a categorical prohibition on certain types of vertical contracts in the broadband industry. If there was strong evidence that the types of vertical contracts the FCC Chairman is seeking to ban harmed consumers, then a categorical ban could be justifiable. But, as I have explained, the best available evidence points in precisely the opposite direction: vertical contracts are far more likely to benefit consumers than to harm them. However, it is undeniably true that vertical contracts can result in anticompetitive outcomes in some circumstances.[20] This raises an interesting question for the FCC: if an outright ban on vertical restraints in the broadband industry cannot be justified, yet there is a chance that vertical restraints could harm broadband consumers, then what should the FCC do? The answer is "nothing," and the reason is because the FTC–my agency–is exceptionally well-equipped to pick up the slack.

The problem with the FCC's proposed approach to net neutrality is that there is no way to identify the vertical contracts that are likely to be problematic ex ante. If economic theory and empirical evidence are correct, most contracts will benefit consumers and some will generate a real risk of competitive harm. In other words, the FCC is faced with a lack of any reliable and economically sound method to identify prospectively network discrimination that should be barred as anticompetitive or absolved as procompetitive.

But what is a novel policy dilemma for the FCC is a problem that antitrust has been grappling with for over a century and for which it offers a clear solution. Indeed, the same sort of reasoning that promotes using tort or contract law to govern occasional disputes between private entities engaged in everyday life and business arrangements rather than to regulate those activities prospectively supports the use of antitrust law to govern arrangements between broadband providers and content providers that end up reducing consumer welfare.

Over the course of the last century, antitrust jurisprudence has evolved a highly sophisticated "rule of reason" to adjudicate various types of vertical arrangements by analyzing their costs and benefits. The rule of reason requires that each vertical arrangement be assessed on a case-by-case basis by marshaling the available economic literature and empirical evidence to evaluate the evidence of actual competitive harm under the specific circumstances of the case. Indeed, antitrust law initially adopted and ultimately rejected–largely based upon the development of the economic and empirical literature I discussed earlier – a categorical prohibition of certain vertical restraints not unlike Chairman Wheeler's proposed prohibition on paid prioritization.[21]

The reason antitrust courts and agencies rejected the view underlying the President and Chairman Wheeler's proposed ban is that a revolution injecting economic analysis and method into antitrust law swept through its institutions in the 1960s and 1970s. The FCC need not catch up its understanding of industrial organization economics to the state of the art in 2015 to get this right; it only needs to embrace what was well understood by 1977 when the Supreme Court first accepted the basic economic principles that rejected categorical prohibitions of the sort embraced by net neutrality proponents.[22]

My view is that antitrust's rule of reason is far more likely to maximize consumer welfare in the broadband industry than Chairman Wheeler's proposed ban. Any legal framework that seeks to maximize consumer welfare must take three factors into account. First, the framework must assess the probability that the challenged business arrangement is anticompetitive. Second, any framework must assess the probability that its application will result in errors, either false positives in which arrangements that benefit consumers are prohibited or false negatives in which arrangements that harm consumers are allowed. Third, the framework must acknowledge the administrative costs of implementing the system.[23] A rule that focuses upon minimizing the social costs of false positives, false negatives, and administrative costs is most likely to generate the highest rate of return for consumers.

Under Chairman Wheeler's proposed categorical prohibition, there will be no false negatives, only false positives. Instances of procompetitive conduct will be erroneously condemned unless you think the empirical research on the effects of vertical restraints is all wrong, at least as applied to the broadband industry. It is true that the rule of reason is probably more costly to administer in the individual case than Chairman Wheeler's proposed blanket prohibition, but the administrative cost the FCC incurs in developing, defining, defending, and re-defining whatever net neutrality order it ultimately adopts that gets upheld by a court is not trivial either.

Although the affirmative case for antitrust over net neutrality is clear on consumer welfare grounds, net neutrality proponents often assert that because antitrust might not "work" in all cases–that is the rule of reason might allow *some* vertical contracts that do in fact harm consumers–a blanket prohibition against all priority contracts is superior. This argument rejects a consumer-welfare based approach to regulation altogether by assuming–contrary to all available theory, evidence, and experience–that every instance of conduct prohibited by the FCC's plan will be harmful. The

argument also seems to suggest that there is some category of harm to consumers that falls outside of the dimensions cognizable within antitrust and consumer protection law–price, output, quality, and innovation–that is both ubiquitous enough to justify categorical prohibition but also only observable to the FCC. That should be enough make any student of regulatory law or economics nervous. I am quite confident that the antitrust regime, after more than a century of developing expertise in applying the rule of reason, will be able to apply it to the broadband industry.

VII. Conclusion

Before we decide *how* best to regulate the broadband industry, we must grapple with the antecedent questions of *whether* and *why* broadband is an industry that even needs regulating. Too often the debate over net neutrality is about the particulars of the FCC's latest proposed regulation and not about the characteristics of the broadband market that justify regulatory intervention in the first place. I hope I have made the case that proponents of net neutrality–the FCC Chairman in particular–have not carried their burden to explain exactly why the broadband industry requires such a tight regulatory regime.

Before I conclude today, I would like to leave you with an example of hospitable regulation in another industry–an industry in which the case for regulation generally is far stronger than in the broadband industry. Those of you who are local will no doubt be familiar with congestion pricing on Interstate 495, the Capital Beltway. Until just a few years ago, all drivers had equal–"non-discriminatory" in the parlance of the FCC's Chairman–access to Beltway in Virginia. Now certain lanes on the Beltway in Virginia are "toll lanes," with the toll to be paid based upon the time of day and the level of congestion. Although at this point it is probably too early to say whether the toll lanes on the Beltway have improved traffic conditions in Virginia, my own experience suggests that it has, though your mileage may vary, literally. In any event, it is noteworthy that the Virginia Department of Transportation is exploring whether to expand the toll program to other highways in the state.

The case for regulation in what I will call the "road" industry is far stronger than it is in the broadband industry. The industry exhibits natural monopoly characteristics–most roads are actually built by the state–and there are obvious negative externalities associated with the use of roads in terms of both traffic and pollution. Yet regulators in this industry, at least in Virginia, are experimenting with new approaches that allow some customers to pay for priority to see if consumers can be made better off. In the broadband industry, the FCC, by contrast, is seeking categorically to prohibit paid prioritization. When the FCC regulates the broadband industry more tightly than Virginia regulates its highways, there is something amiss with the regulatory process. One might even call the FCC's approach "over the top."

Thank you for your time.

Endnotes

1 *See* Verizon v. FCC, 740 F.3d 623 (D.C. Cir. 2014); *In re Preserving the Open Internet*, 25 FCC Rcd. 17905 (2010). *See also* Comcast v. FCC, 600 F.3d 642 (D.C. Cir. 2010); *In the Matters of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd. 14986 (2005).

2 Verizon, 740 F.3d 623 (D.C. Cir. 2014).

3 Ezra Mechaber, *President Obama Urges FCC to Implement Stronger Net Neutrality Rules*, The White House Blog (Nov. 10, 2014), http://www.whitehouse.gov/blog/2014/11/10/president-obama-urges-fcc-implement-stronger-net-neutrality-rules.

4 Tom Wheeler, *FCC Chairman Tom Wheeler: This Is How We Will Ensure Net Neutrality*, Wired (Feb. 4, 2015), http://www.wired.com/2015/02/fcc-chairman-wheeler-net-neutrality/.

5 *See* Harold Demsetz, *Two Systems of Belief About Monopoly*, in Industrial Concentration: The New Learning 164 (Harvey J. Goldschmid et al. eds., 1974).

6 *See, e.g.,* Comment of the Fed. Trade Comm'n to the D.C. Taxicab Comm'n 5-7 (June 7, 2013); Fed. Trade Comm'n, Possible Anticompetitive Barriers to E-Commerce: Wine, app. A, at 8-9 (2003).

7 *See* Dave D. Haddock, *Irrelevant Externality Angst,* 19 J. Interdisc. Econ. 3 (2007).

8 *See, e.g.,* George Akerlof, *The Market for "Lemons": Quality, Uncertainty and the Market Mechanism*, 84 Q. J. Econ. 488 (1970); Howard Beales, Richard Craswell & Steven C. Salop, *The Efficient Regulation of Consumer Information*, 24 J.L. & Econ. 491 (1981).

9 Wheeler, *supra* note 4.

10 Verizon, 740 F.3d at 663-64 (Silberman, J., dissenting) (Noting that "all retail stores, for instance, are 'gatekeepers.' The term is thus meaningful only insofar as the gatekeeper by means of a powerful economic position vis-à-vis consumers gains leverage over suppliers.").

11 *See id.* at 662-667 (Silberman, J., dissenting) (explaining that the FCC failed to undertake analysis of whether broadband providers had market power in individual markets and noting that "[t]he Commission apparently wanted to avoid a disciplined inquiry focused on market power.").

12 *See* Timothy J. Brennan, *Network Neutrality or Minimum Quality? Barking Up the Wrong Tree – and Finding the Right One*, CPI Chronicle (Mar. 2012) ("The relevant market failure is not insufficient competition but failure to recognize the network externality in the broadband environment: the value of internet access to a content supplier depends upon its viewers' ability to access links in its content. This market failure does not justify full net neutrality, in particular a non-discrimination rule. It does suggest a minimum quality standard . . . .").

13 Wheeler, *supra* note 4.

14 *See* Thomas Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price*, 96 Yale L.J. 214 (1986).

15 *See, e.g.,* Benjamin Klein, *Exclusive Dealing as Competition for Distribution "On the Merits"*, 12 Geo. Mason L. Rev. 119 (2003); Oliver E. Williamson, *Assessing Vertical Market Restrictions: Antitrust Ramifications of the Transaction Cost Approach*, 127 U. Pa. L. Rev. 953 (1979); Oliver E. Williamson, Markets and Hierarchies: Analysis and Antitrust Implications (1975).

16 *See, e.g.*, Benjamin Klein & Joshua D. Wright, *The Economics of Slotting Contracts*, 50 J.L. & ECON. 421 (2007); Benjamin Klein & Andres V. Lerner, *The Expanded Economics of Free-Riding: How Exclusive Dealing Prevents Free-Riding and Creates Undivided Loyalty*, 74 Antitrust L.J. 473 (2007); Benjamin Klein & Kevin M. Murphy, *Vertical Restraints as Contract Enforcement Mechanisms*, 31 J.L. & ECON. 265 (1988); Howard Marvel, *Exclusive Dealing*, 25 J.L. & Econ. 1 (1982).

17 *See* Krattenmaker & Salop, *supra* note 15, at 230-31.

18 *See* Joshua D. Wright, Comm'r, Fed. Trade Comm'n, Broadband Policy & Consumer Welfare: The Case for an Antitrust Approach to Net Neutrality Issues, Remarks at the Information Economy Project's Conference on US Broadband Markets in 2013, at 10, n. 15-17 (Apr. 19, 2013).

19 Daniel O'Brien, *The Antitrust Treatment of Vertical Restraints: Beyond the Possibility Theorems*, in Report: The Pros and Cons of Vertical Restraints 40, 72-73 (2008). There is a general consensus among empirical economists on this point. *See also* Francine Lafontaine & Margaret Slade, *Exclusive Contracts and Vertical Restraints: Empirical Evidence and Public Policy*, *in* Handbook of Antitrust Economics (Paolo Buccirossi ed., 2009); James C. Cooper, Luke M. Froeb, Dan O'Brien & Michael G. Vita, *Vertical Antitrust Policy as a Problem of Inference*, 23 Int'l J. Indus. Org. 639 (2005).

20 *See* Krattenmaker & Salop, *supra* note 15.

21 *See, e.g.*, Leegin Creative Leather Prods v. PSKS, Inc., 551 U.S. 877 (2007) (applying rule of reason to minimum resale price maintenance); State Oil Co. v. Kahn, 522 U.S. 3 (1997) (applying rule of reason to maximum resale price maintenance); Continental T.V. v. GTE Sylvania, 433 U.S. 36 (1977) (applying rule of reason to non-price vertical restraints).

22 *See* GTE Sylvania, 443 U.S. 36.

23 Thomas W. Hazlett & Joshua D. Wright*, The Law and Economics of Network Neutrality*, 45 Ind. L. Rev. 767, 798.

Book Review

The Conservatarian Manifesto

By Charles C.W. Cooke

*Reviewed by Jeremy Rabkin**

Charles C.W. Cooke grew up in England, attended Oxford, then came to America and began writing for National Review. Fans of his magazine articles – and I count myself among them – will recognize Cooke's style: cool, witty, firmly judgmental. Each of the ten short chapters in this book could make for a provocative essay if published separately in an opinion magazine. Taken together, however, they don't add up to a very compelling book.

To start with, the title conveys a misleading sense of the contents. The narrative voice is far too relaxed and reasonable for the sort of strident demands Americans associate with the term "manifesto." Yet neither does the book offer up long lists of policy commitments in the style of a British political party's "election manifesto." (In the 2015 campaign, for example, the Tory "manifesto" promised to ease restrictions on fox-hunting – among other things.) The Conservatarian Manifesto defends familiar general perspectives rather than urging precise policies.

The intriguing term "conservatarian" might be worth a book-length explication. Debate between "traditionalists" and "libertarians" was already a staple at "conservative" gatherings in the 1950s. In 1962, Frank Meyer – the father of Federalist Society President Eugene Meyer – published a book elaborating a "fusionist" defense of freedom as common ground between contending conservative camps.

Cooke doesn't claim credit for coining the term "conservatarian." But he also doesn't explore the origins of this apparently new term. He's not very interested in the history of the American conservative movement over the past half century, nor is he very interested in the earlier history of ideas in the wider world.

Cooke remains a topical journalist in this book. The book has no footnotes. When it quotes someone else's words, they are almost always the words of a fellow opinion journalist, a blogger, or another guest on a television talk show where Cooke has appeared.

Still, in his breezy way, Cooke tries to cover quite a lot of issues. His version of "conservatarian" embraces a range of positions that don't usually sit under the same ideological banner. He firmly endorses the libertarian view that the "war on drugs" has been a "failure," and urges that the federal government retreat from this field. But a later chapter defends military spending and an interventionist foreign policy. Cooke argues that same-sex marriage should be allowed, along with ready access to firearms – but he also defends restrictions on access to abortion. He also favors tough enforcement of border controls and limits on immigration. In each case, Cooke offers a quick sketch of his reasons for favoring a particular policy but these arguments remain rather… sketchy.

The discussion of drug legalization is somewhat representative. Cooke notes that federal regulation of narcotics began under Woodrow Wilson and gained further reach under Franklin Roosevelt and Lyndon Johnson. He then offers some figures on the high numbers of people incarcerated in federal prisons on drug charges. Then he urges that regulation of narcotics should be left to the states. He doesn't discuss whether live-and-let-live or local-option should be applied to all recreational drugs or only to the less disabling (or less violence inducing), such as marijuana.

Why do all western countries agree that heroin and cocaine should be strictly regulated? That basic question doesn't get explored here. If all (or almost all) states want to prohibit the most dangerous drugs, could they seek federal assistance in resisting drug trafficking across state lines or across international borders? There's no discussion of that, either. The drug chapter strikes a libertarian posture without offering much assurance that the alternatives will prove acceptable or feasible.

So with the move to same-sex marriage. Cooke disagrees with libertarians who say the state has no business conferring special status on special kinds of relationships. He sensibly replies that every society has a residual interest in the conditions in which the next generation of citizens is reared. The extreme libertarian position, as he notes, must accept polygamy on the same grounds that it accepts same-sex marriage – and perhaps incest as well.

But Cooke himself argues that conservatives should accept same-sex marriage because "little good can come from the government's active suppression of a social change that arose organically and over the course of decades." That might sound soothing – but it ignores the fact that most changes in marriage law have been imposed by courts and almost all in one decade. And it still offers no ground for opposing polygamy or other deviations from traditional man-woman marriage.

The problem with Cooke's assortment of policy positions isn't that they are inherently contradictory. A political program must accommodate circumstances in its own time. Even advocates who want to rail against the prevailing political tides will have more chance of diverting the headwaters into safer channels if they let themselves abandon some positions as no longer feasible. A political program – even a "manifesto" – should not be judged by its logical rigor.

The problem with the "conservatarian" program, at least as Cooke presents it, is that it has no well-defined core, no evident center of gravity. The left side of the American political spectrum favors a vast range of government controls to foster what it conceives as fairness or equality – for consumers, for small business, for workers, for minorities, for women or other groups it sees as requiring extra protection. Both libertarians and more traditional conservatives tend to be much more skeptical of govern-

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The Conservatarian Manifesto *is available for order on Amazon.com: http://www.amazon.com/The-Conservatarian-Manifesto-Libertarians-Conservatives/dp/0804139725*

ment interventions in the economy. Cooke's "manifesto" gives no sustained attention to economic issues, however. It's as if one of the central themes of political debate – and one of the central cleavages in American political life – is beneath his notice.

It's true, of course, that people who share broad skepticism of government's role as an economic manager may still have strong disagreements on other matters, even other matters which affect this main concern. Libertarians tend to distrust state and local government along with the federal government and often urge courts to give more scrutiny to government controls at all levels. More traditional conservatives often embrace a populist distrust of all branches of government, which makes them suspicious of judicial activism, even for conservative causes. Cooke does offer a chapter endorsing conservative veneration of the Constitution and opposing the notion that courts can rely on their own judgments to extend a "living Constitution." But he says almost nothing about how courts should interpret the actual Constitution, which was thought to justify much judicial protection for economic liberty and property rights before progressives preached disregard for the actual Constitution. A parallel debate about how much courts should defer to determinations of administrative agencies – which does not necessarily require new interpretations of constitutional guarantees – goes entirely unnoticed.

For a book that purports to synthesize libertarian and conservative views, Cooke gives surprisingly little attention to their underlying differences. Judicial philosophy is a good example. Before the New Deal, courts were often skeptical of government controls on the economy but treated laws for the protection of "public morals" as a quite different category, which courts rarely dared to challenge. Now courts challenge such laws all the time. If you're a hard-core libertarian, you may want courts to protect sexual freedom or scrutinize government benefits to religion. If that's what judicial activism means, a lot of conservatives won't embrace it at all, even when it happens to be directed at controls on commercial activity.

One could say much the same about religion. Conservatives tend to be sympathetic to traditional government policies that give recognition to shared religious beliefs or provide accommodation to religious practice. Libertarians are wary of giving any special status to religion. Cooke has almost nothing to say about this debate. The conservatarian synthesis here seems to rest on a decision to ignore religion even as a topic worthy of thought or discussion in an overall political philosophy.

Cooke does offer a chapter on federalism, but that discussion also comes across as a ramshackle compilation of the author's personal preferences. Cooke argues that both libertarians and conservatives should recognize the benefits of keeping government close to the governed – even physically close, so different states and localities can develop policies that most suit local constituents. Invoking the claims of federalism and local choice, he scolds the congressional Republicans of the George W. Bush era for trying to outlaw partial birth abortion. Yet he ends this chapter by acknowledging historic concerns about abuse of minorities by local majorities. So, he concludes, "conservatives should be firm in their conviction that protections aimed at defending the fundamental rights of all Americans are best achieved at the national level and should not be at the mercy of local politics." He never acknowledges that there is ongoing debate about what rights should count as "fundamental."

It may be that the collection of policies that happen to be favored by Charles C.W. Cooke will prove a winning formula for Republican candidates in 2016. Still, The Conservatarian Manifesto doesn't spend much time parsing opinion surveys or analyzing demographic trends to persuade readers that this is so. Cooke may well have sound intuitions about what now appeals to a majority of voters – or what might please them, without offending them. But political moods are in constant flux.

It may be, then, that The Conservatarian Manifesto can provide some helpful cues to candidates in next year's elections. It's not likely that people thinking about great political questions will want to give the book another look in the years after that. In Cooke's telling, at least, conservatarianism is not a philosophy for the future, but just a slogan for the moment.

Special Feature

14th Annual Barbara K. Olson Memorial Lecture

*By John A. Allison**

Good evening. It's really both a pleasure and honor to be here. I want to start by congratulating all of you as members of the Federalist Society. I've had the pleasure of speaking at a number of Federalist events over the years, and I've always found a very thoughtful and engaged, focused audience, and you've done an incredibly important job defending the rule of law and defending the Constitution, and that's very important work. And I personally thank you for your impact.

I want to tell you a minute about Cato. Many of you probably know about Cato, but some of you don't, and it's a little context from my presentation. Cato is the world's leading libertarian think tank. Our mission is to create a free and prosperous society based on the principles of individual liberty, free markets, limited government, and peace. We really do believe in limited government. We think the government should stay out of your pocketbook, but we also think the government should stay out of your bedroom. We think government has only one role, but a very important role. Government is fundamentally in the business of protecting individual rights. It's to keep me from using force or fraud to take what you've earned or deny you your individual rights, and to keep you from using force or fraud to take what I've earned or deny me my individual rights.

And in that context, we think government has three primary purposes. We need a national defense to defend us from the bad guys overseas. We need a police force to defend us from bad guys in our neighborhoods, and we need an effective court system to settle legitimate disputes, so we don't have to resort to violence. In our world, there would be radically less regulations and a much more effective court system than we have today.

The reason that we think government should be limited is because it has a unique and special power. It has a gun, and people with guns can be dangerous. Walmart can argue, they can persuade, they can do ads, they can cut prices to try to get you to come in and buy products, but they can't make you go into Walmart. The government can force you to pay taxes. It can force you to obey by its rules. They can put you in jail, or they can kill you. In fact, governments throughout history have killed hundreds of millions of people. After disease and old age, governments are the primary cause of death, so it's a very dangerous institution. This is why its powers need to be limited and controlled, which is what the Founding Fathers were trying to do.

In that context, I believe there is a fundamental philosophical fight going on for the future of western civilization, and the outcome of this fight will have a profound impact on the quality of our lives and particularly our children and grandchildren's lives. On the one side are the classical liberals and libertarians who are defenders of the ideas that made America great—life, liberty, and the pursuit of happiness.

On the other side are the statists of all persuasions. Statists believe that smart people in Washington, D.C., elitists, can figure out how to solve human problems, and that they know what is in the common good. They know what's good for all of us, and they like to exercise power, exercising in that regard towards the common good. The statists do exist on the right as well as the left. The statists on the right largely want to control our personal lives. The statists on the left largely want our money, but they also want to control aspects of our personal lives.

The most visible form of statism today and the one I want to talk about is the progressive movement. The progressive movement is actually an old movement. This philosophical fight has been going on for over 100 years, but it has accelerated recently. The progressives have tried to grab the moral high ground and use that as leverage to advance the role of the state. They have three fundamental philosophical pillars under their ideas: altruism, collectivism, and egalitarianism.

Altruism. Altruism is not benevolence. Benevolence is a good thing. Altruism is other-ism. It says that everybody is important but you. Now, the problem with that is there are only "but yous," right? There's nobody but you, which means no individual is important, and this is how altruists really see the world. Only the group, only the collective is important, but what's ironic, even though individuals don't have rights, everybody has rights. Everybody has a right to a nice house. Everybody has a right to free medical care. Provided by whom? My right to free medical care is a right to force a doctor to provide that care or to force somebody to pay for that doctor. Exactly the opposite in the American concept of rights. In the American concept of rights, you have the right to what you produce and what you create. You don't have the right to what somebody else produces and what somebody else creates. For altruists individuals don't matter. Their focus is on the collective and the so-called common good.

Now, here's one of the dilemmas. The common good to a large degree is an oxymoron. In fact, the Founding Fathers probably defined all the areas of common good in the Bill of Rights. Almost everything else is better or worse for somebody. It's good for me, bad for you, good for you, bad for me. There are very few common goods. It's an oxymoron, and what the common good means in practicality, it becomes the good of my group. Is it good for my sex, good for my race, good for the unions, good for the farmers, good for taxi drivers, good for big business? Good for my group, and so that collectivist idea leads to group warfare which is exactly what we have going on in the United States today. Group warfare in the name of the so-called common good.

Underlying this idea is the basic sense of justice that

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progressives have, and justice largely defines much of public policy, including a lot of the law, and your sense of justice. The sense of justice of progressives is egalitarianism.

Now, what's interesting is in some ways, the United States is an egalitarian society, the Founding Fathers in the Declaration of Independence, said "All men are created equal," but they were talking about equality before the law. Just because you are the son of a baron doesn't give you any special rights. The progressives have redefined egalitarianism as equal outcome.

Here's an interesting observation. We all should be equal before the law, and every human being deserves dignity and respect simply because they're a human being, but it is not true that everybody is equal. In fact, I have never met two equal people. Every person in this room is a unique, special individual. We all have different strengths, different weaknesses, different ambitions, different talents, different goals. We're all unique special individuals. That's actually the great news. That's what makes life so interesting. Every person in this room is a unique special individual, but we're not equal. At the extreme, Thomas Edison and the Boston Strangler are not equal.

The only way to get equal outcomes from unequal people is to use force, is to use a gun, and egalitarians are in the business of using force, of using a gun to take what somebody has produced and giving it to somebody that has not earned it. That's what they do.

I want to concretize egalitarianism for you with a story. The story will tell you a little bit about my age and where I went to school. One of my heroes was Michael Jordan. I thought Michael Jordan was a great basketball player, and he was a real inspiration to poor kids. Now, this will surprise you, but I am not as good a basketball player as Michael Jordan. There is a serious differential in performance. What is interesting is I cannot get to be as good a basketball player as Michael Jordan. It's not possible. I don't care how hard I try and how hard you try to help me. I cannot be as good a basketball player as Michael Jordan. Can't do it. You cannot make the average great. You can make the average better. That may be a very productive, very noble thing to do, but you cannot make the average great. However, you can make the great average, and egalitarians by definition have to be in the business of making the great average. That is the only way you can make people equal.

It's easy to make Michael Jordan as good a basketball player as me. Just cut his legs off.

You say we wouldn't do that, but we've been pretty tough on great people throughout western history. We poisoned Socrates, imprisoned Galileo, burned Joan of Arc. We're more sophisticated today. We do it with lots of balls and chains. We do it with lots of taxes. One percent of the population pays 25 percent of the taxes, 5 percent pays 50 percent, and 50 percent of the taxpayers pay no income tax. It's a great way to run a democracy. Lots of government rules and regulations are designed in many ways to create controls over the productive, the innovative, and the creative. What people fail to realize is that great people make a disproportionate contribution to human well-being. Everybody in this room—your children, your grandchildren—have a better life, thanks to Thomas Edison. He not only invented the light bulb; he invented electrical generation. He invented the research laboratory itself. Put balls and chains on great people, and reduce the quality of life for all of us.

But here's what the egalitarians want to do. They want to claim the moral high ground, and this is important to remember. Whoever owns the moral high ground at the end of the day wins the argument. They want to claim the moral high ground because who can argue with everybody being equal. However, I think the egalitarians do not have the moral high ground. I think what motivates them is the absolute, most destructive of all human emotions, and watch it in yourself. It's called envy. It's hatred of the good for being the good.

And by the way, egalitarianism is a lot worse than I just described. Think about this. Any attribute you want to pick, half the people are below average. It's the math, right? Or technically below the mean.

I love music, and I am a horrible singer. I was raised in the Baptist church. If you've ever been in the Baptist church, the preacher is trying to get everybody to sing but me—but me. "Please don't sing." It would be horrible to make everybody have to sing as badly as I do, and I would actually lose in that process, right? That's how bad egalitarian really is. Well, egalitarians claim they don't want to go that far, but if you want to understand a philosophical idea, you need to see where it ultimately ends.

And I'll say this with certainty, and this certainly defines the Obama administration and egalitarians in general. They would far rather us all be poor and more equal. Their sense of justice which drives a lot of their behavior is about equality, not the overall quality of life.

On the other side of this argument are those classical liberals and libertarians that believe very strongly in life, liberty, and the pursuit of happiness. Each individual's fundamental, unequivocal moral right to their own life, each individual's moral right to the pursuit of their personal happiness, each individual's moral right to the product of their labor, if you produce a lot, you get a lot, including the right to give it away to whoever you want to for whatever reason you want to. If you think about that moral prerogative, it demands personal responsibility, because there is no free lunch. It also demands rationality and self-discipline. It creates the principles that underlie a successful society.

Life, liberty, and the pursuit of happiness. As classical liberals and libertarians, we are primarily defenders of liberty. Now, a lot of people talk about liberty, and a lot of people think of liberty as a nice thing. Well, liberty is a nice thing, but it's a lot deeper than that. Liberty is essential for human flourishing. It's essential for human flourishing economically in the physical world, but it's also essential for human flourishing spiritually. Economically, in order to be productive, a producer must be able to think for himself. He must be able to pursue his truths, what he thinks is right and explore and make innovations, make choices. If somebody makes you act like two plus two is five, you literally cannot think, and lots of government rules and regulations make people act like two plus two is five.

Reflect on this fact. All human progress, by definition, is based on innovation and creativity because unless somebody does something better, which will be different, there can be no progress. Creativity is only possible to an independent thinker. Somebody that thinks like the crowd, cannot be creative, cannot

contribute to human progress. That is why entrepreneurs are so important. Entrepreneurs take the ideas of scientists and engineers and turn them into reality. Without entrepreneurship, there is no progress, and what characterizes entrepreneurs? They are independent thinkers. They are free thinkers. They come up with ideas that the rest of us don't see. They explore, and they fail. For every Google, there's a thousand failed Googles. For every Walmart, there are 10,000 failed Walmarts. But entrepreneurship is only possible to somebody that is free.

We published a book last year called *Poverty and Progress* that looked at human well-being from time immemorial, and it's very interesting. From the evolution of *Homo sapiens*, 250,000 years ago, until the late 1700s, life expectancy for humans was basically flat. There was some improvement in the quality of life, but people lived to about 30 years old on average. That was the human life expectancy. And then something happened in the late 1700s that transformed the quality of life and life expectancy first in western civilization, and the same thing is happening in the rest of the world now. There was an invention in the late 1700s, more important than fire, more important than the wheel. It was the invention of the rule of law, of individual rights, of free markets, of capitalism. That invention transformed the planet. It's because people could think for themselves. They could explore. They can invest. They could create and innovate. Capitalism was the source of physical human well-being and the improvement of life expectancy on the planet. So liberty is not just nice in an economic sense. It's essential for human well-being in a physical sense. It's essential for innovation and creativity, which is the source of all progress.

But liberty is also essential for something that you can argue is even more important. It's essential for spiritual well-being in the context of the pursuit of happiness. The real pursuit of happiness, not having a good time on Friday night, although it's good to have a good time on Friday night, but in the sense of a life well lived, in the Aristotelian sense of the pursuit of happiness, hard work, blood-and-sweat-and-tears happiness. When you're 80 years old, you look back and say, "Man, that was hard, and I'm glad I did it." When you think about happiness in that context, it has to be earned. You cannot be entitled to be happy.

Something I tell students, you have to take personal responsibility if you're going to earn happiness. If you view yourself as dependent, as entitled, you give away the opportunity to be happy because you are dependent on somebody else, and you don't control your own life. To be happy, you have to set goals for yourself. You have to live consistent with your values, what's important to you. You pursue your truths as a free person.

Now, being free doesn't guarantee you will be happy, but if you aren't free, it guarantees you cannot be happy. So liberty is essential for human spiritual well-being.

Let's talk a little more about the pursuit of happiness. That to me is the world-changing idea in the Declaration of Independence. Before Jefferson, before the thinkers of the enlightenment, everybody existed for somebody else's good, good of the king, good of the state, good of the church. Nobody existed for their own good, but Jefferson said that each of us has a moral right for the pursuit of our personal happiness, not guaranteed success in that pursuit, but we have that right. That idea created the most successful society and, interestingly enough, the most benevolent society in human history. When people have the right to their own life, they are naturally nicer to other people. In communist and socialist societies, everybody ends up hating each other because they're all slaves to each other. And by the way, communist and socialist societies also at the same time destroy innovation and creativity. Make a list of all the innovations from the Soviet Union, North Korea, and Cuba. It's a really short list.

I want to talk about the pursuit of happiness at even a deeper level because, by the way, isn't that a very selfish idea, and isn't it bad to be selfish? Isn't that a very strong belief in our society? I can see Johnny in the sandbox, 3 or 4 years old, playing with his truck, not bothering anybody, having a good time. Along comes Fred. Fred would like to have Johnny's truck. Johnny doesn't want to give him the truck. Discussion, debate, argument ensues. Mom, dad, Sunday school teacher, kindergarten teacher get involved in the argument. Mom says, "Hey, Johnny, give that truck to Fred. Don't be selfish. Don't be bad." Two great moral lessons being taught in the sandbox, right? Number one, where did Fred get the right to Johnny's truck? Do you want to know where our social welfare system comes from? There it is. So Fred is now 30 years old, and he wants a Ford Ranger. Okay.

But the real damage is done to Johnny, and I'll bet almost everybody, probably everybody in this room is Johnny. What lesson did you learn in the sandbox? That for some reason, somehow that scoundrel Fred has a right to your life, that you have some kind of obligation to Fred for some unknown reason, or you will be a bad person.

Let's talk about acting in one's rational self-interest. Immutable, non-negotiable fact of reality. Everything that is alive must act in its self-interest or due. Immutable, non-negotiable fact of reality. Everything that is alive must act in its self-interest or die. A lion has to hunt or starve. A deer has to run from the hunter or be eaten. Trees shade out other trees to get sunlight. Amoeba take chemicals that other amoeba would like to have. Life is by definition self-sustaining action. Anything that doesn't self-sustain its life dies. That's how Mother Nature designed the system. Sorry.

To say that man is bad because he is selfish is to say you're bad because you're alive. We get two really destructive false alternatives, and here are the false alternatives, to take advantage of other people or to self-sacrifice, neither one of which make any sense. In fact, a lot of people think that selfish is about taking advantage of other people. Here is the irony. Taking advantage of other people is not selfish. It's self-destructive. It's self-destructive in two ways. First, you might fool Tom, Dick, and Harry, but they're going to tell Sue, Jane, and Fred, and nobody is going to trust you. And you know people like that. If you're not trusted, you're certainly not going to be successful, and you're not going to be happy.

There's a deeper cause. We all want to influence other people. I'm hoping to influence you today, but when you let go of reality, when you let go of the truth to manipulate somebody else for your advantage, you do a whole lot more damage to your psychology than you do to theirs.

My career, running a large bank, I got to meet a lot of

successful people. However, I never met anybody that was both successful and happy that I think got there taking advantage of other people. Now, I've met some people that had a lot of money that I think got there taking advantage of other people, and they were the most unhappy people I ever met. Taking advantage of other people is not selfish. It's self-destructive.

How about self-sacrifice? That is the moral code of our society, right? You hear it in school. You hear it in the newspapers. You hear it on TV. You hear it in church. We're all supposed to self-sacrifice. I want to ask you to ask yourself what I think is the most important question you can ask yourself, and particularly think about this question in terms of how you would like your children and your grandchildren to answer. Do you have as much right to your life as anybody else has to their life? Do you have as much right to your life as anybody else has to their life? Of course, you do. Why would you believe anything different than that? And think about what not believing that means, because in this room, there is only I's, I, I, I, I. If none of the I's, if you do not have a right to your own life, if I don't have a right to my life, nobody has a right to their life, right? And that's where the collectivist power shows up because we don't have a right to our own lives. You have to be willing to defend your right to your life to the pursuit of your personal happiness if you're really going to defend a free society. So neither taking advantage of other people nor self-sacrifice makes any sense. But there is a rigorous, demanding moral code that underlies free and prosperous societies. We are fundamentally traders. We trade value for value. We get better together.

In our business, when I was running BB&T, our goal was to help our clients be economically successful and financially secure, and we expected to make a profit doing it. Life is about figuring out how to get better together. There are only two stable relationship conditions, win-win and lose-lose. Whenever you get greedy and you set up a win-lose—and you see this in spousal relationships—pretty soon, your partner is going to get bitter, and you're going to end up in a lose-lose. Whenever you get self-sacrificial, interestingly enough, and you set up a lose-win, you'll get bitter, and you end up in a lose-lose relationship. So in any meaningful relationship in your life, you should ask, "What's in it for me?" That's a fair question, but you should also ask what's in it for them because if it's nothing in it for them, at the end of the day, there will be nothing in it for you.

Now, of course, it's in your rational self-interest to help the people you care about, your family, your friends, people you work with. If you love your children, helping your children is not a sacrifice. In fact, love is the ultimate expression of selfishness. Now, most people don't think that way, but I'll tell you a story I tell college students. You are getting ready to get married, a big event in your life. Your future spouse comes running up to you and says, "Honey, I'm so excited about marrying you. This is the biggest self-sacrifice I've ever made." Not exactly what you wanted to hear, is it? Not exactly what you wanted to hear.

If you really love somebody, you might be willing to die to protect them because they're so valuable in a very selfish sense to you. I believe it's in my rational self-interest to support the United Way. The United Way is an umbrella charity organization which does lots of good in the community in which I live. I wouldn't want to live in the kind of community that would exist without a United Way, and I wouldn't want my children to live in that community. So I suppose the United Way because I believe it is in my rational self-interest.

So what would be required really to act in your rational self-interest? The first thing you'd have to do is hold the context. Sometimes when people talk about selfishness, they talk about people that take advantage of other people, but also people that are what I call linear thinkers, they have this kind of focus-on-themselves world view. The irony of that, that's not selfish. That's irrational because you have to hold the context, and the context is what kind of world would you like to live in, and what would you enjoy doing helping create that kind of world? It doesn't have to be grand. Maybe you want to open a restaurant and have better food, lower prices. What kind of world would you like to live in, and what would you enjoy doing to help create that kind of world? You'd have a sense of purpose. You'd take care of your body. You'd eat properly. You'd exercise. You'd take care of your mind. You'd read, study, think. You'd work hard to create healthy human relationships with other people that share your values, and you'd have a rational value system. What if everybody had a sense of purpose, did the best they could to take care of their body, did the best they could to take care of their mind, worked hard to create healthy relationships with other human beings and had a rational value system? I would argue that 90 percent of the world's problems would go away.

You hear it over and over again. The problem is that people are selfish. My observation is very few people consistently act in their rational self-interest. Most people are self-destructive in some aspect of their life. I had a brother-in-law who drank 24 beers a day, got cirrhosis of the liver, drank 24 beers a day and died. People say he's selfish. No. He was self-destructive. Bernie Madoff stole hundreds of millions of dollars from his family and friends over 30 years. Can you imagine spending 30 years stealing from the people that are closest to you? The guy was miserable. He said the best thing in his life was when he got arrested. They say Bernie Madoff was selfish. No. He was self-destructive. He was self-destructive.

If we're going to defend a free society, we must defend each individual beginning with your right to the pursuit of personal happiness in the right kind of context, in working towards a better world through a sense of purpose, but doing things that you enjoy for you because you have a fundamental right to your own life.

One last thought about the pursuit of happiness or happiness in general. By the way, happiness is the end of the game. Sometimes business people get confused. They think money is the end of the game. Nothing wrong with money. Money is a good thing, but money is not an end. Happiness in that Aristotelian sense that I described is the end of the game. And the foundation for happiness is rational self-esteem, real self-esteem.

A couple thoughts about real self-esteem. First, real self-esteem is fundamentally confidence in your ability to live and be successful given the facts of reality. Therefore, real self-esteem is earned by how you live your life. Nobody can give you self-esteem. You cannot give anybody self-esteem. You cannot give your children self-esteem. Live your life with integrity; raise

your self-esteem. That's why integrity is important.

Second thought about self-esteem. In order to have a high level of self-esteem, you must believe at a very deep level, you are capable of being good, and you have the moral right to be happy. That whole conversation that we just had about the pursuit of happiness, if you don't believe you have a right to earn happiness, you can't have a high level of self-esteem.

Final thought about self-esteem. In the real world, self-esteem primarily comes from productive work. As human beings, we survive by production as part of our nature, and I use productive work in the broadest context. Raising children is very productive work. For everybody in this room and most of the people on this planet, the single biggest driver of your self-esteem is your work, because you spend a disproportionate amount of time, effort, and energy at work. That's what makes work important. Something I said many times to the employees of BB&T, "It's really important to BB&T that you do your job well, but it's far, far more important to you. You might fool me about how well you do your job. You might fool your boss about how well you do your job, but you'll never fool you. If you don't do your work the best you can do it, given your level of skill, given your level of knowledge, you can't do the impossible. If you don't do your work the best you can do it, you will lose your self-esteem."

Now, here's the good news. The flip is also true. Do your work the best you can do it, given your level of skill, given your level of knowledge, and you will raise your self-esteem, which is more important than whether you get more money, or a promotion, because it's about your character. It's about who you are as a human being, and there's actually a very important societal message in that issue that I think is relevant to this group.

Take a construction worker, a bricklayer. He has a really tough, hard, grinding life. My granddad had that kind of life, tough, hard, grinding life. The bricklayer has a tough, hard, grinding life, but he and his wife successfully raised their children. Maybe his granddaughter becomes CEO of a publicly traded company. Maybe not. He has a tough, hard, grinding life, but he gets something very precious from his work. He gets to be proud of himself. He gets to have self-esteem. Take that same bricklayer and give him welfare. He may have more money, but he loses part of his soul. He loses his pride. He loses his self-esteem.

You know, with the Obama administration, there's a lot of general talk in Washington about security, and it's a false talk about security because what they want us to be secure from is the laws of reality, which you can't be secure from. But even if it were true, it would be off mission for America. People didn't get on a boat and come to Jamestown to be secure. The United States is the land of opportunity, opportunity to be great, opportunity to fail and try again, but most importantly, the opportunity of that bricklayer to live life on his own terms, to pursue his personal happiness based on his beliefs, his values, to pursue his personal happiness as a free and independent person. I think that's what the Founding Fathers were doing when they wrote the Declaration of Independence, defending that ideal. I think that's why what you are doing at the Federalist Society is very important work. You are defending the ideal of the right to pursue your personal happiness, which is a unique American sense of life that is so important for us to protect.

Thank you very much.