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ARTICLE

INTERPRETIVE METHOD AND THE FEDERAL RULES OF EVIDENCE: A CALL FOR A POLITICALLY REALISTIC HERMENEUTICS

ANDREW E. TASLITZ*

In a companion article, Professor Taslitz challenged the claims of many evidence scholars that the United States Supreme Court has adopted a "plain meaning" or "new textualist" approach to interpreting the Federal Rules of Evidence.[1] Rather, he argued, the Court has implicitly followed a more flexible, wide-ranging approach that considers varied data beyond the text.

This Article argues that the Court has recently explicitly and vigorously moved closer to this more flexible approach. The Article more carefully defines this approach—this "politically realistic hermeneutics"—defending it against plain meaning by drawing on the teachings of political science, economics, and literary theory.

I. THE COURT'S MOVEMENT TOWARD A POLITICALLY REALISTIC HERMENEUTICS

In a companion article to this piece, I argued that those evidence scholars claiming that the United States Supreme Court has followed a "plain meaning" approach to interpreting the Federal Rules of Evidence were wrong.[2] Plain meaning or "new textualist" theorists argue that the clear, "ordinary" meaning of a statute's words should control.[3] Moreover, where there is lack of clarity, they will sometimes draw first on the structure of the statute—the form and language of its other purportedly "clear"

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[1] *See* Andrew E. Taslitz, Daubert*'s Guide to the Federal Rules of Evidence: A Not-So-Plain-Meaning Jurisprudence*, 32 HARV. J. ON LEGIS. 3 (1995) [hereinafter Taslitz, Daubert*'s Guide*].

[2] *Id.* at 3–7.

[3] WILLIAM N. ESKRIDGE, JR., DYNAMIC STATUTORY INTERPRETATION 38 (1994) [hereinafter DYNAMIC INTERPRETATION].

provisions[4]—and second, on policy clearly stated in, or easily derivable from, the text.[5] Additionally, they believe that the concept of a public-regarding legislative "intent" is incoherent, both because we cannot accurately aggregate the very different motivations of individual legislators and because most statutes reflect the narrow, selfish demands of powerful interest groups, not any public-regarding purpose.[6] Consequently, they argue, extra-textual inquiries into intent, as revealed by floor speeches, debates, and committee reports, are misguided; only the text is enacted into law, so only the text should control.[7]

The prior article argued that the Court has, in fact, implicitly rejected the assumptions of the plain meaning theorists, instead adopting a more flexible interpretive method, that weighs a wide variety of sources in addition to text, including committee reports, other legislative history, and sound policy. That approach forms the core of an alternative interpretive method—a "politically realistic hermeneutics."[8]

Part II of this Article will define in greater detail what "politically realistic hermeneutics" is and will defend it against plain meaning theorists. Part II will in particular argue that the plain meaning theorists' view of language as having an inherent, "plain" meaning is flawed and that the Rules reflect a real and

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[4] *See id.* at 239, 271. For example, Justice Scalia, a textualist, rarely finds ambiguity in statutory language and usually rejects "vertical coherence"—the search for the statute's consistency with authoritative sources situated in the past, such as the original intent of the enacting legislature, previous administrative or judicial precedent, and traditional or customary norms. Rather, Scalia seeks "horizontal coherence," that is, consistency with the rest of the law today. *Id.* at 239.

> For Scalia, horizontal coherence in law is critically important because law should be an internally coherent system of rights and duties, but the only admissible evidence of it is statutory and constitutional text. Hence, the judge's job is to make the best sense she can of this hard objective stuff, and she is barred from introducing soft stuff (context) both because it is not law and (relatedly) because soft stuff tends to be a reflection of what she would like the law to be rather than what the law actually is.

Id. at 271. *See* William N. Eskridge, Jr., *The New Textualism*, 37 UCLA L. REV. 621, 655 (1990) [hereinafter, Eskridge, *The New Textualism*] ("But, unlike defenders of legislative history, Justice Scalia admits only arguments based upon textual, or horizontal, coherence (this meaning is consistent with other parts of the statute or other terms in similar statutes) . . . .").

[5] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 69–70 (noting that the Court in Williamson v. United States, 114 S. Ct. 2431 (1994), purported to find a clear policy statement in the text of Rule 804(b)(3)—where no such clarity existed—to resolve an ambiguity in the Rule. Although the majority did not end its analysis there, as a new textualist would have done, Justice Scalia presumably joined in the majority opinion, *see id.* at 73, partly because of its early new textualist rhetoric).

[6] *See infra* text accompanying notes 113–121, 138–142.

[7] *See infra* text accompanying notes 139–143.

[8] *See infra* text accompanying notes 108–112.

very public-regarding purpose, not simply the efforts of powerful rent-seeking groups. These realities, and the Rules' preferences for trial court discretion and growth in evidence law by the common law method, support a structured but more flexible interpretive method than plain meaning.

Part I sets the stage, however, for this more theoretical discussion by reviewing in detail the continuing debates among the Justices about proper interpretive method. These debates reveal a sharp and more express recent move by all the Justices but Justice Antonin Scalia—and even some movement by him as well—toward a politically realistic hermeneutics.

Part I of this Article will review the Court's two most recent evidence opinions, in part to update the position defended in the earlier companion piece. But this review serves a more important goal as well: to highlight for the reader the varying approaches to interpretation and the wisdom of a more flexible approach that will be defended at a more theoretical level in Part II. While Part II will draw primarily on the teachings of political science, economics, and literary theory, illustrative examples will be offered there to show how that theory operates in concrete cases. Many of those examples will, however, be drawn from earlier Supreme Court evidence case law, both to demonstrate further that the theory articulated here has always played at least an implicit role in the Court's analysis and to use particular earlier cases that offer the most effective illustration of certain points to be made in Part II.

In particular, Part I emphasizes the diminished role of statutory text for all the Justices, the differing degrees of confidence they have in their ability to divine actual legislative intent, and their differing attitudes toward trial judge discretion, growth in evidence law by the common law method, and interstitial judicial policymaking. The second of the two cases to be reviewed here, *United States v. Mezzanatto*,[9] will in particular stress the need for judicial candor and the impossibility of avoiding judicial lawmaking. The first case examined, however, *Tome v. United States*,[10] is most important because of the interpretive approach articulated by Justice Breyer on behalf of four dissenters that is very close to the politically realistic hermeneutics defended here.

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[9] 115 S. Ct. 797 (1995).
[10] 115 S. Ct. 696 (1995).

A. Tome v. United States

1. The Majority Opinion

In *Tome v. United States*,[11] the Court for the first time had the opportunity to interpret Rule 801(d)(1)(B) of the Federal Rules of Evidence, which reads as follows:

> (d) Statements which are not hearsay.—A statement is not hearsay if—
> (1) Prior statement by witness.—The declarant testifies at the trial or hearing and is subject to cross-examination concerning the statement, and the statement is . . .
> (B) consistent with the declarant's testimony and is offered to rebut an express or implied charge against the declarant of recent fabrication or improper influence or motive . . . .[12]

Tome had been charged with sexually abusing his four-year-old daughter. On cross-examination at trial, the defense suggested that the daughter had concocted these allegations while visiting with her divorced mother to avoid being returned to the father.

On rebuttal, the Government called six witnesses, recounting seven out-of-court statements made by the child about the abuse to her babysitter, a social worker, and three pediatricians. The trial court admitted these statements under Rule 801(d)(1)(B) as rebutting implicit charges that the child fabricated[13] her testimony.

On appeal, the Court of Appeals for the Tenth Circuit affirmed, rejecting the defense argument that only prior consistent statements made *before* the motive to lie arose should be admitted. Whether to admit the statements on rebuttal was a "function of the relevancy rules, not the hearsay rules."[14] But the relevancy rules did not bar post-motive statements "because it is simply not true that an individual with a motive to lie always will do so."[15]

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[11] *Id.*

[12] FED. R. EVID. 801(d)(1)(B).

[13] The trial court also admitted the statement to the babysitter under Rule 803(24)'s residual hearsay exception and the statements to two of the pediatricians under Rule 803(4), the medical diagnosis or treatment exception. But the only issue before the Supreme Court was the wisdom of admitting all these statements under Rule 801(d)(1)(B).

[14] 3 F.3d 342, 350 (10th Cir. 1993).

[15] *Id.*

The United States Supreme Court reversed, finding that Rule 801(d)(1)(B) "embodies . . . [the] temporal requirement."[16]

In reaching this conclusion, the Court relied on a wide variety of data sources, including text, common law history, the Advisory Committee's Notes, and sound policy.

a. *Text.* Rule 801(d)(1)(B) obviously did not "plainly" state that "only prior consistent statements made *before* the alleged motive to fabricate are admissible under this Rule." Nevertheless, the Court found that the Rule's language—including what was missing from that language—was key. Thus, the Rule did *not* give non-hearsay status to *all* prior consistent statements but only to those rebutting a charge of improper motive or recent fabrication. What would explain selecting out a single category of prior consistent statements for special treatment? The Court's answer was that pre-motive prior consistent statements are a "direct and forceful refutation"[17] of charges of recent fabrication. But prior consistent statements "carry little rebuttal force"[18] when most other types of impeachment, like a showing of bad character, are involved. To eliminate the pre-motive requirement would, therefore, ignore Congress's purpose to limit the exclusion only to a type of hearsay that had particular probative force. Indeed, had Congress meant to admit prior consistent statements more broadly, it could have said so, for example, by declaring that "a witness' prior consistent statements are admissible whenever relevant to assess the witness's truthfulness or accuracy."[19] That Congress did not say so made it clear to the Court that "the drafters of Rule 801(d)(1)(B) were relying upon the common-law temporal requirement."[20]

b. *Common law history and academic commentary.* Moreover, found the Court, the "peculiar language of the Rule bears close similarity to the language used in many of the common law cases that describe the premotive requirement."[21] Furthermore, leading commentators at the time the Rules were adopted

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[16] 115 S. Ct. at 700.
[17] *Id.* at 701.
[18] *Id.*
[19] *Id.* at 702.
[20] *Id.*
[21] 115 S. Ct. at 702.

described the premotive requirement categorically—without exception—viewing post-motive statements as simply irrelevant.

c. *Advisory Committee's Notes.* The Court also relied on the Advisory Committee Notes for two reasons. First, the "well-considered Notes" are a "useful guide in ascertaining the meaning of the Rules"[22] and, where Congress did not amend the Advisory Committee's draft, the "Committee's commentary is particularly relevant in determining the meaning of the document Congress enacted."[23]

Second, however, apart from the Committee Notes' value in discerning legislative intent, the "Notes are also a respected source of scholarly commentary"[24] by a committee led by a "distinguished commentator on the law of evidence" that "consulted and considered the views, criticisms, and suggestions of the academic community in preparing the Notes."[25]

While the Notes could thus be both persuasive commentary and a guide to legislative intent, however, the Note to Rule 801(d)(1)(B) was silent on the pre-motive requirement.[26] Nevertheless, the Court concluded that the Notes generally disclosed a purpose to adhere to the common law absent express provisions to the contrary, for when the Committee meant to change the common law, their Notes generally said so. Indeed, given the leading commentators of the time stating the pre-motive rule categorically (that is, without exception), the Court would not believe that "the drafters of the Rule intended to scuttle the whole premotive requirement and rationale without so much as a whisper of explanation."[27]

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[22] *Id.*

[23] *Id.*

[24] *Id.*

[25] *Id.*

[26] That Note read in its entirety as follows:

> Prior consistent statements traditionally have been admissible to rebut charges of recent fabrication or improper influence or motive but not as substantive evidence. Under the rule they are substantive evidence. The prior statement is consistent with the testimony given on the stand, and, if the opposite party wishes to open the door for its admission in evidence, no sound reason is apparent why it should not be received generally.

FED. R. EVID. 801 (d)(1)(B) advisory committee's note.

[27] 115 S. Ct. at 703. The Court also relied on subsequent legislative history, noting that Edward Cleary, the Reporter for the Advisory Committee, did not mention in his 1972 revision of McCormick's treatise that the then-proposed Rules worked any change in the common law pre-motive requirement. Again, the Court relied on Cleary's *silence* as suggesting that no change had been wrought in the Rules. *Id.*

d. *Discretion.* Before the Rules were adopted, academic commentators criticized the categorical exclusion of hearsay, favoring instead a case-by-case balancing of a hearsay statement's probative value against its prejudicial effect. However, the Court emphasized that the Notes revealed that "'[t]he Advisory Committee has rejected this approach to hearsay as involving too great a measure of judicial discretion, minimizing the predictability of rulings, [and] enhancing the difficulties of preparation for trial.'"[28] While, therefore, the Rules revealed a liberal approach to relevancy, they adopted, in the Court's view, a far less discretionary approach to hearsay.

Apart from the Advisory Committee Notes, however, the Court expressed its own independent distrust of the need for discretion, viewing "the parade of sympathetic and credible witnesses"[29] to the child's prior consistent statements in *Tome* as "shed[ding] but minimal light"[30] on whether she had a motive to fabricate. Moreover, while the Court conceded that it may be difficult to determine when a motive to fabricate arose, as the pre-motive rule requires, the Court viewed the case-by-case weighing of all the circumstances that a relevancy approach would require as imposing an even greater burden on trial judges, with even less guidance to attorneys.

Importantly, however, the Court recognized that trial judge discretion to admit post-motive statements still existed, but under the residual exceptions to the hearsay rule, not Rule 801(d)(1)(B). The Court would "intimate no view," however, regarding whether the statements at issue should have been admitted under the residual exception.[31]

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[28] *Id.* at 704 (quoting Fed. R. Evid. advisory committee's Introductory Note: The Hearsay Problem).

[29] *Id.* at 705.

[30] *Id.*

[31] Interestingly, the Court, while acknowledging the need to be "sensitive" to the difficulties of prosecuting child abusers, emphasized that it could not "'alter evidentiary rules merely because litigants might prefer different rules in a particular class of cases.'" *Id.* (quoting United States v. Salerno, 505 U.S. ____, 112 S. Ct. 2503, 2507 (1992)). On the one hand, this statement is a curious one, for the Court conceded that "sensitivity" was needed partly because of the great need for additional evidence beyond the child's testimony. But, at least in the relevancy area, need is recognized to be a valid part of the admissibility decision. *See* RONALD L. CARLSON ET AL., EVIDENCE IN THE NINETIES 314 (3d ed. 1991). By refusing to view the problem as involving discretionary relevancy and thus ignoring the state's great need for the evidence, the Court demonstrated some distrust, albeit not total distrust, of trial judge

2. Justice Scalia's Partial Concurrence

Justice Scalia concurred in the judgment and in all but Part II-B of the Court's opinion. Scalia's objection was to the Court's giving effect to the Advisory Committee Notes as displaying the "purpose" or "intent" of the drafters.[32] Given Scalia's earlier adherence to a plain meaning philosophy,[33] one might have expected him then to turn his attention to the language and structure of the Rules. Surprisingly, however, he instead turned to the Advisory Committee Notes, which mattered because:

> Having been prepared by a body of experts, the Notes are assuredly persuasive scholarly commentaries—ordinarily *the* most persuasive—concerning the meaning of the Rules. But they bear no special authoritativeness as the work of the draftsmen, any more than the views of Alexander Hamilton (a draftsman) bear more authority than the views of Thomas Jefferson (not a draftsman) with regard to the meaning of the Constitution.[34]

Scalia went on to argue, like a good textualist, that only the words of the Rule, not "thoughts, unpromulgated as Rules,"[35] were adopted, and the promulgated Rule "says what it says, regardless of the intent of its drafters."[36] Despite so paying homage to plain meaning, Scalia found that the "merely persuasive force of the Advisory Committee Notes suffices."[37]

But, Scalia went on, the case could also be adequately resolved without the Advisory Committee Notes because it was

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discretion. *See infra* text accompanying notes 348–366 for a more detailed discussion of this point.

On the other hand, the Court's comments can be viewed in a more positive light: the Rules were written in general terms, to apply to many new and unforeseen circumstances, and, because of their generality, were likely not and should not be the result of the domination of interest groups seeking future benefits, for such benefits could not accurately be predicted. To carve out special treatment for any group would compromise this political neutrality. *See infra* text accompanying notes 202–231 (discussing importance of Rules' generality).

[32] 115 S. Ct. at 706.

[33] *See infra* notes 134–136 and accompanying text.

[34] 115 S. Ct. at 706.

[35] *Id.* His subjective view of group "intent" as the sum of individual motivations was made even clearer when he continued: "In my view even the adopting Justices' thoughts, unpromulgated as Rules, have no authoritative (as opposed to persuasive) effect, any more than their thoughts regarding an opinion (reflected in exchanges of memoranda before the opinion issues) authoritatively demonstrate the meaning of that opinion." *Id.* As we will see, a more defensible conception of group intent than Justice Scalia's is possible. *See infra* text accompanying notes 243–260.

[36] 115 S. Ct. at 706.

[37] *Id.*

"well established" that the "'body of common law knowledge' must be 'a source of guidance' in our interpretation of the Rules."[38] Because Rule 801(d)(1)(B) tracks common law cases and prescribes a result that makes no sense without the assumption that the common law rule applied, the common law controlled.[39]

Moreover, "only the premotive-statement limitation *makes it rational* to admit a prior corroborating statement to rebut a charge of recent fabrication or improper motive, but not to rebut a charge that the witness' memory is playing tricks."[40] Advisory Committee Notes, common law practice, attributed rational legislative purposes, but *not* ordinary meaning[41] as revealed by the dictionary, were the tools in Justice Scalia's interpretive kit.

3. Justice Breyer's Dissent

Justice Breyer, joined by Chief Justice Rehnquist and Justices O'Connor and Thomas, dissented, relying, as did the majority, on a variety of interpretive sources, but with a different reading of those sources and a greater willingness to trust trial judge discretion.

a. *Text as a guide to rational legislative purposes.* Justice Breyer rejected the majority's argument that the only rational reason for treating prior consistent statements offered to rebut charges of improper motive or recent fabrication differently from other types of prior consistent statements was that the former had special probative force.[42] Thus, he noted, even McCormick, upon whom the majority had relied, recognized that at least one

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[38] *Id.*

[39] Justice Scalia's reference to the common law is arguably consistent with his earlier approval in Green v. Bock Laundry Mach. Co., 490 U.S. 504 (1989), of the "benign fiction" that Congress intended the rules to be most compatible with the "surrounding body of law." *Id.* at 528. If, however, the "surrounding body of law" is no longer limited to the purportedly plain text of the Rules or similar statutes, and indeed includes the common law, and if meaning may be guided by the Advisory Committee Notes, it is hard to see how Justice Scalia can continue to describe his revised views in *Tome* as textualist ones, despite his protestations to the contrary. *See* 115 S. Ct. at 706.

[40] *Id.* (emphasis added).

[41] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 30 (discussing Justice Scalia's long commitment to "ordinary usage").

[42] Justice Breyer identified at least four types of prior consistent statements used to rehabilitate, specifically those: (1) placing an apparently inconsistent statement in context so that it no longer seems inconsistent; (2) showing that the claimed inconsistent statement was never made; (3) demonstrating that the witness' memory is not as poor as the cross-examiner claims; and (4) showing that the witness did not recently

other type of prior consistent statement had significant probative force: "'[i]f the witness's accuracy of memory is challenged, it seems *clear common sense* that a consistent statement made shortly after the event and before he had time to forget, should be received in support.'"[43]

More important to Justice Breyer, however, was that Congress's goal could not have been to assure admissibility of statements with special probative force because "probative force has little to do with the concerns underlying hearsay law."[44] Hearsay is concerned not with probative force but with "an out-of-court declarant's reliability, as tested through cross-examination."[45] Thus, a post-motive prior consistent statement may have diminished probative force, but the statement's "reliability"—its ability fairly to be evaluated by the jury for the witness's ability to observe, remember, communicate, and tell the truth—is neither more nor less than the reliability of a pre-motive statement.

On the other hand, noted Justice Breyer, there is a rational hearsay-related (as opposed to relevancy-related) explanation for Rule 801(d)(1)(B). Juries have trouble distinguishing between the rehabilitative and substantive use of one kind of prior consistent statement: those offered to rebut a charge of improper motive or recent fabrication. Before Rule 801(d)(1)(B), such statements were admissible to rehabilitate but not for their substance, that is, not for the truth of what they asserted. While limiting instructions to prevent substantive use were given, juries tended to ignore those instructions. "It is possible," therefore, concluded Justice Breyer, that the "Advisory Committee made them [prior consistent statements] 'non-hearsay' for that reason, i.e., as a concession 'more of experience than of logic.'"[46] "*If* there was a reason why the drafters excluded from Rule 801(d)(1)(B)'s

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fabricate his testimony as a result of an improper influence or motive. 115 S. Ct. at 706.

[43] *Id.* (quoting MCCORMICK ON EVIDENCE § 49, at 105 n.88 (emphasis added by Justice Breyer)).

[44] *Id.* The Advisory Committee agreed: "The only way in which the probative force of hearsay differs from the probative force of other testimony is in the absence of oath, demeanor, and cross-examination as aids in determining credibility." Advisory Committee's Introductory Note: The Hearsay Problem. Consequently, concluded the Advisory Committee, for a trial judge to exclude hearsay purportedly for its low probative force would involve the court in credibility judgments. "For a judge to exclude evidence because he does not believe it has been described as 'altogether atypical, extraordinary . . . .'" *Id.* (quoting Chadbourn, *Bentham and the Hearsay Rule—A Benthamic View of Rule 63(4)(c) of the Uniform Rules of Evidence*, 75 HARV. L. REV. 932, 947 (1962)).

[45] *Id.*

[46] *Id.*

scope other kinds of prior consistent statements (used for rehabilitation), *perhaps* it was that the drafters concluded that those other statements caused jury confusion to a lesser degree."[47] But, noted Justice Breyer, on this rationale there is no basis for distinguishing between *pre-* and *post*-motive statements.

b. *"Plain" meaning.* There was, of course, a plain meaning argument that the "words . . . mean exactly what they say":[48] *if* a trial court admits a consistent statement to rebut an "express or implied charge . . . of recent fabrication or improper influence or motive," then that statement is not hearsay and may be considered for the truth of what the statement says. But the Rule does *not* say when a trial court should admit a prior consistent statement for rehabilitative purposes, and nowhere does the Rule mention a "premotive requirement." Consequently, general principles of logical and legal relevancy should be the only limitations on the admissibility of prior consistent statements.

Justice Breyer indeed crafted precisely this argument based on the Rule's "plain words." But he did not argue, as would a textualist, that the words had some self-evident, inherent meaning,[49] nor did he argue that "plain meaning" should always control. Rather, he argued that "*because* the Rule addresses a hearsay problem and one can find a reason, unrelated to the premotive rule, for why it does so, I would read the Rule's plain words to mean exactly what they say . . . ."[50]

c. *Common law.* Having concluded that the hearsay rules did not bar the prior consistent statement at issue, the question for Justice Breyer was then whether the relevancy rules did so by imposing a pre-motive requirement. Justice Breyer agreed

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[47] *Id.* (emphasis added).

[48] *Id.*

[49] Some textualists are aware that context, not simply a dictionary, is sometimes necessary to give words meaning. *See* ESKRIDGE, DYNAMIC INTERPRETATION, *supra* note 3, at 226 ("Scalia is aware of the familiar precepts that words do not interpret themselves . . . ."). But they generally view the relevant context as other text in the same or similar statutes, assuming that the words read as a whole, and aided by a dictionary, will reveal a "plain" meaning. They therefore ignore the roles of the reader and the policy-driven choice of interpretive communities as inevitable aspects of the process by which we give words meaning. *See infra* text accompanying notes 129–133, 144–196. It is in this sense that textualists view words as having "self-evident, inherent" meanings.

[50] 115 S. Ct. at 708.

that the common law was relevant to answering this question, but he found that the common law did not control here.

First, the common law premotive rule was not as uniform as the majority suggested. To the contrary, a minority of courts recognized that post-motive statements could be relevant to a charge of recent fabrication.

Second, Justice Breyer relied heavily on *Daubert v. Merrell Dow Pharmaceuticals, Inc.*,[51] in which the Court rejected the rigid common law *Frye* rule—excluding novel scientific evidence that was not generally accepted—in favor of a more flexible test of the "relevancy and reliability of the scientific evidence."[52] Justice Breyer saw *Daubert* as recognizing that the Rules "worked a change in common-law relevancy rules in the direction of flexibility."[53] Moreover,

> *Daubert* suggests that the liberalized relevancy provisions of the Federal Rules can supersede a pre-existing rule of relevance, at least where no compelling practical or logical support can be found for the pre-existing rule. It is difficult to find any strong practical or logical considerations for making the premotive rule an absolute condition of admissibility here.[54]

Third, given the Rules' liberal approach to relevancy, the drafters surely would have made it clear had they meant to insulate the common law premotive rule from the Rules' liberalizing effect. The language of Rule 801(d)(1)(B) "would have been a remarkably indirect (and therefore odd) way of doing so—both because Rule 801(d)(1)(B) is utterly silent about the premotive rule and because Rule 801(d)(1)(B) is a rule of hearsay, not relevancy."[55] Moreover, assuming that the drafters meant by this rather odd device to continue the common law seems particularly absurd given that there is an "equally plausible"[56] reason to write the Rule the way they did: to allow substantive use of a category of prior consistent statements that was especially impervious to a limiting instruction.

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[51] 113 S. Ct. 2786 (1993).

[52] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 44–50 (discussing *Daubert's* holding and reasoning).

[53] 115 S. Ct. at 709 (Breyer, J., dissenting).

[54] *Id.* He noted, however, "Perhaps there are other circumstances in which categorical common-law rules serve the purposes of Rules 401, 402, and 403 and should, accordingly, remain absolute in the law. But . . . this case, like *Daubert*, does not present such a circumstance." *Id.*

[55] *Id.*

[56] *Id.*

d. *Discretion.* In emphasizing the Rules' strong movement toward greater "flexibility" in relevancy rules, Justice Breyer made clear that he meant that the Rules vested substantial discretion in the trial judge: "The codification, as a general matter, relies upon the trial judge's administration of Rules 401, 402, and 403 to keep the barely relevant, the time wasting, and the prejudicial from the jury."[57]

While Justice Breyer conceded that an absolute, category-bound rule like the premotive rule might be easier to administer, he found "no indication in any of the cases that trial judges would, or do, find it particularly difficult to administer a more flexible rule in this context."[58] Moreover, greater flexibility would enable the trial judge "to tie rulings on the admissibility of rehabilitative evidence more closely to the needs and circumstances of the particular case."[59] Consequently, Justice Breyer saw no need to reevaluate the trial judge's "factbound conclusion."[60]

e. *Policy.* Justice Breyer additionally rejected the claim that, as a matter of simple logic, post-motive statements could never be relevant. To the contrary, under particular circumstances a motive to lie may be outweighed by a far more powerful motive to tell the truth, as where a speaker may want to lie to help an acquaintance but realizes that only the truth will save the speaker's child's life. Thus a prior statement "may have been made not *because of*, but *despite*, the improper motivation."[61] Moreover, allowing greater flexibility will usually yield the same result as the premotive rule, for most post-motive statements will not be significantly probative, and the prejudicial impact will be slight because "the prior consistent statements will (by their nature) do no more than repeat in-court testimony."[62]

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[57] *Id.* at 709.

[58] *Id.* at 708.

[59] *Id.* at 709. *See also infra* text accompanying notes 351–359 (arguing rules reflect a preference for individualized justice).

[60] 115 S. Ct. at 710 (Breyer, J., dissenting).

[61] *Id.* at 708.

[62] *Id.* at 710. *Tome* is the second major Rules' opinion in which the prosecution lost. I argued in the companion piece that many of the Court's Rules' opinions were consistent with a pro-prosecution bias. Taslitz, Daubert*'s Guide, supra* note 1, at 16. I argued further, however, that the first opinion in which the prosecution lost, Williamson v. United States, 114 S. Ct. 2431 (1994), demonstrated first, that the Court's arguable bias was not so extreme as to lead it to implausible interpretations, and, second, that, properly understood, *Williamson* was still consistent with a pro-prosecution bias.

4. Interpretive Significance

The most important interpretive lesson of *Tome* is that almost all the Justices joined in an opinion that self-consciously departed from a plain meaning jurisprudence. Indeed, eight of the nine Justices—all but Justice Scalia—relied on an interpretive approach that engaged in a flexible weighing of a wide array of data—text, Advisory Committee Notes, common law, evidence scholarship, the structure of the Rules, and sound policy.

Even Justice Scalia at least implicitly moved closer to a more flexible methodology. Thus he has previously described his textualism as requiring that words be given their "ordinary" meanings.[63] Yet here the supposedly "ordinary reader" was someone knowledgeable about the common law, the Advisory Committee Notes, and underlying policies. Scalia has obviously replaced the "ordinary" reader with a specialized interpretive community, a policy-driven choice that ultimately required the weighing of extratextual data while ignoring the more traditional textual arguments, arguments briefly reviewed by Justice Breyer.[64] Moreover, Justice Scalia effectively inquired into what a rational legislature would have intended to achieve by Rule 801(d)(1)(B), despite his denying that that was what he was doing.[65] This is not textualism.

Tome is also important, however, because of the differences among the remaining Justices, all of whom admitted to a more flexible approach than Scalia. Specifically, the majority and dis-

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Taslitz, Daubert*'s Guide*, *supra* note 1, at 73–74. Moreover, the Court's other 1995 opinion, *United States v. Mezzanatto*, garnered seven votes for an opinion openly admiring of prosecutors. *See infra* text accompanying notes 84–90. It is hard to tell, however, whether *Tome* fits the pro-prosecution pattern. A rule prohibiting post-motive consistent statements hurt the prosecution in *Tome*, but there is no evidence that the rule will benefit either the defense or the prosecution disproportionately in future cases, for either side can at any time find itself in need of rehabilitating its witnesses. On the other hand, a more discretionary rule like that proposed by Justice Breyer would at least have left open the possibility that a law-and-order trial judiciary would exercise its discretion in favor of the prosecution in close cases, yet the majority rejected such an approach. Furthermore, Justice Souter's dissenting opinion in *Mezzanatto* reflected, if anything, some distrust of the prosecution, *see infra* text accompanying notes 96–104, and Justice Ginsburg's concurring opinion in *Williamson*, joined by Justices Souter, Stevens, and Blackmun, argued for a clearly pro-defense result. *See* Taslitz, *supra* note 1, at 71, n.374. Four Justices have thus demonstrated at least occasional sympathy for pro-defense positions.

[63] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 30.

[64] *See supra* text accompanying notes 48–50 (discussing Breyer's "plain words" analysis and why it ultimately was not a textualist theory).

[65] *See supra* text accompanying notes 40–41 (Scalia's analysis of what a *rational* Congress would have done).

sent differed in three ways. First, the majority suggested that the Court had divined the actual intent of the Congress regarding the pre-motive rule.[66] In fact, however, the silence of both Rule 801(d)(1)(B) and its legislative history about the pre-motive requirement suggests that Congress never even considered the question. Moreover, the argument that Congress must, therefore, have simply assumed that the pre-motive rule would continue to apply is precisely the type of argument that the Court recently rejected in *Daubert*. There, from the expert evidence Rules' and Advisory Committee Notes' silence about the common law *Frye* rule, the Court concluded that the Rules' general relevancy approach, not the rigid common law rule, was meant to apply,[67] precisely the type of conclusion the majority rejected in *Tome*. Professor Giannelli's careful examination of the history of the expert evidence Rules has indeed established that the Rules were silent about *Frye* because the issue was ignored.[68] That is indeed the most realistic way to read Rule 801(d)(1)(B)'s silence about the pre-motive Rule.

Breyer's dissent, on the other hand, was more candid, recognizing that there was no actual intent—just silence—and therefore focusing on text, rational purposes, the general structure and philosophy of the Rules, and sound policy. While the majority focused on these things as well, they viewed them in the very different light shed by a presumed actual legislative intent that simply did not exist.

Second, as discussed earlier, the majority and dissent had very different attitudes toward discretion. While both thought it necessary to categorize the pre-motive issue as one of relevancy for the trial judge to have discretion, Justice Breyer seemed to believe that the Rules expressed a wise preference for discretion; he therefore sought to categorize the issue as one of relevancy. Breyer could have gone even further, however, for the majority was simply wrong to see the hearsay rules as uniformly non-discretionary (at least outside of the residual exception). To the contrary, many of the supposedly "categorical" hearsay exceptions—for example, business records,[69] public records,[70] and dec-

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[66] *See supra* text accompanying notes 17–27 (describing majority's analysis, which often suggested that Congress had actually considered the question before the Court).

[67] *See* Taslitz, Daubert*'s Guide, supra* note 1, at 45–50.

[68] Paul C. Giannelli, Daubert*: Interpreting the Federal Rules of Evidence*, 15 CARDOZO L. REV. 1999, 2016–17 (1994).

[69] FED. R. EVID. 803(6).

[70] FED. R. EVID. 804(8).

larations against interest[71]—in fact accord much discretion to the trial judge.[72] This Article will demonstrate that, while not all the Rules are discretionary, ambiguous Rules should be read as discretionary ones, reflecting the Rules' philosophical preference for individualized justice.[73]

Third, the majority and Justice Breyer had different views of the role of the common law under the Rules. The majority's view was binary: either a Rule adopted or rejected a common law rule. But Justice Breyer saw the common law simply as a source of guidance, its history and policies to be weighed against the text, structure, and policies of the Rule. Moreover, Justice Breyer seemed to see a link between trial judge discretion and change in the common law. The trial judge crafts new approaches to meet new situations. Yet his discretion is not unlimited.

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[71] FED. R. EVID. 804(b)(3); Taslitz, Daubert*'s Guide*, *supra* note 1, at 68–75 (explaining discretionary nature of the Rule).

[72] *See* Williamson v. United States, 114 S. Ct. 2431 (1994) and Tome v. United States, 115 S. Ct. 696 (1995). Interestingly, counting the votes in the two evidence cases in which discretion was expressly discussed after the first of the two Clinton appointees joined the Court reveals that the Justices' views on discretion fall into three groups: Ginsburg, Stevens, Souter (relatively distrustful of discretion); O'Connor, Rehnquist, Thomas, Breyer (trustful of discretion); and Kennedy, Scalia (inconsistent attitudes toward discretion, e.g., willing to trust discretion in *Williamson* but not in *Tome*.) *Compare* Taslitz, Daubert*'s Guide*, *supra* note 1, at 68–75 (comparing Justices' views on discretion in *Williamson*) *with supra* text accompanying notes 28–31 (similar discussion regarding *Tome*). This is, of course, a limited sample, and it ignores comments in earlier cases that may alter the picture slightly. For example, Justice Rehnquist's dissent in *Daubert* praised trial judges and stressed the need for their involvement in the case-by-case growth of rules governing scientific evidence, yet expressed fear about trial judge abilities to understand such evidence. *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 50–52. His views in *Daubert* are, therefore, either internally inconsistent or suggest he is more trustful of discretion in some contexts than others, perhaps requiring that he be shifted into the Kennedy, Scalia group. Moreover, Justice Ginsburg, in a case to be discussed shortly, United States v. Mezzanatto, 115 S. Ct. 797 (1995), joined in an opinion implicitly approving of some limited discretion involved in certain preliminary fact finding. *See infra* text accompanying note 107. Nevertheless, the *Williamson/Tome* comparison may give us at least a fuzzy snapshot of where the present lineup of Justices stands.

[73] *See infra* text accompanying notes 348–366. Some important caveats are necessary. Some rules establish per se, not discretionary standards. For example, Rule 608 flatly bars extrinsic evidence of specific instances of a witness's untruthful conduct. FED. R. EVID. 608(b). *See also* David P. Leonard, *Appellate Review of Evidentiary Rulings*, 70 N.C. L. REV. 1155, 1192 (1992). Such standards should be reviewed de novo on appeal. *Id.* at 1192. Moreover, that a Rule is discretionary should not mean automatic approval on appeal. To the contrary, "abuse of discretion" requires more or less deference to the trial judge, depending on the context, and should often involve the appellate court in a relatively careful examination of the trial judge's reasons and whether he considered and weighed them consistently with the purposes of the Rules. *See id.* at 1192–93, 1198–1211. Justices Breyer's otherwise well-reasoned opinion in *Tome* was thus flawed when it jumped from concluding that the admissibility decision was a discretionary one to the conclusion—without stating his reasons—that there was no reason to reevaluate the trial judge's "factbound" decision. *See* 115 S. Ct. at 710.

For example, following common law experience, Breyer recognized that most post-motive statements will not be significantly probative, suggesting that admission of many such statements could lead to reversal.[74] Therefore, drawing on the common law as a helpful resource, trial judge experimentation leads to new rules, modified by appellate precedent, thus permitting growth in evidence law.[75]

Breyer's recognition of the dynamic nature of the Rules and the continuing creative policymaking role of the courts was highlighted further in *United States v. Mezzanatto*, in which the Court, in a fascinating turn, found a laissez-faire, non-interventionist philosophy in the "market" for admissible evidence embodied in the Rules.

B. United States v. Mezzanatto

1. Majority Opinion

In *United States v. Mezzanatto*,[76] a defendant charged with possessing methamphetamine with intent to distribute sought to negotiate a plea with the prosecutor. The prosecutor agreed to do so only if the defendant first agreed—which he did—that any statements he made during the negotiation could be used to impeach him should the case go to trial. During the negotiations, however, the defendant sought to shift primary responsibility to another individual, a Mr. Shuster. The prosecutor thus cut short the negotiations, believing the defendant had lied. At trial, the prosecutor, over defense objection, impeached the defendant with the prior inconsistent statements that he had made during the plea bargaining. The jury convicted him, and he appealed, arguing that he was impeached in violation of Rule 410 of the Federal Rules of Evidence.

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[74] *See* 115 S. Ct. at 710.

[75] The Advisory Committee similarly noted that its use of specific hearsay exceptions, followed by more general residual exceptions, constituted a "plan . . . calculated to encourage growth and development in this area of law, while conserving the values and experience of the past as a guide to the future." Advisory Committee's Introductory Note: The Hearsay Problem. While the majority, had it adverted to this comment, might have characterized it as permitting growth only via the residual exceptions, the comment in fact referred to the "plan" as consisting of both the residual and specific exceptions read together. Moreover, such a narrow, inflexible reading is inconsistent with the Rules' sound design. *See infra* text accompanying notes 348–366.

[76] 115 S. Ct. 797 (1995).

Rule 410 (and the substantially identical Rule 11(e)(6) of the Federal Rules of Criminal Procedure) declares that "any statement made in the course of plea discussions with an attorney for the prosecuting authority which do not result in a plea of guilty" is "not, in any . . . criminal proceeding, admissible against the defendant."[77] The Ninth Circuit reversed the defendant's conviction, holding that, because neither Rule 410 nor its two narrowly drafted exceptions said anything about waiver, Congress must have meant to preclude it.

The United States Supreme Court, however, reversed the Ninth Circuit, reinstating the conviction.

a. *The sounds of silence.* The Court conceded the Rule's silence about waiver. However, the Court had long recognized a presumption of waivability in a broad array of constitutional and statutory provisions, absent a clear statement that Congress meant to preclude such waiver. Moreover, the practice of trial parties, routinely honored by trial judges, is to exchange stipulations—including waivers—for tactical purposes. Thus, the Rules were enacted against a "background presumption that . . . evidentiary provisions specifically, are subject to waiver by voluntary agreement of the parties."[78] The Court refused, therefore, to "interpret Congress' silence as an implicit rejection of waivability."[79]

b. *Truth as a value.* The Court agreed, however, that there may be some evidentiary provisions "so fundamental to the reliability of the fact-finding process that they may never be waived without irreparably 'discrediting the federal courts.'"[80] Whether the basis for this position was the Constitution, the inherent power of the courts, or an assumption that Congress would not then intend waiver was unclear. What the Court did make clear, however, was that it did not face such a case, for the waiver agreements here would enhance truth-seeking by revealing lies and inconsistencies, "without risking institutional harm to the federal courts."[81]

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[77] FED. R. EVID. 410. *See also* FED. R. CRIM. P. 11(e)(6) (substantially identical).
[78] 115 S. Ct. at 803.
[79] *Id.*
[80] *Id.* (quoting 21 CHARLES A. WRIGHT & KENNETH A. GRAHAM, FEDERAL PRACTICE AND PROCEDURE § 5309, at 207–08 (1977)).
[81] *Id.*

c. *Text.* The Court further noted that the Rule's text provided that statements made in the course of plea discussions are inadmissible "against" the defendant, leaving open the possibility of his offering such statements in his favor. Similarly, a Rule 410 exception admits plea negotiation statements that "ought in fairness be considered contemporaneously" with other statements made in the course of the same plea discussion and already admitted.[82] Again, this suggests a party could choose to seek admission if tactically advantageous; the Rules' language thus "contemplates a degree of party control that is consonant with the background presumption of waivability."[83] Moreover, citing a scholarly treatise, the Court described Rule 410 as creating a privilege, and privileges can be waived. The implication was that an informed reader, aware of Rule 410's nature as a privilege, would read the Rule's language with the understanding that it created a measure of party control.

d. *The free market and congressional purpose.* The Court rejected the defendant's claim that waiver would defeat the congressional goal of encouraging plea bargaining. Because of the great need for prosecutors to secure accurate information about the credibility of testimony before they can make critical judgments early in a case about whom to pursue, or to grant immunity or leniency, noted the Court, a prosecutor might prefer to decline cooperation discussions absent the incentive for truthfulness created by a waiver agreement:

> To use the Ninth Circuit's metaphor, if the prosecutor is interested in "buying" the reliability assurance that accompanies a waiver agreement, then precluding waiver can only stifle the market for plea bargains. A defendant can "maximize" what he has to "sell" only if he is permitted to offer what the prosecutor is most interested in buying. And while it is certainly true that prosecutors often need help from the small fish in a conspiracy in order to catch the big ones, that is no reason to preclude waiver altogether. If prosecutors decide that certain crucial information will be gained only by preserving the inadmissibility of plea statements, they will agree to leave intact the exclusionary provisions of the plea-statement Rules.[84]

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[82] FED. R. EVID. 410.
[83] 115 S. Ct. at 804.
[84] *Id.* at 805.

Indeed, the Court noted, the empirical evidence was that the "market for plea bargains" was unharmed by waiver agreements. Thus, prior to the Ninth Circuit's decision in this case, federal prosecutors in the Circuit had used similar waiver agreements, achieving 92.2% of convictions in the Circuit by pleas, compared to an 88.8% plea rate in all federal courts. The defense apparently had the burden—which it did not meet—of identifying contrary empirical data.[85]

The majority rejected as well the argument that government guilty plea market intervention was justified by "'gross disparity'" in the "relative bargaining power"[86] of the parties. The defendant's dilemma—cooperate to get sentencing guidelines leniency but risk impeachment if no agreement is reached—was similar to the "number of difficult choices that criminal defendants face every day."[87] Moreover, the "mere potential for abuse" was insufficient since "'tradition and experience justify our belief that the majority of prosecutors will be faithful to their duty.'"[88] Indeed, the only waiver agreements that need be invalidated are those that are the "product of fraud or coercion,"[89] language reminiscent of contract rescission but that the Court equated with an "unknowing" or "involuntary" waiver,[90] a claim Mezzanatto had not made.

2. Souter's Dissent

Justice Souter, joined by Justice Stevens, dissented, purportedly on grounds of plain meaning, congressional intent to maxi-

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[85] There are, of course, many questions raised by the Court's purported use of empirical evidence. For example, what percentage of all plea negotiations involved impeachment waiver agreements, and over what period of time? If, let us say, only five percent of all negotiations involved waiver demands, an experiment that had been tracked for only a few months, that minimal intervention would be unlikely to reduce plea rates. But the Court considered the little data before it as sufficient to shift the burden of contrary evidence to the defense.

[86] 115 S. Ct. at 805.

[87] *Id.*

[88] *Id.* (quoting Corbitt v. New Jersey, 439 U.S. 212 (1978)).

[89] *Id.* at 805.

[90] Justice Ginsburg filed a concurring opinion, joined by Justices O'Connor and Breyer, stressing the central importance of Congress's efficiency goals. Thus Justice Ginsburg speculated that it "may be" that extending waivers so that prosecutors can use prior consistent statements as substantive evidence in their case-in-chief "would more severely undermine a defendant's incentive to negotiate, and thereby inhibit plea bargaining." *Id.* Consequently, Ginsburg stressed that the Court did not face and did not explore that very different situation. *Id.*

mize settlements, and very different notions from the majority about evidence market intervention.

a. *Plain meaning.* Justice Souter described Rule 410's text as "unconditional . . . unsoftened by any provision for waiver or allusion to that possibility . . . ."[91] Consequently, he concluded, "[b]elievers in plain meaning might be excused for thinking that the text answers the question."[92] However, "history may have something to say about what is plain, and here history is not silent."[93] Moreover, he conceded that rules that create personal rights are waivable. That Rule 410 created such a personal right was plausible, given that other evidence rules, notably hearsay and best evidence, are "equally uncompromising on their face but nonetheless waivable beyond any question."[94] Moreover, he conceded further that there is a presumption in favor of waiver and that "were [there] nothing more to go on here,"[95] he would have joined the majority, despite the Rule's contrary language. However, he read the Advisory Committee Notes to express unequivocally the intent of Congress to prohibit waiver.

b. *"Intent," efficiency, and the slippery slope.* Justice Souter emphasized that the central fact underlying the Advisory Committee Notes was that "the federal judicial system could not possibly litigate every civil and criminal case filed in the courts."[96] Consequently the Advisory Committee Note to Rule 410 declared its purpose to be the "promotion of disposition of criminal cases by compromise."[97] To do so, said the Committee, required "free communication,"[98] what the Advisory Committee Notes to identical Federal Rule of Criminal Procedure 11(e)(6) called "unrestrained candor."[99] These Notes meant that Congress "probably" assumed that such candor was the best way to encourage pleas, viewing Rule 410 not as a personal right benefitting the defendant but rather as a public right to efficiency, benefitting the courts. Furthermore, Congress "must have" un-

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[91] *Id.*
[92] *Id.* at 806.
[93] *Id.* at 807.
[94] *Id.*
[95] *Id.*
[96] *Id.* at 807.
[97] FED. R. EVID. 410 advisory committee's note.
[98] *Id.*
[99] FED. R. CRIM. P. 11(e)(6) advisory committee's note.

derstood that waivers will diminish the "zone of unrestrained candor"[100] because a defendant must pause to think whether the guilty plea negotiations are worth the risk.

Justice Souter rejected too the majority's presumed free market philosophy. Congress, he suggested, sought market intervention instead to promote more pleas than would the free market: "There is, indeed, no indication that Congress intended merely a regime of such limited openness as might happen to survive market forces sufficient to supplant a default rule of inadmissibility."[101] He rejected as well the limited empirical evidence that candor was unnecessary, concluding simply that the judiciary could not substitute its own choice of method for Congress's.

Souter was also, apart from congressional intent (though he would not admit this), distrustful of the fairness of unregulated markets, viewing waiver demands as "contracts of adhesion."[102] Indeed, he noted, standard forms indicate that many federal prosecutors already routinely require Rule 410 impeachment waivers. But, since the Rule makes no distinction between use for impeachment and for substance, he argued, permitting the former will encourage routine demands for the latter. Because admissions of guilt during plea negotiations will then be available in the prosecutor's case-in-chief, the prospect of a trial if no agreement is reached becomes a mere "fantasy." Defendants will have no admissibility protection "beyond what the Constitution may independently impose or the traffic may bear."[103]

These concerns about contracts of adhesion and derision of market choice thus embody notions of fairness and equalized resources between defendants and the state, a far cry from the truth-finding emphasized by the majority or the efficiency that Souter himself had identified as Congress's only goal. Souter does briefly suggest, however, that once we slide down the slippery slope to free waiver for *all* Rule 410 uses, the dangers of negotiating will be so high, and the likelihood of benefits so low, that plea bargaining will stop.[104] This suggestion ties at least part

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[100] 115 S. Ct. at 807. Justice Souter's notion of "candor" was, of course, an odd one. Is it really plausible to believe that Congress meant to encourage pleas based on lies, lies that might falsely implicate an innocent person in crime, or at least shift responsibility from the real ringleader to a less culpable party? Yet this was arguably the kind of "candor" at issue in *Mezzanatto*.

[101] *Id.* at 808.

[102] *Id.*.

[103] *Id.* at 809.

[104] *See id.* at 808.

of his argument back to efficiency, for, if he is right, the majority's empirical evidence is meaningless, a poor predictor of what the future will bring.

c. *Interpretive implications.* Despite Justice Souter's dabbling in plain meaning rhetoric, the discussion above demonstrates that neither he nor any other Justice in *Mezzanatto* signed onto an opinion adopting the new textualism. The most important difference between the majority and dissenting opinions, however, was that Justice Souter insisted that he had discovered with great confidence Congress's actual intent on the waiver question. The majority came closer to recognizing that Congress had no actual intent, had indeed never even thought about the question, and silence was, in any event, certainly skimpy evidence from which the majority could derive confident conclusions. Instead, the majority apparently tried to imagine what the enacting Congress would have done had it thought about the issue, looking to precedent, history, and the longstanding presumption of waivability to make that judgment. Indeed, Justice Souter conceded that historical inquiry supported the majority's conclusion. But, he insisted, on very little evidence, that no such exercise in imaginative reconstruction was necessary because the Advisory Committee Notes had answered the question.

But the majority properly recognized that the Notes—which the majority apparently agreed reflected congressional intent—never once mentioned waiver. Rather, the Notes did little more than provide policy justifications for the Rule.[105] What the majority seemed to recognize, and Souter claimed to but in fact did not, is that a central question was whether waiver would or would not serve those policy goals. While Souter indirectly suggested that the majority's rule would not serve those goals, he repeatedly insisted that Congress had already chosen the means—a flat, nonwaivable rule—to its ends, so the Court could not act. But he had no evidence whatsoever to support that claim.

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> We cannot agree with the dissent's conclusion that the policies expressed in the Advisory Committee Notes to the plea-statement Rules indicate congressional animosity toward waivability. The Advisory Committee Notes always provide some policy justification for the exclusionary provisions in the rules, yet those policies merely justify the default rule of exclusion; they do not mean that the parties can never waive the default rule.

Id. at n.5.

Indeed, while insisting he had discovered a clear legislative intent against waiver, and fulminating against the majority's usurpation of that intent, he nevertheless hedged his arguments with descriptions of what Congress "probably" intended or "must have intended," descriptions that sound more like exercises in imaginative reconstruction or the identification of what a rational legislature would have done than a discovery of this legislature's actual intent.

That there was substantial interstitial and unavoidable judicial policymaking going on was something else that Souter denied, yet, as we have seen, both he and the majority focused on notions of fairness, the basic assumptions of any rational system of evidence law (laissez-faire or interventionist), and the empirical/psychological question of what means will best achieve Congress's ends. The majority seemed a bit more candid at points, for example, in discussing its duty to ensure a sufficiently reliable trial process to avoid "'discrediting the federal courts.'"[106] But the Court's candor lagged when it suggested that the Rules' contemplation of party control entailed a fully developed laissez-faire free market theory of evidence. The majority apparently assumed that market outcomes were by definition good outcomes, certainly efficient and arguably fair, and that prosecutors were presumptively trustworthy. These assumptions cannot, however, fairly be located from the available data in any workable notion of "intent," at least from the minimal evidence of intent before the Court. Some market theory was, of course, probably necessary to resolve the ambiguous pulls of the various interpretive sources—text, legislative history, and limited empirical data—because the problem at issue, "waiver," by definition involved a bargained-for market exchange. But whether that theory should be laissez-faire (the majority) or interventionist (Souter), and how to weigh the values of truth-seeking, equality, and fairness in crafting this theory, could only be resolved by the courts within the broad limits set by Congress. This Article will indeed argue that such interstitial policymaking is part of the Rules' sound design.

Finally, while not expressly addressed by any of the Justices, the majority and dissenting opinions reflected different attitudes toward judicial discretion. The dissent's "no waiver under any circumstances" rule gives the trial judge no discretion whatso-

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[106] 115 S. Ct. 797, 803.

ever. The majority's rule gives relatively greater discretion, however, by invalidating waivers resulting from "fraud" or "coercion," for such judicial fact-finding—especially for "facts" that involve the normative decisions of how much pressure is too much, how much puffing is fraud—is inherently discretionary.[107] But erring on the side of greater discretion is precisely what the Rules contemplate.

The debates among the Justices in *Tome* and *Mezzanatto* thus reflect many of the themes to which this Article now turns. When, if ever, do words have a "plain meaning"? What are the roles of "interpretive communities" and informed readers in determining that meaning? Does legislative "intent" exist, should it be the touchstone for statutory interpretation, and, if so, how do we find it? And what are the roles of judicial discretion and policymaking in the interpretive process? The textualist's answers to these questions would, of course, be that the ordinary meaning of text, not "intent" or judicial policy, should control. It has been the task of this section to demonstrate, however, that the Court has recently moved more self-consciously away from textualism and toward a more flexible and sensible approach, an approach toward which we now turn our attention.

II. Interpretive Method and the Federal Rules of Evidence

This Part seeks to articulate that "more sensible" approach to Rules' jurisprudence and to justify it. I call this approach "politically realistic hermeneutics."

Hermeneutics denies the existence of a single, objectively valid interpretation of a piece of text and questions the confinement of an individual to his or her own viewpoint.[108] Instead, the interplay between author and interpreter creates meaning through the medium of language.[109] Judge Posner has summarized hermeneutics well:

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[107] *See, e.g.*, Joseph D. Grano, Confessions Truth, and the Law 63–64 (1993) ("overborne will" test for finding a confession involuntary under the due process clause is a normative, not an empirical, inquiry, for all choices are "voluntary" in the sense of representing a choice among alternatives. The real question is what limitations upon, or pressures to make, certain choices serve the policy goals of confession law); Aharon Barak, Judicial Discretion 12 (Yadin Kaufman trans., 1989) (fact-finding involves substantial judicial discretion).

[108] *See* A.R. Lacey, A Dictionary of Philosophy 91 (1986) (defining "hermeneutics").

[109] *See id.*

> You must try to put yourself in the place of the author you are trying to interpret and understand the problems that he was trying to solve. Documents must be read as a whole. Much communication is tacit—a matter of shared practices—so you must understand an entire culture in order to be able to understand its writings . . . . Interpretation across time or cultures, like translation from a foreign language, is a form of collaboration in which the horizons or perspectives of two cultures fuse; meaning is the common ground between writer and reader.[110]

That there is never a single, objectively valid interpretation does not mean, however, that we cannot choose among competing interpretations. This choice is "politically realistic" because it recognizes that particular statutory interpretations serve political values. Choosing among competing interpretations thus requires a theory of politics—of how the legislature works, whether it works well, and what is and should be its relationship to the courts. This political analysis reveals a loose hierarchy of sources of interpretation that aids the choice among alternatives.[111] There are often political reasons for favoring a particular approach to interpretation for a particular statute. The Rules are no exception.

This Part will examine the interaction between hermeneutics and politics to craft an approach to interpretation more workable than plain meaning. Other commentators have also criticized plain meaning interpretation of the Rules, turning to legislative history, holistic readings, and underlying policies. They have

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[110] RICHARD A. POSNER, THE PROBLEMS OF JURISPRUDENCE 297 (1970) [hereinafter POSNER, JURISPRUDENCE]. This is "sound advice," says Judge Posner, but it does not, in his view, offer a workable method for choosing the correct interpretation. He suggests that a pragmatic approach, emphasizing whether a particular interpretation will have good consequences, is more useful. *See id.* at 299–300. Posner's pragmatics are useful but incomplete. Hermeneutics sensitizes courts to the dangers of relying on text or any other single, isolated source for interpretation. Furthermore, political conceptions and goals give direction to the analysis. A hermeneutic approach recognizes the need to serve competing values and the impossibility of a mechanistically "correct" answer to interpretive questions. That there is no necessary, self-evident answer dictated by logic, however, does not mean we cannot find an answer that is most credible, plausible, or probable, even if eluding the "certainty of calculations." *See* CHAIM PERELMAN & L. OLBRECHTS-TYTECA, THE NEW RHETORIC 1 (1969). As Aristotle recognized in his theory of practical reasoning, "one can determine what is right in specific cases, even without a universal theory of what is right." William N. Eskridge, Jr. & Philip P. Frickey, *Statutory Interpretation as Practical Reasoning*, 42 STAN. L. REV. 321, 323 (1990) (applying Aristotle's practical philosophy to statutory interpretation). *See* ARISTOTLE, NICHOMACHEAN ETHICS bk. VI, chs. 5–11 (H. Rackham trans., 1962).

[111] *See* Eskridge & Frickey, *supra* note 110, at 323 (outlining such a hierarchy).

not, however, justified their reliance on such data.[112] This Part will do just that.

A. *Public Choice Theory*

1. Rent-Seekers Win

An understanding of theories of statutory interpretation requires an understanding of the theory of public choice. Public choice theory applies the tools of economics to politics.[113] It assumes that re-election is the primary motive for legislators.[114] It also acknowledges the prominence of rent-seeking groups.[115] These groups will organize and try to "buy" legislation, by promising to provide money, advertising, and the votes of members

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[112] *See* Hon. Edward R. Becker & Aviva Orenstein, *The Federal Rules of Evidence After Sixteen Years—The Effect of "Plain Meaning" Jurisprudence, the Need for an Advisory Committee on the Rules of Evidence, and Suggestions for Selective Revision of the Rules*, 60 GEO. WASH. L. REV. 857 (1992); Randolph Jonakait, *The Supreme Court, Plain Meaning, and the Changed Rules of Evidence*, 68 TEX. L. REV. 745 (1990); Glen Weissenberger, *The Supreme Court and the Interpretation of the Federal Rules of Evidence*, 53 OHIO ST. L.J. 1307 (1992) [hereinafter Weissenberger, *The Supreme Court*]. The single exception is Eileen Scallen's forthcoming article *Classical Rhetoric, Practical Reasoning and the Law of Evidence* 44 AM. U. L. REV. (forthcoming May 1995) (draft, on file with the author). Professor Scallen argues that the teachings of the classical rhetoricians, embodied in the Rules, require an interpreter to rely on a broad array of data. We agree on this need for a wide-ranging inquiry, although I reach this conclusion by emphasizing the teachings of modern political and hermeneutic theory, rather than classical Greco-Roman rhetoric. We disagree, however, about the role of legislative intent, she being even more skeptical than I about such intent. *See* Scallen, *supra*, at 36, 52 (criticizing legislative intent as mythological and justifying resort to Advisory Committee Notes solely because they represent the views of evidence "experts"). Furthermore, I rely on the literary theorist's concept of interpretive communities. While the choice of interpretive community is policy-driven, there can nevertheless often be agreement about what community should be chosen, and, once that choice is made, textual meaning can be relatively determinate. *Compare* Scallen, *supra*, at 77–93 *with* Taslitz, Daubert*'s Guide*, *supra* note 1, at 34–35 n.167 (critiquing her analysis as giving too little weight to text and intent). Finally, while we agree on the Rules' preference for trial judge discretion, I stress that that preference can help us choose among competing plausible interpretations. *See supra* text accompanying notes 69–73; *infra* text accompanying notes 348–366. We both, however, offer a choice in emphasis—not previously offered by other evidence scholars—of a pragmatic alternative to prevailing formalist theories.

[113] IAN MCLEAN, PUBLIC CHOICE: AN INTRODUCTION 1, 9 (1987).

[114] DANIEL A. FARBER & PHILIP P. FRICKEY, LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION 22 (1991). The theory need not be so rigid. It has been modified to recognize that sometimes politicians are genuinely interested in the content of the policies they adopt. *See* MCLEAN, *supra* note 113, at 30. But the assumption that most legislative conduct is explained by vote maximization nevertheless continues to be fundamental to the theory. *See* FARBER & FRICKEY, *supra*, at 22.

[115] Jonathan Macey, *Promoting Public-Regarding Legislation Through Statutory Interpretation: An Interest Group Model*, 86 COLUM. L. REV. 223, 224 n.6 (1986).

to help re-elect a legislator.[116] "Rent-seekers" try to obtain more from the government than they would be able to obtain from the free market,[117] and they cost the public more than they themselves gain, making society as a whole worse off.[118]

Rent-seeking groups are likely to have power because of "free riders." A "free rider" recognizes that his impact on how much of a particular good the government provides is small. He thus has an incentive not to work for the provision of that good. While others will ensure that the good is provided, they will not be able to exclude the non-participating "free-rider" from receiving the benefits of a government program such as national defense.[119] The ordinary free-riding citizen thus does not lobby the legislature. But small, rent-seeking groups are likely to be aware of what their members are doing and can use threats, promises, and conditional cooperation to ensure that members will act together for the good of the group.[120] Under public choice theory, therefore, legislation results from rent-seeking behavior, *not* the legislators' conception of the public interest.[121]

2. Arrow's Paradox

Public choice theory also maintains that legislative outcomes do not reflect the will of legislative majorities. Instead, the order of two-option voting may determine the result. In such cases, whoever controls the voting agenda controls the result.

An example demonstrates this problem. Three congressmen must decide which military bases to keep open. They have the following preferences: Legislator 1 prefers closing a base in Texas to closing a base in Illinois and one in Illinois to one in Florida; Legislator 2 prefers Illinois to Florida and Florida to Texas; and Legislator 3 prefers Florida to Texas and Texas to Illinois.[122]

If they first choose between Texas and Illinois, Legislators 1 and 3 both will vote for Texas, both preferring it to Illinois, and the Texas base will close. Then they will vote between Texas

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[116] *See id.*

[117] *Id.*

[118] FARBER & FRICKEY, *supra* note 114, at 34.

[119] *See* MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS 25 (1965).

[120] *See* MCLEAN, *supra* note 113, at 63.

[121] *See id.*

[122] This example is a variation of one in FARBER & FRICKEY, *supra* note 114, at 39.

and Florida, since Illinois will have been eliminated. Florida, however, will win this vote because Legislators 2 and 3 prefer Florida over Texas. This does not reflect majority preferences, though, because Legislators 1 and 2 prefer Illinois to Florida. The same example will yield a different result if the voting occurs in a different order.[123] This phenomenon is called Arrow's Paradox.[124]

Arrow's Paradox and the success of rent-seekers suggest that legislation may reflect neither the public nor the legislative will. The prevailing technique for interpreting statutes, however, searches for the "intent" of the legislature.[125] Courts claim their interpretations carry out the will of the people embodied in laws passed by their elected representatives.[126] Public choice theory purports to reveal the weaknesses of these judicial claims. Legislation often reflects the will not of the people but of small, rent-seeking groups. Furthermore, legislation often reflects not the preferences of the legislative majority but the views of those legislators controlling the agenda. Legislative "intent" is thus illusory. We should abandon the futile quest for intent and focus on a better key to statutory interpretation: the language of the statute.

B. *The New Textualism*

The "new textualism"[127] emphasizes statutory language. Under the traditional approach to statutory interpretation, the plain meaning of the text governs unless legislative history strongly contradicts it.[128] Where a statute is ambiguous, legislative history is often decisive.[129] Proponents of the new textualism, however,

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[123] *See id.*

[124] GERALD S. STROM, THE LOGIC OF LAWMAKING 28 (1990). The Paradox is admittedly more complex than this example suggests. Arrow and his followers have argued that no method of combining individual preferences will satisfy the basic requirements of a rational system of collective choice. *See* FARBER & FRICKEY, *supra* note 114, at 38–39; MCLEAN, *supra* note 113, at 165–68.

[125] Weissenberger, *The Supreme Court*, *supra* note 112, at 1308.

[126] *See id.* at 1308–09.

[127] Eskridge, *The New Textualism*, *supra* note 4 (coining the term "new textualism"). While the justifications for, and details of, the "new" textualism are indeed new, scholarly support for a textualist approach is not. *See* Oliver Wendell Holmes, *The Theory of Legal Interpretation*, 12 HARV. L. REV. 417–18 (1899) ("We ask, not what [the author] meant, but what those words would mean in the mouth of a normal speaker of English, using them in the circumstances in which they were used.").

[128] Eskridge, *The New Textualism*, *supra* note 4, at 624.

[129] *Id.*

generally ignore legislative history if the statute has a plain meaning, and they confirm plain meaning with text-based arguments, for example, from the overall structure of the statute.[130]

The new textualists read the text from the perspective of an "ideal reader," with superior knowledge of English grammar,[131] who gives words their "ordinary meanings."[132] They believe grammatical analysis, canons of construction, and a quest for consistency with other parts of the statute in question or with similar terms in other statutes will resolve most ambiguities and yield a workable "plain meaning."[133]

New textualists deem substantive policies relevant only to ensure that a statutory meaning makes sense—in other words, that it is not absurd.[134] Justice Scalia, the primary defender of new textualism on the Court, gave the clearest statement of this approach in analyzing Federal Rule of Evidence 609 in his concurring opinion in *Green v. Bock Laundry Mach. Co.*[135] In the rare instances when text-based arguments do not resolve a dispute, Justice Scalia is willing to look to legislative history, but some other proponents of new textualism will not go even that far.[136]

New textualism is arguably consistent with public choice theory. One of the new textualists, Judge Frank Easterbrook of the Seventh Circuit, has expressly relied upon public choice theory to justify his approach.[137] New textualism finds additional support in other justifications.

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[130] *Id.* at 623–24. *But see* Taslitz, Daubert*'s Guide*, *supra* note 1, at 30 (noting that some new textualists might turn to legislative history to verify that plain meaning was actually intended).

[131] *See* William D. Popkin, *An "Internal" Critique of Justice Scalia's Theory of Statutory Interpretation*, 76 MINN. L. REV. 1133, 1142–48 (1992).

[132] *See id.* at 1140–41.

[133] *See* Eskridge, *The New Textualism*, *supra* note 4, at 655–56.

[134] Popkin, *supra* note 131, at 1142.

[135] 490 U.S. 504, 528–29 (1989) (Scalia, J., concurring in part). For a more detailed discussion, see Taslitz, Daubert*'s Guide*, *supra* note 1, at 30. Note that Justice Scalia will, however, apparently examine legislative history to confirm that an absurd meaning was not intended. *See id.* Moreover, Scalia departed substantially from a strict textualism in a recent opinion. *See supra* text accompanying notes 32–41, 63–65 (analyzing Scalia's concurrence in Tome v. United States, 115 S. Ct. 696 (1995)).

[136] *Compare* Taslitz, Daubert*'s Guide*, supra note 1, at 30 (discussing Scalia's approach) *with* ESKRIDGE, *Dynamic Interpretation*, *supra* note 3, at 34–42. (discussing other theorists). Note that Scalia cryptically suggested in *Tome* that "plain" meaning could be found by examining the Advisory Committee Notes, the most "persuasive scholarly commentaries" on the Rules' meaning. *See supra* text accompanying note 34.

[137] *See* Frank Easterbrook, *Statutes' Domains*, 50 U. CHI. L. REV. 533, 547–48 (1983) ("This [new textualism] follows from the discoveries of public choice theory."). Recently, Judge Easterbrook has favored a moderate textualism. Frank H. Easterbrook,

First, new textualists argue that "collective legislative intent" is meaningless. Each legislator acts for different reasons.[138] He may vote in favor of some legislation about which he cares little to gain support for future, more important legislation. Another may vote another way in anticipation of a particular voter reaction ("he's tough on crime"), even if he personally dislikes the bill. No single intent can easily be attributed to a legislative body.

Second, even if collective intent exists, the new textualists deny that judges can determine it reliably.[139] For example, committee reports may reflect the views of only a few members of Congress.[140] Moreover, rent-seeking legislators will seek to include self-serving legislative history favoring the rent-seeking group's interpretation.[141] Relying on legislative history is problematic because it may embody the views of legislators who were unable to have certain language included in the statute.[142]

Third, only the statutory language, not the legislative history, is enacted by Congress and approved by the President. Therefore, only such language has the force of law.[143] Democratic values thus compel reliance on the statutory text.

These justifications of the new textualism are flawed, especially as applied to the Federal Rules of Evidence, including the failure to acknowledge the reader's role in creating meaning.

Text, History, and Structure in Statutory Interpretation, 17 HARV. J.L. & PUB. POL'Y 61, 67 (1994) ("[i]n interesting cases meaning is not 'plain'" and requires "footing more solid that [sic] a dictionary—which is a museum of words, an historical catalog rather than a means to decode the work of the legislature.").

[138] *See, e.g.*, Edward L. Rubin, *Beyond Public Choice: Comprehensive Rationality in the Writing and Reading of Statutes*, 66 N.Y.U. L. REV. 1, 8 (1991) ("No one from Madison to the Progressives to the contemporary opponents of public choice would dispute that [individual legislators'] preferences differ or that they cannot be aggregated without complications and distortions.").

[139] *See* FARBER & FRICKEY, *supra* note 114, at 22–34. Alternatively, in *Green v. Bock Laundry Mach. Co.*, 490 U.S. 504 (1989), Justice Scalia argued that the text is the best guide to collective intent because it is only the text that is read by the entire Congress. *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 30. More recently, however, Scalia has purported to reject entirely any inquiry into intent, the text having a life of its own. *See supra* text accompanying notes 32–41.

[140] *See* FARBER & FRICKEY, *supra* note 114, at 95.

[141] *See infra* sources cited notes 202–231, 292–311.

[142] *See* FARBER & FRICKEY, *supra* note 114, at 90.

[143] *See id. See also supra* text accompanying notes 32–41 (noting Justice Scalia's recently making this very point).

C. *A Reader-Centered Approach*

1. The Reader's Viewpoint

It is impossible to read any text without certain background assumptions.[144] Thus a reader's knowledge of the world, including his values and prejudices, affects the meaning of words, even if the reader is unaware of his application of these assumptions.[145] A word may have a single meaning for a particular person because his assumptions lead him to see that meaning. If most people share his assumptions, then most will agree that the word has a "plain meaning." But those assumptions, not textual clarity, give the word meaning.

A modern hearsay problem illustrates the complexities of interpretation. Rule 803(4) excepts from the hearsay bar "[s]tatements made for purposes of *medical* diagnosis or treatment and describing *medical* history . . . ."[146] Does this rule allow a court to admit, in a criminal trial, statements made by a three-year-old alleged victim of sexual abuse to a psychiatrist, psychologist, or psychiatric social worker?

The "ordinary speaker" of English would likely agree that a statement to a psychiatrist, a licensed physician, is for the purpose of "medical" diagnosis or treatment.[147] It is less likely that the "ordinary speaker" of English would think of a psychologist as offering "medical" treatment,[148] and it is even more unlikely that statements to a social worker would be considered to involve "medical" treatment.[149] The ordinary speaker may be unable to

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[144] *See* KENT GREENAWALT, LAW AND OBJECTIVITY 73 (1992) ("Much modern writing on interpretation, or hermeneutics, emphasizes the inevitability of an interpreter's reliance upon his or her own presuppositions in interpreting a text or practice."); CASS R. SUNSTEIN, THE PARTIAL CONSTITUTION 101 (1993) ("[N]o text has meaning apart from the principles held by those who interpret it, and those principles cannot be found in the text itself.").

[145] *See* Eskridge & Frickey, *supra* note 110, at 343 ("A final problem undercuts textualism: the importance of the interpreter's own context, including current values.").

[146] FED. R. EVID. 803(4) (emphasis added).

[147] *See* WEBSTER'S NINTH NEW COLLEGIATE DICTIONARY 737, 950 (1990) (defining "medical" as "1: of, relating to, or concerned with physicians or the practice of medicine 2: requiring or devoted to medical treatment," and defining "psychiatry" as "a branch of *medicine* that deals with mental, emotional, or behavioral disorders.") (emphasis added). I also took an informal survey of law students who had not yet taken a course in evidence and non-lawyer friends and family (using non-leading questions and without explanation), and all in the sample agreed with the ordinary understandings I offer here.

[148] *See id.* at 951 (defining "psychology" as a "science of mind and behavior" but not mentioning any form of the words "medicine" or "physician").

[149] *See id.* at 1119 (defining "social work" as "any of various professional services,

articulate the reasons for these distinctions, which he senses because of common usage, experience, and images. If pressed, he might observe that social workers lack the training of psychiatrists. He might further maintain that social workers are just not doctors and that only doctors and their assistants, like nurses, offer "medical" treatment.

Yet psychologists and social workers would disagree. They would argue that they are healers, and healing a child's emotional trauma from abuse is as important as healing a gunshot wound. The difference between their talking therapy and the somatic treatments often used by psychiatrists should not matter.[150] Indeed, many might argue that psychologists are often *more* successful than psychiatrists in healing emotional injuries.[151] And many psychologists and social workers will maintain that their patients trust and need them just like patients of psychiatrists.[152] The prejudices and preconceptions of the two groups—"ordinary" speakers of English, and psychologists and social workers—affect the meaning they give the word "medical."

2. The Author's Viewpoint

But should any of this matter if Congress intended something different? It is unlikely that members of Congress expressly considered whether statements to psychologists or social workers should be considered to be made for the purposes of "medical" treatment. No legislative history reveals such consideration.[153] What Congress likely had in mind—to the extent we can

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activities, or methods concretely concerned with the investigation, treatment, and material aid of the economically underprivileged and socially maladjusted," again without reference to "medicine" or "physicians").

[150] Interview with Lana Wright, a licensed Virginia psychiatric social worker, in Herndon, Va. (May 14, 1994). *See also* E. JERRY PHARES, CLINICAL PSYCHOLOGY: CONCEPTS, METHODS, AND PROFESSION 6 (4th ed. 1992) (noting that social workers, psychiatrists, and clinical psychologists often function together as a single mental health team).

[151] *See* Charles A. Kiesler, *The Training of Psychiatrists and Psychologists*, 32 AM. PSYCHOL. 108 (1977) ("Psychiatrists receive standard medical training, little formal training in the study of human behavior, and practically no experience in research. Clinical psychologists, on the other hand, . . . are engaged for 5 or more years in a broad study of human behavior.").

[152] *See* PHARES, *supra* note 150, at 6 (In "private practice [the work of psychiatric social workers] . . . in individual or family therapy is often indistinguishable from that of psychiatrists or clinical psychologists.").

[153] *See* 1–4 JAMES F. BAILEY & OSCAR M. TRELLES, THE FEDERAL RULES OF EVIDENCE: LEGISLATIVE HISTORY AND RELATED DOCUMENTS (1980) (including no such references). Analogous issues were, however, considered in the debate over the

speak of a collective congressional mind[154]—was to permit admission of statements by patients motivated to be truthful because of their interest in proper treatment.[155] Congress may have also contemplated that objective means of confirming reports of medical symptoms and doctors' interests in obtaining relevant and reliable data would be additional guarantees of trustworthiness.[156]

Rule 803(4) admits statements made for the purposes of diagnosis, even where obtained solely for use as evidence at trial.[157] Statements made in preparation for litigation are more suspect than statements made in anticipation of treatment.[158] That Congress permitted admission of the former seems inconsistent with the trustworthiness rationale. Indeed, the Advisory Committee articulated a more pragmatic rationale for admission: patient statements made to doctors consulted solely to offer expert opinions at trial are generally admitted anyway on non-hearsay theories.[159] Juries will likely ignore an instruction not to use the statements for hearsay purposes, so the court might as well admit them for the truth of the matter asserted.[160] Commentators have suggested that there was also a trustworthiness rationale, even for these litigation preparation statements: "As a matter of policy, a fact reliable enough to serve as the basis for diagnosis is also reliable enough to escape hearsay proscription."[161]

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proposed-but-never-adopted psychotherapist-patient privilege. *See* 3 *id.* at 450–52, 458–59, 472–73, 478–80.

[154] *See infra* text accompanying notes 243–260.

[155] *See* FED. R. EVID. 803(4) advisory committee's note. ("Even those few jurisdictions which have shied away from generally admitting statements of present condition have allowed them if made to a physician for purposes of diagnosis and treatment in view of the patient's *strong motivation to be truthful.*") (emphasis added).

[156] *See* Robert F. Mosteller, *Child Sexual Abuse and Statements Made for the Purpose of Medical Diagnosis or Treatment*, 67 N.C. L. REV. 257, 267–69 (1989).

[157] *Id.*

[158] *See* VAUGHN BALL ET AL., MCCORMICK ON EVIDENCE 692–94 (Edward W. Cleary ed., 2d ed. 1972) (claiming that diagnostic statements for purposes of litigation do not provide adequate incentives for patients to tell the truth because they know that their treatment will be unaffected).

[159] Such statements would be offered to explain the basis of the expert's opinion. That the expert asked the right questions and received useful answers supporting his opinions show he is good at what he does and should be believed. But the statements are not offered to show that they are indeed true; therefore, they are not hearsay. *See id.* at 692–93.

[160] *See id.* at 694.

[161] JACK B. WEINSTEIN & MARGARET A. BERGER, WEINSTEIN'S EVIDENCE MANUAL 16–22 (rev. student ed. 1991). Weinstein and Berger so conclude based upon Rule 803(4) advisory committee's note. That note summarized the pragmatic rationale for admitting diagnostic statements: "[t]his position is consistent with the provisions of Rule 703 that the facts on which expert testimony is based need not be admissible in

If Congress intended to allow admission of only trustworthy statements, then the word "medical" must include assurances of trustworthiness. There may be a lower amount of patient self-interest in accurate reporting (and thus a lower level of trustworthiness) for psychological illnesses than for somatic ones.[162] Moreover, psychological maladies are less capable of objective verification than physical ones.[163] Further problems result when a psychologist becomes a "surrogate witness" and testifies to a story told by a criminal defendant without the defendant subjecting himself to cross-examination.[164] According to some, when the exception extends to mental health interviews prepared solely for the purposes of [criminal] litigation, the exception loses its "general integrity,"[165] whether conducted by a psychiatrist, psychologist, or social worker.[166] If trustworthiness were Congress's primary purpose, then mental health interviews under certain circumstances should not be viewed as involving "medical" treatment.

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evidence if of a kind ordinarily relied upon by experts in the field." FED. R. EVID. 803(4) advisory committee's note. But these Rule 703 limitations seek to ensure a minimal standard of trustworthiness. See FED. R. EVID. 703; FED. R. EVID. 703 advisory committee's note. By drawing a parallel to Rule 703, the Rule 803(4) note therefore suggests that a similar concern with trustworthiness underlies the diagnostic-opinions portion of the latter Rule.

[162] MOSTELLER, *supra* note 156, at 268.

[163] *Id.* While commentators have focused on trustworthiness concerns such as objective verifiability in addition to patient self-interest, *id.* at 267–68, and while there is support from the advisory committee's note for this focus, a contrary text-based argument can be made. The Rule speaks of statements made for the "purposes of medical diagnosis or treatment . . . ." FED. R. EVID. 803(4). Consequently, even statements made to parents, ambulance drivers, and others, where a patient understood that his statements would be transmitted to a doctor for diagnosis or treatment, arguably fit within the Rule. *See* RICHARD O. LEMPERT & STEPHEN A. SALTZBURG, A MODERN APPROACH TO EVIDENCE: TEXT, PROBLEMS, TRANSCRIPTS AND CASES 421–22 (2d ed. 1982). Yet such persons are not trained to elicit or evaluate the reliability of the statements. Under this argument, patient self-interest, not some other "objective" indicia of trustworthiness, is the Rule's sole concern. *But see id.* at 421 (noting that a focus on patient self-interest makes sense, "at least as [the theory of Rule 803(4)] relates to treatment," suggesting that a different focus may make sense concerning statements made purely for diagnosis).

[164] *See* GLEN WEISSENBERGER, WEISSENBERGER'S FEDERAL EVIDENCE 397 (1987) [hereinafter WEISSENBERGER, EVIDENCE]. Additionally, a mental health patient may suffer from hallucinations, delusions, detachment, or incoherence, all of which may impair the trustworthiness of his statements. *Id.* Furthermore, Rule 803(4)'s requirement that all patient statements be "reasonably pertinent to [medical] diagnosis or treatment" is meaningless in the psychiatric context because virtually everything a patient says is pertinent. *See* PAUL R. RICE, EVIDENCE: COMMON LAW AND FEDERAL RULES OF EVIDENCE 594 (2d ed. 1990).

[165] Mosteller, *supra* note 156, at 283.

[166] *Compare* PAUL EKMAN, TELLING LIES: CLUES TO DECEIT IN THE MARKETPLACE, POLITICS, AND MARRIAGE (1992) (summarizing *psychologist's* research on spotting lies) *with supra* note 151 and accompanying text (emphasizing relatively greater

3. The Informed Reader

The focus on "purpose" shows that speakers may give words different meanings than readers give them. But the analysis of purpose can also be viewed from the perspective of a reader. A member of the congressional committee that recommended the adoption of Rule 803(4) or the Advisory Committee that drafted it would probably read the word "medical" with the understanding that it implies certain guarantees of trustworthiness. That understanding would also guide his judgment whether the exception should include statements to a social worker, even if he had not considered social workers when promulgating the Rule.

A lawyer might bring a similar perspective to reading the Rule. Indeed, statutes are written for different audiences,[167] and the audience to which a procedural rule is addressed is one of lawyers. Because of their common background of legal education, most lawyers will associate the medical diagnosis and treatment exception, and thus the word "medical" in the Rule, with trustworthiness.[168] They will at least recognize ambiguity in deciding whether the exception extends to statements made to psychiatric social workers. How lawyers resolve that ambiguity will partly turn on their knowledge of present day realities, like the skills of social workers or psychologists in eliciting trustworthy information by, for example, avoiding leading questions. A lawyer might ask: Do they have tools to explore the accuracy of self-reports? Do patients believe they need to give psychologists and social workers accurate information? What do patients think are the consequences of lying? If social workers are well-trained to maximize the likelihood of accurate responses, and if most patients believe social workers are essential to curing what they view as serious illnesses, then a lawyer might easily include social workers within the scope of Rule 803(4).

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training of psychologists in human behavior). This comparison suggests that psychiatrists, who are most likely to be viewed as engaging in "medical" diagnosis, are in fact *least able* to spot a patient's lies.

[167] *See* LIEF H. CARTER, REASON IN LAW 87 (4th ed. 1994) ("Legislatures direct different statutes to different kinds of audiences . . . . [H]ighly technical laws may [therefore] communicate only to special classes of people . . . .").

[168] *See, e.g.*, LEMPERT & SALTZBURG, *supra* note 163, at 420–22.

4. The Ideal Reader

The point may perhaps be clarified by the notion of an "ideal reader." Writers of texts, including legal texts, hope and expect that the texts will be read in different contexts by different audiences not yet known or imagined.[169] But cultural meanings change over time.[170] New cultural meanings and circumstances raise new questions about text.[171] Thus, texts are sources for ongoing conversations about their meaning among members of the relevant interpretive community; the texts help to unite and create such communities (a point to which I will return later).[172]

Two simple concepts illustrate this. First, one learns to read a particular text in part from other readers. Second, that we debate the meaning of statutes shows that there is rarely an indisputable meaning "out there." Instead, we create meaning from our conversations with each other.[173] For those conversations to be meaningful, the text contemplates an ideal reader who appreciates the *possibilities* for perception and response that the text seeks to realize.[174] Being such a reader

> requires an understanding of the text in its cultural and political context, in light of the accepted meanings of words, and with an understanding of the major purposes of the text, of its types and examples. It thus requires one to become an expert reader of the culture itself.[175]

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[169] JAMES BOYD WHITE, HERACLES' BOW: ESSAYS ON THE RHETORIC AND POETRY OF THE LAW 88–89 (1985).

[170] *Id.* at 88.

[171] *Id.* at 89.

[172] *See id.* at 78, 80, 87–88, 95–96; *infra* text accompanying notes 178–196.

[173] *See id.* at 78, 95–98.

[174] *Id.* at 91.

[175] *Id.* at 96. Professor White would reject the notion that the author's subjective intent controls. *Id.* at 81, 101–02. A statement of intention always faces the challenge, "If that is what he [the writer] meant, why didn't he say it?" *Id.* at 101. Moreover, it is hard to describe an intent not expressly stated in a text where the text is meant to be read in changing contexts that may not have been conceived by the author. *See id.* Furthermore, a statement of intention can always be made at differing levels of generality, *id.*, and the question must always be answered: Whose intent matters, and how do we find it? *Id.* at 81. Consequently, determining "intention" is itself an act of interpretation. *Id.* at 101.

Nevertheless, White considers intent a relevant but not controlling inquiry. *See id.* at 102. Even more importantly, unlike some of the public choice theorists, he is equally skeptical of text and instead argues that examination of the cultural context in which text was written and in which it is being read creates meaning. *See id.* at 103 (arguing for "a conception of law and of cultural life generally . . . as a way of giving usable present meaning to past experience."). *See also* RONALD DWORKIN, LAW'S EMPIRE 313–54 (1986) [hereinafter, DWORKIN, LAW'S EMPIRE] (pseudo-literary approach to statutory interpretation that also rejects plain meaning and speaker's intent as sole

The "ideal reader" of Rule 803(4) is therefore a lawyer informed about and concerned with the truth-related and pragmatic justifications for hearsay exceptions generally, and for Rule 803(4) specifically. That reader creates meaning from the interaction between his own values, his knowledge of the world, and his understanding of the speakers' goals as revealed by the political context in which they spoke. This understanding requires considering Rule 803(4)'s words and legislative history and present knowledge of patient perceptions of psychiatric social workers' roles and the quality of their training. But Rule 803(4)'s text alone embodies no fixed, eternal answer to the problem.[176]

To summarize: The new textualists' view of language as an immutable fact to be found "out there" contradicts our understandings of the biological and cognitive bases of language,[177] and its role as both social behavior and literary text. Statutory

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determinants of meaning). *But compare* RICHARD A. POSNER, LAW AND LITERATURE: A MISUNDERSTOOD RELATION 246–58 (1988) [hereinafter POSNER, LAW AND LITERATURE] (statutory law is fundamentally different from literature) *with* STANLEY FISH, DOING WHAT COMES NATURALLY: CHANGE, RHETORIC, AND THE PRACTICE OF THEORY IN LITERARY AND LEGAL STUDIES 303–04 (1992) (Fish distinguishes law and literature because the interpretive community in law seeks to narrow, rather than expand, meaning, not because of more fundamental differences.).

[176] For another illustration of an ideal, or at least an "informed" reader, see Tome v. United States, 115 S. Ct. 696, 706 (1995) (Scalia, J., concurring in part), discussed *supra* text accompanying notes 32–41, 64.

[177] *See* LAWRENCE M. SOLAN, THE LANGUAGE OF JUDGES (1993). Solan argues that, despite our learning a set of grammatical rules through biological and cognitive tendencies, much language is still ambiguous. *See id.* at 95–99. First, the words of a sentence may be read as having more than one syntactic structure, with each structure having a different meaning. *Id.* at 95. For example, the validity of a jury instruction not to be swayed by "mere sentiment, conjecture, sympathy, [and] passion . . ." turned on whether "mere" modified only "sentiment" or all other items in the list. *Id.* at 56–57 (discussing California v. Brown, 479 U.S. 538 (1987)). Second, a sentence with a given syntactic structure can have more than one logical structure. For example, "Each of the lawyers thought that he should conduct a thorough cross-examination of the witness" could mean that lawyer A thought lawyer A should be thorough while lawyer B thought that lawyer B should be thorough, or it could mean that each of the members of a group of lawyers believed that a particular lawyer should do a thorough cross-examination. *Id.* at 95–96. Third, when a statute references a category of things or events, grammatical rules often do not resolve whether a particular item or event fits within the category. *Id.* at 96–98. Yet, "[o]ur need to understand the context in which utterances are made in order to choose among multiple possible interpretations is beyond dispute . . . ." *Id.* at 98. Even though only a reference to context will resolve disputes over meaning, courts often insist on justifying their results as dictated by "plain language" when our instincts as speakers of English tell us that they are wrong. *Id.* at 34–36, 115–17. *See generally* POSNER, JURISPRUDENCE, *supra* note 110, at 263–64 (the "plain meaning fallacy" results partly from an underappreciation of the widespread existence of "internal" ambiguity, based on unclear sentence grammar and syntax, and "external" ambiguity, ambiguity revealed only by awareness of a sentence's background).

language thus specifically offers an occasion for a conversation among ideal readers in the relevant interpretive community.

D. *Interpretive Communities*

If law is the occasion for a conversation about meaning among members of an interpretive community, then the membership of that community must be determined. Different communities may assign different meanings to the same word. Yet no "plain" or other meaning can be found without choosing an interpretive community. The choice inevitably incorporates values and policy preferences.[178]

The choice of interpretive community was critical—and controversial—in *Daubert* where the Court found that the *Frye* general acceptance test for admitting scientific evidence was superseded by a Rule 702 "relevancy and reliability" test.[179] Rule 702 permits expert opinion if "scientific . . . knowledge will assist the trier of fact . . . ."[180] The Court looked to three different interpretive communities—ordinary persons to define "knowledge," scientists to define "scientific knowledge," and lawyers and law professors to define relevance.[181] Yet scientists did not draft Rule 702, and it is unlikely that the drafters had in mind the scientists' definition of "science" or the hallmarks of the scientific method. Still, the Court's definition of "scientific knowledge" apparently incorporated elements of the scientists' conception, the conceptions of the philosophers of science, and related conceptions of the sociology of scientific knowledge.[182] The Court chose a broad, yet highly specialized community whose mem-

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[178] *See* FISH, *supra* note 175, at 303 ("[A]s a fully situated member of an interpretive community, be it literary or legal, you 'naturally' look at the objects of the community's concern with eyes already informed by community imperatives, urgencies, and goals."); GREENAWALT, *supra* note 144, at 87 (recognizing legitimate and substantial disagreement over the extent to which interpretation should be bound by the authors' interpretive community or by a contemporary interpretive community); POSNER, JURISPRUDENCE, *supra* note 110, at 263 ("Whether the authors' linguistic community is the right one to use to fix statutory meaning is not, as Holmes seems to have thought, self-evident.").

[179] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 45 (summarizing holding of Daubert v. Merrill Dow Pharmaceuticals, Inc., 113 S. Ct. 2786 (1993)).

[180] FED. R. EVID. 702.

[181] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 62–64.

[182] *See infra* text accompanying notes 188–196. I use the plural "conceptions" because philosophers of science differ in their views of what science means (and even regarding what good science is), and the Court failed to adopt a particular view.

bers likely did not share the interpretation of science chosen by lawyers or laypersons.

The Court's implicit reasoning for including scientists in the interpretive community must have been this: The words "scientific knowledge" were meant to identify a particular type of expert, a "scientist." A "scientist" must, however, have the necessary qualifications and knowledge or he cannot help the jury. Moreover, if he follows unreliable methods, his results cannot be useful to the jury. But it is this community of qualified experts, not lawyers, that is best equipped to judge whether a scientist has followed good methods. Only the scientific community will know when methods fall so short of what is reliable that the result should not even be considered "scientific" knowledge. Therefore, only by turning to the community of scientists to give meaning to the words "scientific knowledge" can we achieve Rule 702's mandate to "assist the jury."[183]

This argument resembles the *Frye* test because it relies on the views of the scientific community. It differs from *Frye*, however, in that while scientists decide in part the standards for judging good science, the courts decide whether a particular technique passes muster. The analysis turns on assumptions about the competence of various groups, scientists, judges, jurors; the purpose of Rule 702 to encourage reliable, trustworthy evidence; and the role of the jury to reach an unbiased decision, based on valid information, unhindered by the jury's limited ability to understand.[184] This is not the mechanical, "objective" assignment of plain meaning to which the new textualists pretend.

Nonetheless, *Daubert* did not rely solely on the scientific community in defining "scientific knowledge." "Scientific knowledge" meant "reliability," which involved evaluating factors like the known or potential error rate and the maintenance of stand-

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[183] Note that this chain of reasoning views the phrases "scientific knowledge" and "assist the trier of fact" as inseparable: one helps to define the other. The Court's express analysis, however, treated the two terms as distinct and unrelated. Thus "scientific knowledge" required "reliability" and "assist[ing] the jury" required relevance. *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 46–47. This mechanical, artificial effort contradicts how we read sentences—by obtaining meaning from context and sentence structure—and is illogical. Does this mean that other types of Rule 702 knowledge, that is, "technical, or other specialized knowledge," can be unreliable?

[184] This skeptical view of the jury contrasts sharply with the Court's later statement rejecting Respondent's apprehension that abandoning *Frye* would result in a "'free-for-all' in which befuddled juries are confounded by absurd and irrational pseudoscientific assertions." *Daubert*, 113 S. Ct. at 2798. The Court viewed Respondent as "overly pessimistic about the capabilities of the jury . . . ." *Id.* Again, this reflects the compromise of *Daubert*, here a compromise between fear of, and respect for, the jury.

ards.[185] Lawyers, whose conclusions did not necessarily depend on the views of the scientific community, suggested some of these factors.[186] Furthermore, the Court emphasized the importance of the impact of the testimony on the jury under Rule 403, again not a question decided by the scientific community.[187] Moreover, the Court's decision reflected a split within the scientific community about whether testability and testing are the *sine qua non* of good science.[188] Consequently, contrary to the views of some commentators,[189] the *Daubert* Court did not rely upon a single community.

To the contrary, as Margaret Farrell has recognized, *Daubert* reflects a perhaps flawed compromise between two competing world views.[190] One view, the "Faustian," "Faigmanian," or positivistic view, posits value-free facts that mechanistically exist independently of the minds that perceive them, and universal

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[185] *Id.* at 2796–98.

[186] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 47–50, 62–64.

[187] *Daubert*, 113 S. Ct. at 2797–98.

[188] The Court did, in discussing testability and testing, draw support from the work of Karl Popper, the leading philosopher of science adopting a "positivistic" view of science, and from other adherents of Popperian philosophy. See id. at 2796–97. Popperians believe "the criterion of the scientific status of a theory is its falsifiability, or refutability, or testability." KARL POPPER, CONJECTURES AND REFUTATIONS: THE GROWTH OF SCIENTIFIC KNOWLEDGE 37 (5th ed. 1989) (this quote was among those recited in *Daubert*, 113 S. Ct. at 2796–97). The leading proponent of Popperian philosophy in evidence law has argued that this citation constitutes a wholesale adoption of Popper's philosophy. *See* Audiotape of David Faigman, Evidence After *Daubert*, Presentation of the Section of Law and Social Science, American Association of Law Schools, Annual Meeting (January 3–6, 1994) (on file with author) [hereinafter AALS]. But, were that so, the Court would not have said that testability and testing are "ordinarily" (*not* "always") "a" (*not* "the") key question. *Daubert*, 113 S. Ct. at 2796. Nor would the Court have gone on to list other factors to weigh along with testing, for, to a Popperian, something that is not tested is not science. *See* David Faigman, *To Have and Have Not: Assessing the Value of Social Science to the Law as Science and Policy*, 38 EMORY L.J. 1005, 1016–19 (1989). Indeed, the Court was aware of other views of science as a "cultural, 'socially embedded activity,'" Brief *Amici Curiae* of Physicians, Scientists, and Historians of Science in Support of Petitioners, at 17, *Daubert*, 113 S. Ct. at 2786 [hereinafter Historians' Brief] (quoting STEPHEN JAY GOULD, THE MISMEASURE OF MAN 21 (1981)).

Indeed, an alternative view of science incorporates concepts that cannot be or have not been "falsified" in the Popperian sense; it supports, for example, admission of the clinical judgment of psychologists in certain cases. *See* Andrew Taslitz, *Myself Alone: Individualizing Justice Through Psychological Character Evidence*, 52 MD. L. REV. 1, 101 (1993). Indeed, Sheila Jasanoff expressed surprise at Faigman's citing Karl Popper because in Jasanoff's field Popper is universally rejected. Sheila Jasanoff, AALS, *supra*. She emphasized that testability, like all else in science, was fundamentally a sociological process, not a mechanical, objective, or empirical one. Under this view, courts must decide which community to turn to for validation of testing and must rely on the sociologically molded views of those communities, a process once again similar to *Frye*.

[189] *See supra* note 188 (discussing Professor Faigman's views).

[190] AALS, *supra* note 188.

rules of nature that only science can uncover.[191] Accordingly, science has a superior claim to truth, so the law should defer to the views of the scientific community.

Under the alternate view, however, no facts are divorced from values. Under this view, reality is a statement of probabilities about the future, a statement made differently by different learned communities for different purposes. Science is not a slow, steady progress to truth but a sociological process of consensus-building among the community of scientists. Even under this view, however, science seeks to be descriptive, positive, and predictive. But law is normative and its goal is justice, not descriptive accuracy. Justice may require much that science does not.[192] Therefore, the legal community must participate in the interpretive conversation.[193]

Had *Daubert* chosen a single view, it would have been a simpler and clearer decision. Indeed, some positivists have sought to attribute a clarity to *Daubert* that its text and reasoning will not bear by arguing that it fully adopted the positivistic view of (a particular segment of) the scientific community.[194] This interpretation implies that judges must exclude from trial all techniques that have not been empirically tested, are not amenable to empirical testing, or have been inadequately empirically tested. Almost all clinical assessments, including testimony about battered women's syndrome, insanity, and the psychology of eyewitness identification would be excluded.[195] "Testability and testing" would not be a factor in a flexible weighing process but would instead become a talisman. *Daubert* did not make this choice, however. If it had, it would have created insuperable problems in courtrooms.[196]

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[191] The terms "Faustian" and "Faigmanian" are mine. Both Faust and Professor Faigman spoke at the AALS presentation, and both adopt what is essentially a Popperian stance. *See* AALS, *supra* note 188. *See generally* David L. Faigman, Elise Porter, & Michael Saks, *Check Your Crystal Ball at the Courthouse Door, Please: Exploring the Past, Understanding the Present, and Worrying About the Future of Scientific Evidence*, 15 CARDOZO L. REV. 1799 (1994).

[192] Margaret Farrell, AALS, *supra* note 188.

[193] *See also* STEVEN GOLDBERG, CULTURE CLASH: LAW AND SCIENCE IN AMERICA 20–23 (1994) (concluding *Daubert* represented an uneasy compromise between the respective "progress" and "process" values of scientists and lawyers).

[194] *See supra* note 74 (discussing the views of Professor Faigman).

[195] *See* AALS, *supra* note 188.

[196] For example, "meta-analysis," a technique partly at issue in *Daubert* itself, involves statistical truth, but the mathematics are not open to empirical testing. Tape of Professor Richard Lempert, Expert Testimony in the Wake of *Daubert*, Evidence Section Presentation, AALS, *supra* note 188. Moreover, of the types of methodologies

Thus the choice of interpretive community affects meaning and is an ambiguous and value-laden exercise. But even after the interpretive community is chosen, disputes within that community may result in ambiguity. For example, scientists may disagree themselves on the hallmarks of good science. In no sense, therefore, is the quest for plain meaning a mechanistic linguistic exercise.

E. *Rule 102*

Rule 102 of the Federal Rules of Evidence rejects new textualism:

> These rules shall be construed to secure fairness in administration, elimination of unjustifiable expense and delay, and promotion of growth and development of the law of evidence to the end that the truth may be ascertained and proceedings justly determined.[197]

As understood in the community of lawyers, this Rule's "plain meaning" invites interpretation of the Rules to allow for growth by the common law method, with regard for the policies underlying evidence law.[198] Edward Cleary, the Reporter for the Advisory Committee on the Federal Rules of Evidence, confirmed this reading: "It seems essential that the Rules contain at some point a provision allowing expansion by analogy to cover new or unanticipated situations . . . ."[199] The Rules contain many

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involved in *Daubert* (animal studies, structural studies, and epidemiological studies), epidemiology is generally viewed as deserving the most weight. But the truth of that conclusion cannot be empirically tested. *Id.*

[197] FED. R. EVID. 102.

[198] *See* Weissenberger, *The Supreme Court*, *supra* note 112, at 1328–30 & n.117. Professor Imwinkelried's argument favoring a textual approach relies on Rule 402—which is not an interpretive rule—ignoring the only true interpretive rule in the statute, Rule 102. *See* Glen Weissenberger, *Are the Federal Rules of Evidence a Statute?*, 55 OHIO ST. L.J. 393, 397–98 (1994) [hereinafter Weissenberger, *The Rules as a Statute?*].

[199] Proposed Rules of Evidence: Hearings before the Subcomm. on Criminal Justice of the House Committee on the Judiciary, 93d Cong., 1st Sess. Supp. 4 (1973). Professor Imwinkelried has stressed that, in a post-Rules-adoption article, Professor Cleary stated that common law knowledge continues to exist but in the form of guidance for the exercise of "delegated" powers. Edward J. Imwinkelried, *A Brief Defense of the Supreme Court's Approach to the Interpretation of the Federal Rules of Evidence*, 27 IND. L. REV. 267, 279–80 (1993). Professor Imwinkelried argues that the common law, while relevant to explaining the meaning of expressly delegated power, cannot be used as the basis for crafting new rules. His analysis ignores, however, the tenor of Cleary's article read as a whole, and, more clearly and importantly, Cleary's *pre*-Rule statement at congressional hearings that Rule 102 was specifically designed to promote growth in the law of evidence "by analogy."

broad, vague phrases—"assist the trier of fact," "probative value . . . substantially outweighed by . . . unfair prejudice"—that do not mandate how to decide particular cases. Rather, the terms' breadth demonstrates a recognition of the need for case-by-case development of their meaning.[200] Rule 102 and the broad, open-ended language found throughout the Rules instruct judges *not* to be bound by a rigid, textualist approach to the Rules. Surprisingly, despite its role in the creation of the Rules, the Court nevertheless sometimes adopts a rigid, unworkable approach, contrary to the general interpretive instruction of Rule 102.[201]

F. *Collective Intent Exists*

As shown above, the theory of language underlying the new textualism is unworkable generally and under the Rules. This section will turn to a critique of the public choice theorists' arguments for heightened emphasis on text, starting with the assertion that statutes lack coherent purposes.

1. A Coherent Public Purpose

Public choice theorists' most extreme conclusion—that legislative intent or purpose are incoherent[202]—is untenable. First, political science research demonstrates that ideology—defined as individual beliefs about the public interest[203]—often predicts legislators' behavior better than economics.[204] Legislators thus prob-

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[200] Professor Weissenberger has also persuasively argued that the creation of new law is an inevitable part of the process of case-by-case reasoning that gives life to ambiguous language. Weissenberger, *The Rules as a Statute?*, *supra* note 198, at 399–400. The very act of applying existing rules to new, case-specific circumstances thus creates new law. *Id.*

[201] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 3–6, 34–35.

[202] While a hermeneutic approach denies that a single, objective authorial intent can be divined, or, if divined, should necessarily control interpretation, hermeneuticists nevertheless acknowledge the important role of such intent in the hermeneutic enterprise. *See* Steven Knapp & Walter Benn Michaels, *Intention, Identity, and the Constitution: A Response to David Hoy*, *in* LEGAL HERMENEUTICS: HISTORY, THEORY, AND PRACTICE 187–88 (Gregory Leyh ed., 1992) [hereinafter LEGAL HERMENEUTICS]; Michael J. Perry, *Why Constitutional Theory Matters to Constitutional Practice*, *in* LEGAL HERMENEUTICS, *supra*, at 241, 246–49.

[203] FARBER & FRICKEY, *supra* note 114, at 23. For a comprehensive discussion of competing definitions of "ideology," *see* TERRY EAGLETON, IDEOLOGY: AN INTRODUCTION 1–31 (1991).

[204] *See* FARBER & FRICKEY, *supra* note 114, at 29; Rubin, *supra* note 138, at 29 (debunking public choice theorists' response to this critique).

ably make choices based on ideology and a combination of constituent and group interests, a combination related to re-election motives. All legislation is thus not the simple result of rent-seeking behavior.[205]

While no empirical or historical studies offer definitive proof, most of the Rules are probably not the result of rent-seeking. They are not, of course, free from political influence.[206] There was, for example, enormous political and economic interest in *Daubert*, generating an unusually large number of *amicus* briefs from interest groups.[207] Plaintiffs' trial lawyers urged the Court to adopt lax admissibility standards, promoting easier recovery in product liability suits.[208] Representatives of product manufacturers and doctors, fearing recoveries proven by novel or questionable techniques, argued for tougher admissibility standards.[209] Rules of evidence do, therefore, often affect political interests.

Political interests, however, probably did not dominate the drafting of the expert evidence Rules. In particular, when the Rules were drafted, "junk science" was simply not perceived as a problem.[210] Neither the Advisory Committee Notes nor other legislative history indicate a concern for this problem.[211] Indeed, the drafters sought to relax technical, traditional barriers to ex-

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[205] *See* Abner J. Mikva, *Foreword*, 74 VA. L. REV. 167, 167 (1988): ("The politicians and other people I have known in public life just do not fit the 'rent seeking' egoist model that the public choice theorists offer . . . .")

[206] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 27–29. For example, the debate over whether or not to permit impeachment of criminal defendants with prior felony convictions might, logic suggests, be viewed as a clash between prosecutorial and pro-defense interests. *See id.*

[207] *See* Docket, Daubert v. Merrell Dow Pharmaceuticals, Inc., 113 S. Ct. 2786 (1993) (No. 92-102) (listing amicus briefs by the American Insurance Association, Product Liability Advisory Council, Defense Research Institute, Inc., and the Association of Trial Lawyers of America).

[208] Brief of Association of Trial Lawyers of America as *Amicus Curiae* in Support of Petitioner, *Daubert*, 113 S. Ct. 2786 (1993) (No. 92-102).

[209] Brief of Product Liability Advisory Council, Inc., et al. as *Amici Curiae* in Support of Respondent at 5, *Daubert*, 113 S. Ct. 2786 (1993) (No. 92-102) ("The putative expert who offers to testify about issues of science without regard to the scientific method imperils the very foundation of rational decisionmaking."); Brief of the American Medical Association, et al. as *Amici Curiae* in Support of Respondent at 5, *Daubert*, 113 S. Ct. 2786 (1993) (No. 92-102) ("Recent history demonstrates that legal judgments based upon opinions not developed in accordance with scientific methodology have caused manufacturers to withdraw a number of safe and effective vaccines and drugs . . . from the market. Such legal judgments also have significantly stymied innovation in pharmaceutical and vaccine research.").

[210] *See* PETER HUBER, GALILEO'S REVENGE: JUNK SCIENCE IN THE COURTROOM (1992) (critiquing recent growth of "junk science" in trials).

[211] *See* FED. R. EVID. 702–06 advisory committee's notes; *see generally* BAILEY & TRELLES, *supra* note 153; Giannelli, *supra* note 68.

pert testimony.[212] While today this relaxation might be viewed as a victory of certain oppressed, often unorganized, groups, like plaintiffs in personal injury and civil rights suits, against monied interests, had such a battle been waged in the drafting there surely would have been a record of the struggle. No such record survives.[213]

The impetus for the Rules was indeed a concern for efficiency and clarity.[214] The articulated rationale was the incoherence, complexity and inconsistency of the common law.[215] The Rules were meant to simplify and rationalize federal evidence law, leaving trial judges discretion to individualize justice.[216] There were some interest group and ideological struggles over some Rules.[217] Nothing indicates, however, that these involved the Rules generally or that particular groups managed to dominate the process.

The generality of the Rules makes it difficult for particular interest groups or particular ideologies to triumph. Suppose the Rules were being considered for the first time today and a ma-

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[212] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 45.

[213] *See generally* BAILEY & TRELLES, *supra* note 153. Professor Kenneth Graham did argue that the Rules appeared to favor the "Establishment" by, for example, admitting business records of The Bank of America to prove it was owed money by consumers but excluding consumers' own, personal records to prove the opposite. Letter from Kenneth W. Graham, Jr. to the Committee on Rules of Practice and Procedure (July 28, 1971), *reprinted in* 3 BAILEY & TRELLES, *supra* note 153, at 195–96. But Professor Graham pointedly noted that he did not believe that the drafters intended this result. "Rather this was the inevitable result of the decision to preserve rules that were evolved in an era when the courts were viewed as protectors of the Privileged Classes and it was accepted as natural that rules should favor property rights over personal values." *Id.*

To the extent that the Rules fail to alter pre-existing inequalities in our society, they reflect our civil procedural system's "ideological" commitment to furthering dispute resolution among private parties without altering their relationship. *See* MIRJAN DAMASKA, THE FACES OF JUSTICE AND STATE AUTHORITY: A COMPARATIVE APPROACH TO THE LEGAL PROCESS 71–77, 140 (1986). While an objection to this pervasive commitment might be a call to a revolution in our procedural system, it does not demonstrate that, given that system, some rent-seeking groups prevailed over a broader conception of the public interest.

[214] Victor J. Gold, *Do the Federal Rules of Evidence Matter?*, 25 LOY. L.A. L. REV. 909, 909 (1992).

[215] *See* Preliminary Report of the Special Committee on Evidence, 30 F.R.D. 77, 77–79, 108–10 (1961); Proposed Rules of Evidence: Hearings Before the Subcomm. on Reform of Federal Criminal Laws of the House Comm. on the Judiciary, 93d Cong., 1st Sess. 90, 547 (1973) (testimony of Albert Jenner, Chairman of the Advisory Committee on Rules of Evidence and Edward Cleary, Reporter of the Advisory Committee on Rules of Evidence).

[216] Thomas M. Mengler, *The Theory of Discretion in the Federal Rules of Evidence*, 74 IOWA L. REV. 413, 458 (1989) ("[T]he Advisory Committee intended to give trial courts the maneuverability to craft its rulings to do individual justice.").

[217] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 27–29; *supra* note 213, and accompanying text (debate over felony impeachment and comments of Professor Graham).

jority of the Supreme Court and a majority of the members of Congress are "conservative," which I here define as "tough on crime" and favoring the interests of corporate America.[218] "Conservativism" may be both an ideological stance and reflect the support of interest groups or the electorate.[219] Under such circumstances, would the ruling elite choose a *Frye* rule or a *Daubert*-style reliability test? The *Frye* rule might favor corporate interests by making recovery in products liability suits more difficult. But the *Frye* rule also might frustrate prosecutor efforts to use novel techniques, like DNA-typing in its early days[220] or the application of the battered woman syndrome to lesbian lovers.[221]

On the other hand, a *Daubert*-style reliability test might damage corporate and prosecutorial interests in other cases. A corporate defendant in an antitrust suit could not introduce a novel theory devised solely for a particular case, and thus untested by peer review, to demonstrate limited market power. Similarly, some commentators interpret *Daubert* to exclude rape trauma syndrome testimony.[222] Thus "conservative" decisionmakers might favor a different test depending on the circumstances.

One might believe after *Daubert* that the conservative Court was uncertain what would favor conservative interests and therefore left trial judges discretion to make case-by-case adjustments.[223] But, since few evidence appeals reach the Su-

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[218] *Cf.* JEFFREY A. SEGAL & HAROLD J. SPAETH, THE SUPREME COURT AND THE ATTITUDINAL MODEL 243 (1993) (defining "criminal procedure conservatives" as opposing criminal accuseds and "economic conservatives" as supporting business, employers, and arbitration while opposing competition, liability, indigents, small businesses vis-a-vis big ones, debtors, bankrupts, consumers, the environment, and accountability).

[219] The generalist, trans-substantive nature of the Rules makes it unlikely that they will consistently serve a conservative agenda, except in the sense that any procedurally oriented rule will tend to conserve the status quo.

[220] There was a significant dispute over whether the particular techniques used for DNA-typing (as opposed to the theory that individuals have near-unique DNA) were generally accepted. *See, e.g.*, People v. Castro, 545 N.Y.S.2d 985, 999 (Sup. Ct. 1989).

[221] *See* Angela West, *Prosecutorial Activism: Confronting Heterosexism in a Lesbian Battering Case*, 15 HARV. WOMEN'S L.J. 249 (1992) (discussing case in which syndrome so used to aid the prosecution).

[222] *See* Faigman, AALS, *supra* note 188 (arguing that *Daubert* governs social science and that much social science is untested or inadequately tested and therefore excluded by *Daubert*).

[223] *See* Mark Kelman, A GUIDE TO CRITICAL LEGAL STUDIES 40–63 (1987) (describing some advantages and disadvantages of purported mechanical rules and more discretionary standards); Segal and Spaeth, *supra* note 218 (arguing that judicial attitudes, not interpretive theory, are the primary determinants of judicial behavior); Stephen A. Saltzburg, *Judicial Control of Scientific Evidence: The Implications of* Daubert, A.B.A., CRIM. JUS. SEC., EXPERT TESTIMONY: EVIDENCE, TRIAL ADVOCACY

preme Court, the Court cannot then fine-tune a conservative agenda.[224]

Had rent-seekers prevailed, the expert evidence Rules, and the Rules generally, would not have taken the form of broad, transsubstantive rules giving significant discretion to trial judges.[225] Instead, the Rules would have sought to codify the rent-seekers' victory to protect it from later re-interpretation. Those who challenge the Rules as the product of rent-seeking—rather than of a more public-regarding ideology— have not proven their case.[226]

Even if a rent-seeking theory predicts legislative behavior, it offers no effective interpretive theory.[227] It suggests that statutes are pernicious and their ill-intended effects will be achieved whether we comply with their literal meaning or with alternative indications of the intent of the rent-seeking groups. Public choice thus renders passage of legislation an essentially meaningless act.[228]

AND NEW DEVELOPMENTS 7 (Nov. 5, 1993) (describing *Daubert* as creating a system of guided judicial discretion).

[224] Giving discretion to a largely Republican-appointed trial judiciary maximizes the likelihood of a pro-conservative result. *See* Andrew I. Gavil, *Attitudinal Discretion and the Prospects for Reinvigorating Antitrust: A Look at the New Federal Rules*, 34 ANTITRUST BULL. 27 (1994) (arguing that assigning discretion to conservative Federal trial judges under the Federal Rules of Civil Procedure renders it likely that such discretion will work to plaintiffs' detriment in antitrust cases.).

[225] *See infra* text accompanying notes 348–366 (defending view that the Rules generally establish a system of guided discretion for trial judges); *cf. Proposed Deletion of Supersession Provision by the Rules Enabling Act Amendments of 1988: Hearings on H.R. 3152 Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary*, 100th Cong., 1st Sess., pt. 2, at 1260-61 (1988) (statement of Paul D. Carrington). Professor Burbank has suggested, on the other hand, that even general rules can be politically biased by, for example, having foreseeable disparate impacts. *See* Stephen B. Burbank, *The Transformation of American Civil Procedure: The Example of Rule 11*, 137 U. PA. L. REV. 1925, 1934–40 (1989). However, even if proven, intended disparate impacts might nonetheless be motivated by and serve the public interest. Moreover, while disparate impact might support amending a rule, it does not entail textualism, and, indeed, the more flexible approach argued for here allows a policy-sensitive court to minimize unfair disparity and individualize justice.

[226] For a discussion of the ideological and epistemological assumptions of evidence law and the process by which courts and juries socially construct facts, see generally WILLIAM TWINING, RETHINKING EVIDENCE (1990).

[227] *See* Rubin, *supra* note 138, at 16–19, 53.

[228] *Id.* at 54. Professor Rubin rejects the "legislative bargain" theory of statutory interpretation, which seeks to enforce the deal reached between competing rent-seeking groups where no single group has prevailed, because he believes this theory is based on public choice. *See id.* at 46. Yet that analysis overlooks practical politics, which suggests that even where legislation reflects a more public-regarding purpose, deals will have been struck by legislators seeking to reconcile competing visions of the public interest, as well as by those seeking to protect their chances for re-election, in order to muster a working majority. The difficulty of aggregating the private motivations of the various groups and legislators into a collective intent suggests that a search for the

A more useful approach recognizes that legislators act from a variety of motives, including both re-election and ideology.[229] Once ideology's role is acknowledged, legislative intent can be viewed as public-regarding and rent-seeking motivations lose importance, particularly in the context of the Rules.[230] While uncertainty regarding intent, the ability to define intent at varying levels of generality, the elusive nature of language, and the need to serve alternative values suggest that intent should not be a talisman, majoritarian values counsel significant weighing of relatively reliable indicators of intent.[231]

2. Arrow's Paradox Debunked

Furthermore, the conditions for the instability ("cycling") predicted by Arrow's Paradox often may not exist. If there are "unipeaked preferences," where all legislators agree in advance to a ranking of their preferences on a conservative-to-liberal scale, a stable, majority position not controlled by agenda-setting will result.[232] Stable majorities may also develop because political party members often share preferences and vote together.[233] Furthermore, the full Congress often adopts congressional committee proposals because the committees submit proposals they have previously determined can obtain majority support.[234] Additionally, stable, majority support for a bill is fostered by leg-

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"deal" may be an effective way to give collective intent meaning, without necessarily assuming that the deal is inimical to the public interest. *See infra* text accompanying notes 243–260.

[229] Rubin, *supra* note 138, at 57.

[230] *Id.* at n.201 (reviewing selected methods for distinguishing provisions resulting primarily from interest group pressures from those provisions reflecting the popular will or public-oriented deliberation).

[231] *See infra* text accompanying notes 336–347 (further discussing these concerns). Judge Posner has offered a different spin on this analysis. He argues that if the public choice theorists are right, then arguably we should favor a more pragmatic approach to statutory interpretation—one that achieves good consequences—rather than relying on the "evil" intent of the rent-seekers or their corrupt statutory text. *See* RICHARD POSNER, OVERCOMING LAW 400 (1995). Posner's only point was that public choice, even if correct, does not entail textualism, for he has acknowledged elsewhere that there is an important role for intentionalism in construing statutes. *See* POSNER, JURISPRUDENCE, *supra* note 110, at 270–78.

[232] FARBER & FRICKEY, *supra* note 114, at 48 (defining unipeakedness and its implications); STROM, *supra* note 124, at 14–19, 21–22 (accessible mathematical treatment of unipeakedness, which explains that outcomes under such conditions are unaffected by agenda-setting); Kenneth Koford, *Dimensions in Congressional Voting*, 83 AM. POL. SCI. REV. 949, 959 (1989) (conceding that 25–50% of votes are explained by a unidimensional scheme).

[233] FARBER & FRICKEY, *supra* note 114, at 49.

[234] STROM, *supra* note 124, at 90–91.

islative inertia. Legislators are unlikely to oppose legislation absent strong political capital or ideological reasons.[235]

Legislators would not view opposition to technical rules directed to lawyers and judges, proposed to rationalize evidence law after extensive study by experts, as politically advantageous. Such technical rules are unlikely to inflame ideological passions. Most members of Congress likely either substantially agreed with the committees' recommendations or deferred to the committees' superior knowledge.[236]

Where there was political capital to gain—by, for example, appearing "tough on crime"—there was significant debate and compromise.[237] In these instances, the Advisory Committee itself sought to modify proposals to respond to criticism and the need to garner support.[238] The give-and-take among the various constituencies and the lengthy hearings on the Rules[239] were inconsistent with simple agenda-setting.

Legislative debate does not simply reflect pre-existing preferences as public choice theorists assume. Rather, legislative debate molds and shapes such preferences.[240] The hearings on the Rules, the Advisory Committee Notes, and the reports of congressional committees indicate a deliberative, preference-shaping process rather than one resulting from agenda manipulation.[241] Because viewing legislation as only the result of agenda control is often misleading,[242] especially so here, the burden should lie with public choice theorists to demonstrate that manipulation underlay passage of the Rules.

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[235] *See* Interview with Elizabeth Holtzmann, former Congresswoman (D-N.Y.), in New York City, N.Y. (Jan. 15, 1994). This analysis follows logically from a public choice model. If the indebtedness of colleagues can be gained at low cost, there is every reason to do so. *Cf.* Rubin, *supra* note 138, at 28 (public choice theorists argue ideological voting will be greatest where its costs are lowest).

[236] *See infra* text accompanying notes 294–311, 348–366.

[237] *See, e.g.*, Taslitz, Daubert*'s Guide*, *supra* note 1, at 27–29. *Cf.* STROM, *supra* note 124, at 90 ("When a reported bill [from a committee] differs significantly from a position favored by a full chamber majority, the costs of formulating, offering, and passing on an amendment will not constrain this majority.").

[238] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 27–29.

[239] *See generally* BAILEY & TRELLES, *supra* note 153.

[240] *See* FARBER & FRICKEY, *supra* note 114, at 58–59.

[241] *See* 3–4 BAILEY & TRELLES, *supra* note 153.

[242] *See* FARBER & FRICKEY, *supra* note 114, at 58–59.

3. Group Intent and the Legislative Deal

One can view collective intent as a concept related to, but slightly different from, individual intent. As Justice Breyer has noted, we commonly ascribe group intent to group actions without practical difficulties.[243] Individual basketball players, for example, may have different reasons for stalling to "run the clock"—like instinct or imitation of teammates—but one still speaks sensibly of the group's goal.[244]

Recognizing that law does not result from a single action, but from various interacting activities, leads to deriving intention from a series of acts, emphasizing context and plans.[245] To ascertain a group's intent may require asking: "Of what type of plan would this action be a reasonable first step?"[246] This inquiry avoids ascribing a subjective motive to a group, yet remains consistent with both the common usage of "intent" as applied to groups and the sense that group activity is goal-oriented.[247] By focusing on a group's plan, as revealed by its context, action, and words, this inquiry enables us to determine group legislative intent for the Rules.

Individual members and subgroups of an enacting coalition with different motives nevertheless reach an often identifiable "deal." There are three primary groups involved in legislation: ardent supporters, ardent opponents, and moderates.[248] The ardent supporters pass their legislation only through compromise with the moderates.[249] The accommodations to satisfy the moderates reveal the legislative deal, which should be enforced.[250]

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[243] Stephen Breyer, *On the Uses of Legislative History in Interpreting Statutes*, 65 S. CAL. L. REV. 845, 864 (1992). Breyer uses "intent" to mean "purpose," not "motive," by which he presumably means group goals rather than individual motivations. *See infra* notes 273–291 and accompanying text for a discussion of other distinctions between intent and purpose.

[244] *Id.* at 865.

[245] BRIAN BIX, LAW, LANGUAGE AND LEGAL INDETERMINACY 187 (1993).

[246] *Id.*

[247] *See* Breyer, *supra* note 243, at 864–65; BIX, *supra* note 245, at 186–88. *Cf.* Nicholas Zeppos, *Legislative History and the Interpretation of Statutes: Toward a Fact-Finding Model of Statutory Interpretation*, 76 VA. L. REV. 1295, 1341–44 (1990) (arguing for pragmatic value of legislative intent, even if it has no "real" existence).

[248] *See* Barry R. Weingast, Matthew McCubbins, & Roger C. Noll, *Positive Canons: The Role of Legislative Bargains in Statutory Interpretation*, 80 GEO. L.J. 705, 711 (1992).

[249] *Id.*

[250] *Id.* at 711–12.

Green v. Bock Laundry Machine Co.[251] embodied this "legislative deal" approach. The "plain meaning" of original Rule 609 permitted impeaching civil *defendants* with felony convictions only after a weighing of probative value against prejudice, while allowing questioning civil *plaintiffs* about felony convictions with no discretionary balancing. However, the Court rejected that plain meaning as absurd, turning to legislative history.

The House majority, the "ardent supporters," had adopted a proposed version of Rule 609 that prohibited impeachment by prior convictions not crimen falsi.[252] The House version had been proposed by the House Judiciary Committee out of fear that allowing impeachment would deter accused criminals from testifying and would unfairly prejudice other witnesses.[253] The Senate majority, the "ardent opponents," were less concerned about the rights of criminal defendants and opted for a proposal that admitted *all* felony and crimen falsi convictions, without balancing.[254]

The choice was between two polar extremes: a flat bar on impeachment by felony convictions or an automatic right to such impeachment. The Conference Committee resolved this dispute by striking a deal.[255] Impeachment by felony convictions would be permitted if, but only if, the court determined that the probative value outweighed prejudice to the defendant. The Conference Committee Report clearly stated that the compromise sought to protect *only* the criminal accused;[256] neither the prosecution nor non-criminal-defendant witnesses were to be protected.[257]

This compromise became original Rule 609,[258] and the *Green* Court relied on this deal to conclude that Rule 609 guaranteed

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[251] 490 U.S. 504 (1989).

[252] For a more complete discussion, see Taslitz, Daubert*'s Guide, supra* note 1 at 27–29.

[253] H.R. Rep. No. 93-650, 93d Cong., 1st Sess., at 11 (1973).

[254] Taslitz, Daubert*'s Guide, supra* note 1 at 27–30.

[255] The comments of Representative Dennis reveal the difference between a legislator's individual motivations and the importance of focusing on the legislative deal: "In conference, we came up with a compromise which does not suit me 100 percent, but which is a slight advance over the present law. It is the best we thought we could do . . . ." 120 Cong. Rec. 40894 (daily ed. Dec. 18, 1974) (Statement of Rep. Dennis). *See also* Foster, 57 FORDHAM L. REV. 1, 8 (1988) ("This rule emerged in its present form as a deliberate, yet uneasy compromise between opposing positions in a sharply divided Congress.").

[256] *See* H.R. Conf. Rep. No. 93-1597, 93d Cong., 2d Sess., at 9–10 (1973).

[257] *Id.*

[258] 490 U.S. 504, 520 (1990).

the opportunity to impeach civil witnesses with prior non-crimen falsi felony convictions, without balancing.[259]

Thus the "deal approach" gives real definition to the concept of legislative intent. Of course, because many of the Rules were adopted without modifications, there may be no legislative deal to divine. Still, Congress may have adopted deals already reached among members of the Advisory Committee, whose views are often well-presented in the Committee's Notes.[260]

4. Imaginative Reconstruction

For many issues, however, there was no legislative deal to divine because the legislature had not even thought about the question before the Court. Judge Richard Posner has suggested resolving this problem by "imaginative reconstruction." Under this theory, one examines the values and concerns of the legislators who enacted a law and asks: "What would they have chosen had they been faced with this problem?"[261] The most sophisticated version of this approach considers both the prob-

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[259] *See id.* at 520–25 (reciting additional reasons, not immediately relevant to this discussion).

[260] *See infra* notes 292–311 and accompanying text (arguing that Congress generally intended to adopt the views of the Advisory Committee). Sometimes, the deal, if there was one, is not easily discernible from the Advisory Committee Notes. For example, those Notes reflect differing definitions of "habit." *See* RONALD CARLSON, ET AL., EVIDENCE IN THE NINETIES: CASES, MATERIALS, PROBLEMS 468 (3d ed. 1991). This may mean that the Committee could not reach agreement on the issue. Mengler, *supra* note 216, at 416. Alternatively, it may mean that the Committee meant for trial judges to have the discretion to choose between two definitions. *Id.* at 417. Either way, defining habit requires an inquiry beyond the deal specifically reached regarding Rule 406, such as the overall purposes sought to be achieved by the Rules. *See id.* at 425. Thus, a narrow conception of intention as limited to what legislators actually contemplated is unworkable.

[261] *See* Eskridge & Frickey, *supra* note 110, at 329–32 (characterizing Posner's approach). In Posner's latest version of imaginative reconstruction, he analogizes statutory interpretation to a military subordinate's trying to decipher the incomplete or garbled message of his superiors. POSNER, JURISPRUDENCE, *supra* note 110, at 273. This analogy assumes that the commander had a relevant, complete message that he wanted to communicate—that he had an "actual" intent about the matter in dispute. The process of imagining what that actual but garbled or unstated intent must have been is the same as assuming no intent, no previous consideration of the question by Congress, and then imagining what Congress would have intended had they thought about the matter. In other words, divining an existing but unknown actual intent collapses into divining a speculative intent had Congress thought about and addressed the matter. Both processes constitute imaginative reconstruction as Eskridge & Frickey, *supra* note 110, at 329–32, recognize. *See also* ESKRIDGE, DYNAMIC INTERPRETATION, *supra* note 3, at 125 (the relational contract, which establishes an ongoing relationship between parties over time, is a better analogy than the platoon commander because a relational agent understands that "her primary obligation is to use her best efforts to carry out the general goals and specific orders over time.")

ability and consequences of taking a particular position.[262] The advantages of this approach are legitimacy, since the legislative will is controlling, and flexible adaptation to modern conditions.[263] Because this approach makes counterfactual assumptions, however, it magnifies the problems of intent-based statutory interpretation, particularly the danger that an interpreter may invent an "intent" to cover his own agenda.[264] Nevertheless, imaginative reconstruction tries to understand the problem facing the enacting legislature and the changed circumstances facing the court.[265]

United States v. Owens[266] is an example of imaginative reconstruction. *Owens* involved Rule 801(d)(1)(C)'s hearsay exemption for prior statements identifying a person where the declarant testifies at trial and is "subject to cross-examination" about the statement.[267] The *Owens* Court had to decide whether an assault victim was "subject to cross" under that Rule where he had no memory at trial of whether he had seen his assailant, nor a memory of whether his earlier hospital bed identification of his assailant was prodded by hospital visitors. The Rule did not define the word "subject," and neither the Rule nor its legislative history directly addressed it. There was no evidence, therefore, that Congress, the Supreme Court, or the Advisory Committee had ever expressly considered the question. Nevertheless, the Court found that the amnesiac was "subject to cross" within the meaning of the Rule. In effect, the Court asked, "Had the enacting Congress considered this issue, what would they have done?"[268]

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[262] *See* FARBER & FRICKEY, *supra* note 114, at 102–06.

[263] *See* POSNER, JURISPRUDENCE, *supra* note 110, at 269–73.

[264] *See* Eskridge & Frickey, *supra* note 110, at 330 (explaining that "Judge Posner's theory is indeterminate because it often asks counterfactual questions of a long-departed legislature."); POSNER, JURISPRUDENCE, *supra* note 110, at 274 (noting danger in some versions of imaginative reconstruction that "the line between interpretation and policy making will disappear altogether . . . .").

[265] *See* E.D. HIRSCH, JR., *Counterfactuals in Interpretation*, in INTERPRETING LAW AND LITERATURE 55 (Sanford Levison & Steven Mailloux eds., 1988), for a superb defense of using counterfactual, imaginative reconstruction in both literary and legal interpretation.

[266] 484 U.S. 554 (1988).

[267] FED. R. EVID. 801 (d)(1)(C).

[268] That the Court did not attempt a new textualist's approach is clear. The dictionary defines "subject," when used as a verb, as "to bring under control or dominion," or "to make liable: PREDISPOSE," or "to cause or force to undergo or endure (something unpleasant, inconvenient, or trying) . . . ." WEBSTER'S NINTH COLLEGIATE DICTIONARY 1174 (1988). Forcing a crime victim to endure questioning by a defense attorney designed to reveal the victim's flawed memory is literally "subjecting" the victim to cross. The Court instead used the meaning ordinarily given the phrase "subject to cross"

The Court used both text and legislative history to imagine likely congressional intent. Although the Court seemed to consider *actual* legislative intent, there clearly was no such intent.

Thus the Court looked to the language of a different rule, Rule 804(a)—defining unavailability as including "a lack of memory of the subject matter of the declarant's statement"[269]—as showing that Congress had indeed thought about forgetful witnesses. Therefore, concluded the Court, because Congress chose not to exclude them from Rule 801(d)(1)(C)'s exemption, that exemption covered forgetful witnesses too.

But demonstrating that Congress considered the possibility of forgetful witnesses in Rule 804(a)'s definition of unavailability,[270] does not mean they considered it under Rule 801. The *Owens* Court's inference of intent in Rule 801, based upon Rule 804's reference to forgetfulness, was thus merely informed speculation, or counterfactual imagination, not archaeological discovery of intent.

Similarly, the Court discussed the Advisory Committee's Note to Rule 801, which revealed only the broad purposes of the Rule's drafters: to favor pre-trial identifications over trial identifications since witness memory is more reliable when probed closer to the time of the incident.[271] This, the Court concluded, supported the idea that the presently forgetful witness's earlier, pretrial identification should be admitted. But to conclude that Congress actually contemplated admission of a prior identification from a total amnesiac who could not vouch in any way for the reliability of his earlier statement is mere fantasy. Instead, the broad goals of Congress served as a guide to determine what Congress would have wanted had it confronted the *Owens* issue, again an exercise in imaginative reconstruction.

The Court's exercise involved the more sophisticated version of imaginative reconstruction, however. Apparently recognizing that several intents can be imagined at various levels of generality, the Court chose its version of intent by evaluating the consequences of its choice. An intent to include testimony like

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by courtroom actors, which requires truly meaningful questioning. *See* 484 U.S. at 562. For a fuller description of *Owens'* attitude toward textualism and its less than candid claims to finding an actual, rather than an imagined intent, see Taslitz, Daubert*'s Guide*, supra note 1, at 17–20.

[269] FED. R. EVID. 804(a).

[270] *Id.*

[271] *Id.*

that of the victim in *Owens* would not, in the Court's view, undermine "meaningful" cross.[272] Where meaningful cross is available, no untoward consequences result from the Court's imagined congressional intent.

The Court analyzed the practical consequences of its decision unrealistically, however, imbuing cross-examination with an almost supernatural power to undermine direct examination. But its approach, its effort at imaginative reconstruction, was a sound first step toward interpreting the Rules.

5. Purposivism

Imaginative reconstruction, of course, has its limits, for there may often be so little relevant evidence of legislative intent as to make it impossible to hazard even an educated guess regarding what Congress would have wanted done in a particular case. Hart and Sacks sought to solve this problem by suggesting a more flexible version of imaginative reconstruction.[273] They believe judges should assume that legislators were reasonable persons intending reasonable results in the public interest.[274] Courts should therefore determine the plausible objectives the legislature sought, then interpret the statute to best carry out those objectives.[275]

But determining plausible legislative objectives requires understanding the problems the enacting legislature faced and how the statute tried to solve them.[276] This, in turn, requires examining the statements of legislative committees and bill sponsors to understand how prior law failed to solve a problem.[277] This purposive approach differs from a simple "intent" approach because

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[272] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 17–20.

[273] *See generally* HENRY M. HART, JR. & ALBERT M. SACKS, THE LEGAL PROCESS: BASIC PROBLEMS IN THE MAKING AND APPLICATION OF LAW (tent. ed. 1958). *See also* POSNER, JURISPRUDENCE, *supra* note 110, at 274 (describing Hart and Sacks' approach as a version of imaginative reconstruction).

[274] HART & SACKS, *supra* note 273, at 1414–15 (tent. ed. 1958) (asserting that "A court should put itself in imagination in the position of the legislature which enacted the measure . . . . [and assume] that the legislature was made up of reasonable persons pursuing reasonable purposes reasonably.").

[275] *Id.* at 1200.

[276] *See* CARTER, *supra* note 167, at 84.

[277] *Id.* at 86–87. Hart and Sacks' original formulation of the purposive approach was apparently more distrustful of legislative history than the formulations of other purposivists, like Lief Carter, *see id.*, for Hart and Sacks cautioned that legislative history should be consulted last and only to help in choosing among plausible purposes. *See* HART & SACKS, *supra* note 273, at 1284–86.

it examines evidence beyond legislative history in order to understand the problem and its attempted solution. Such evidence might include competing social policies and social history.[278] Legislative history may, however, be particularly important if it is necessary to select the most likely intent from among numerous, perhaps conflicting, purposes.[279]

Purposivism obviously conflicts with public choice theory. But the most extreme version of public choice teachings is not tenable.[280] This is especially true for the Rules, which, while subject to the rent-seeking efforts of some interest groups, had a real, public-regarding purpose.[281] While purposivism has other flaws,[282] it focuses on statutory context and permits evolution of the law in the face of changing conditions.[283] That this arguably invites judicial policymaking should not be a major concern under the Rules, however, because the Rules were largely designed to invite such policymaking within the broad objectives set by Congress.[284]

Imaginative reconstruction in its narrower sense was not available as a technique in *Daubert*, where the Court held that a "relevancy and reliability" test embodied in the Rules, including especially Rule 702, superseded the common law *Frye* general acceptance test for scientific evidence.[285] The Advisory Commit-

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[278] *See id.* A similar approach acknowledges that legislative intent concerning a particular problem either does not exist or cannot be discovered and, therefore, seeks to advance the policies that furnish the best political justification for the statute. *See* DWORKIN, LAW'S EMPIRE, supra note 175, at 326–27, 329–31. This approach is an unabashed judicial statement of political morality. *Id.* at 329. It abandons any pretense of connection to legislative intent but involves the court in essentially the same process as does a purposive interpretation. *See id.* at 316–31 (defending and applying such an approach to the Civil Rights Act of 1964).

[279] *See* HART & SACKS, *supra* note 273, at 1201.

[280] *See supra* text accompanying notes 202–242. *But see* Zeppos, *supra* note 247, at 1332 (asserting that textualism causes statutes to be construed narrowly, thereby decreasing the legislature's power and frustrating the objective of public choice theory); Macey, *supra* note 115, at 250–68 (attempting to justify purpose approach but for public choice reasons).

[281] *See supra* text accompanying notes 202–231.

[282] Purposivism may make unrealistic assumptions and suffers from indeterminacy and the need to serve competing values. *See* Eskridge & Frickey, *supra* note 110, at 358. Yet, if, as this Article and others have argued, *see, e.g.*, DWORKIN, LAW'S EMPIRE, *supra* note 175, at 329, indeterminacy is unavoidable, then some of these objections have less force.

[283] Eskridge & Frickey, *supra* note 110, at 350–51.

[284] *See infra* text accompanying notes 312–377. There is a powerful constraint on judicial policymaking: to avoid a legislative override, the Court often seeks interpretations consistent with the will of the present Congress. *See* ESKRIDGE, DYNAMIC INTERPRETATION, *supra* note 3, at 69, 75, 79, 151.

[285] *See* Taslitz, Daubert's *Guide*, *supra* note 1, at 46–50, 56–68.

tee Note on Rule 702 was skimpy, and there was no other written legislative history.[286] Indeed, the strongest argument that *Frye* was not meant to be overturned by Rule 702 came from the deafening silence of the Rule and the legislative history. Some argued that Congress would not have intended to change the long-standing *Frye* rule without expressly saying so.[287] Although the Court presented its analysis as a textual one, its analysis of text in fact involved a complex, policy-driven choice of interpretive communities, a use of text that new textualists would not understand.[288]

Moreover, despite its protests to the contrary, the Court went far beyond anything that could be read into Rule 702's text.[289] The absence of legislative history from which to reconstruct likely congressional intent—and the likelihood that Congress probably never even considered the *Frye* question[290]—made the case appropriate for a purposive analysis. Indeed, without saying so, this is precisely what the Court did. The Court identified Congress's purpose as ensuring the reliability of scientific evidence while recognizing the Rules' preference relative to the common law for admissibility and trust of the jury. To determine how to achieve that purpose, the Court examined the nature of science, for only then could it understand what problem faced Congress and how a solution might be crafted to solve that problem. The Court rejected *Frye* as a solution incompatible with part of the congressional purpose—the preference for admissibility and trusting the jury—and instead crafted a more flexible, multi-factor test more likely to achieve Congress's goals. The Court also gave trial judges significant discretion in applying this new test, consistent with another congressional purpose: giving trial judges discretion in reading and applying the Rules.[291]

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[286] *See id.* at 56.
[287] *See id.* at 59.
[288] *See id.* at 62–63.
[289] *See id.* at 56–68.
[290] *See* Giannelli, *supra* note 68, at 1999, 2009. Professor Mengler has argued, however, that the silence of the Advisory Committee and the Rules themselves demonstrate an intent that trial judges have discretion whether to apply *Frye*. Mengler, *supra* note 216, at 448–49.
[291] *See infra* text accompanying notes 348–366.

G. *Identifying Collective Intent*

Given that some legislative intent useful to courts exists, how can we identify it? The most important source other than text is legislative history. The most available sources are Advisory Committee Notes and congressional committee reports. Courts frequently refer to both these sources as do professors teaching evidence courses.[292] Public choice theorists criticize reliance on committee reports, however, arguing that they do not necessarily reflect the views of the majority of Congress and may reflect strategic behavior. Rent-seeking minorities may plant positions in the legislative history, hoping courts will later rely on these positions.[293]

Recent public choice scholarship demonstrates, however, that the success of committee positions in the full chamber is not the result of agenda control. Instead, committees generally succeed because they are adept at identifying positions likely to be supported by a majority of the full chamber.[294] Consequently, while some committee reports may be suspect, there is often good reason to give committee reports substantial weight, especially where the reports are consistent with statutory language and purpose.[295] Furthermore, staff members monitor statutes and reports and propose modifications to bridge gaps between the language and their members' goals.[296] They alert members to significant substantive and political concerns and seek their guidance on how to proceed.[297]

House or Senate committee reports concerning the Rules would therefore likely reflect any disagreements with the Rules' Advisory Committee on significant matters. Where there is no expressed disagreement, the congressional committee can fairly be presumed to have meant to agree with the Advisory Committee. But, because they likely reflect majority sentiments, the views of the congressional committees, where no changes were made by the full chamber, should be given significant weight. Further-

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[292] *See, e.g.*, CARLSON, *supra* note 31.

[293] In response to the public choice critique, Farber and Frickey argue that legislators do concentrate on the text of committee reports and that the competitive interaction of interest groups prevents the use of legislative history for blatantly subversive reasons. *See* FARBER & FRICKEY, *supra* note 114, at 95–102.

[294] STROM, *supra* note 124, at 125.

[295] *See* FARBER & FRICKEY, *supra* note 114, at 101.

[296] Breyer, *supra* note 243, at 858.

[297] *Id.*

more, where the two chambers disagreed, the Conference Committee Report likely reflected the views of a majority of the whole Congress, as embodied in the legislative deal, a situation illustrated by the reference to the Conference Committee Report in *Green v. Bock Laundry Co.*[298]

Legislators know the general purpose of a bill but rely on committee members for the details, particularly technical ones, as in the Rules, often adopting committee members' views on those details as their own.[299] Consequently, even if the majority of Congress never considered the wisdom of the details of the Rules (that "relatively inconsequential" piece of legislation),[300] there is still reason to defer to the committee reports. This supports reliance on the chamber committee reports where they disagree with the Advisory Committee, but reliance on the Advisory Committee Notes absent such disagreement.[301]

Conflicting legislative history will only sometimes create a problem. First, such a conflict may be rare,[302] particularly under the Rules, for where the Advisory Committee and the Congress disagreed, the history should show which view prevailed and why.[303]

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[298] 490 U.S. 504 (1989). *See* Taslitz, Daubert*'s Guide*, *supra* note 1, nn.142–51. While most of the *Green* Court's analysis focused on the legislative deal, the Court's conclusion that Congress did not intend for Rule 403 to govern civil witnesses covered by Rule 609 was based on a textual analysis. 490 U.S. at 524–26. The Court ignored other indications of legislative intent or purpose that may have required a contrary result. *See* WEISSENBERGER, EVIDENCE, *supra* note 164, at 1337–38.

[299] FARBER & FRICKEY, *supra* note 114, at 101.

[300] *Green*, 490 U.S. at 528 (Scalia, J., concurring).

[301] Where the Advisory Committee Notes are silent or ambiguous, the extensive hearings on the Rules or the writings of Committee members prior to the Rules' adoption may help. This poses risks, however, because the statements of an individual may not represent the views of an entire committee. *See infra* notes 306–307 and accompanying text (discussing hierarchy of legislative history). Nevertheless, the comments may help where consistent with the Advisory Committee Notes, the language, structure, and history of the Rules, and the comments of the other Committee members. *See* Mengler, *supra* note 216, at 437–54. *See also* HART & SACKS, *supra* note 273, at 1285–89 (manipulation of legislative history can be accounted for by giving the comments of individual legislators weight "only to the extent that the application envisaged fits rationally with other indicia of general purpose"); FARBER & FRICKEY, *supra* note 114, at 101 ("[W]hen a fundamental aspect of legislative history, like a committee report, is unimpeached by other sources and is consistent with the apparent political equilibrium, it should be an important interpretive source.").

[302] *See* Breyer, *supra* note 243, at 862 ("[The] workload [of the federal courts of appeals] includes many unclear statutory provisions where lack of clarity does *not* reflect major political controversy. Such cases usually do not involve conflicting legislative history . . . .").

[303] *See, e.g.*, Taslitz, Daubert*'s Guide*, *supra* note 1, at 27–32 (discussing history of Rule 609).

Second, where there is a conflict between, for example, the House and Senate committee reports, with no subsequent change in textual language and thus no conference committee report, the conflict can sometimes be resolved by determining which position is most consistent with the language of the Rule and most effectively cures the problem to which the Rule was addressed.[304] Where there is such a conflict, however, courts should place less weight on the legislative history and a greater emphasis on other guides to statutory interpretation.[305]

Other sources of legislative history may be entitled to less weight. Floor debates, unlike committee reports, may reflect the views of only individual members of Congress.[306] Nevertheless, comments by a bill's primary sponsor merit greater weight because the sponsor is familiar with the purposes of the legislation and other members tend to rely heavily on the views of sponsors in deciding what legislation means and how to vote.[307]

All legislative history provides context, shedding light on the legislation's purposes, goals, approaches, and deals ultimately reached.[308] It can be evaluated critically and ranked in order of persuasiveness.[309]

Where the legislative history is silent on a particular point, the history at least provides context.[310] The Advisory Committee Notes and committee reports help narrow the relevant intentions or purposes and often reveal a single, clear legislative intention.[311]

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[304] *See, e.g.*, Taslitz, Daubert*'s Guide, supra* note 1, at 23–27 (noting that Beech Aircraft Corporation v. Rainey, 488 U.S. 152 (1988), took a similar approach to resolving conflicting legislative history under Rule 803(8)(C)).

[305] *See* Breyer, *supra* note 243, at 862 ("If the history is vague, or seriously conflicting, do not use it."); *infra* text accompanying notes 336–347.

[306] *See* Eskridge, *The New Textualism, supra* note 4, at 639. Eskridge describes the following hierarchy of legislative history, moving from most to least authoritative, as implicit in the Court's decisions: (1) committee reports, (2) sponsor statements, (3) rejected proposals, (4) floor and hearing colloquy, (5) views of nonlegislator drafters, (6) legislative inaction, and (7) subsequent legislative history. *Id.* at 636.

[307] *See id.* at 637–38.

[308] *See supra* text accompanying notes 243–291.

[309] *See, e.g.*, Eskridge, *The New Textualism, supra* note 4, at 689 ("At the very least, the new textualists urge a more critical use of legislative history, and I join their call, based upon the realist problems with legislative history in many cases.").

[310] *See* Taslitz, Daubert*'s Guide, supra* note 1, at 17–20, 23–32.

[311] *See Owens* 484 U.S. at 562–63 (1981) (advisory committee notes and congressional committee reports effectively used to identify legislature's goals); *Beech*, 488 U.S. at 164–68 (various reports revealed conflicting intentions but gave Court guidance for choosing between those intentions); *Green*, 490 U.S. at 513–24 (single clear intention revealed from various reports regarding one issue before the Court).

H. *Practical Reasoning*

Discussions of statutory interpretation often imply that a single "grand theory" must control how to read a statute, focusing either on the words of the text, the intent of the legislature, or the purpose of the legislation.[312] Yet these calls for a grand theory contrast sharply with the practices of lawyers, who tend to rely on fact-based reasoning.[313] Judges, too, eschew a single, controlling theory.[314] A judge must compare incommensurables, weigh conflicting forms of evidence, pursue multiple goals, deal with uncertainty, and, within the constraints of the law, seek justice. These tasks cannot be accomplished well by application of grand theory:

> Judges are disciplined by the specificity of the cases they must decide, and this discipline not only puts a limit to the speculative theorizing in which they may engage, but is also bound to remind them, as they go about their work, of the value of deliberative wisdom—the wisdom that consists in a knowledge of particulars and that no general theory can provide.[315]

This emphasis on practical wisdom or practical reason has its roots in Aristotelian thinking: what is right in the particular case can be determined without a universal theory of what is right.[316]

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[312] *See* Eskridge & Frickey, *supra* note 110, at 321–22.

[313] *Id.* at 321.

[314] Eskridge & Frickey, *supra* note 110, at 321–22 ("Judges' approaches to statutory interpretation are generally eclectic, not inspired by any grand theory, and this is a good methodology."); *cf.* RONALD DWORKIN, A MATTER OF PRINCIPLE 319–20 ("There is no agreement about theories of legislation among American judges . . . .").

[315] ANTHONY T. KRONMAN, THE LOST LAWYER: FAILING IDEALS OF THE LEGAL PROFESSION 318–19 (1993). See also DAVID LUBAN, LEGAL MODERNISM (1994) (debunking "grand theory" and advocating a more pragmatic and humanistic view of law as narrative).

[316] *See* ARISTOTLE, *supra* note 110; *see* RONALD BEINER, POLITICAL JUDGMENT 72–82 (1983). When Professor Kronman wrote of "practical wisdom," he did not have statutory interpretation in mind. Rather, he wrote of the ideals that should shape legal practice. *See generally* KRONMAN, *supra* note 315. But his analysis of "practical wisdom" was rooted in Aristotle's NICHOMACHEAN ETHICS, *see id.* at 41–46, as is the approach to "practical reasoning" in statutory interpretation favored in this Article. *See also* Scallen, *supra* note 112, at 4–22 (tracing Aristotelian roots of practical reason in interpreting the Rules). Both Kronman's approach and that advanced here emphasize fact-specific, ad hoc reasoning, reasoning not limited by the demands of any single theory.

Kronman is, however, a proponent of "practical reason" in another related sense; he argues, in the manner of what Richard Posner derisively calls "neotraditionalism," that law is an autonomous discipline from other disciplines and that a reliance on the traditional modes of legal reasoning is desirable. POSNER, JURISPRUDENCE, *supra* note 110, at 71, 433–53. But practical reasoning as ad hoc reasoning, or, giving it Judge

This Aristotelian theme is found today in both hermeneutics and American pragmatism, which emphasize the "concrete situatedness of the interpretive enterprise"[317] and that different values will pull an interpreter in different directions.[318] Practical reason recognizes that we must ultimately rely on the good judgment of those best able to make a decision.[319] And good judgment, in turn, is partially a trait of character.[320]

That judicial decisionmaking involves character and intellect should not cause despair, nor lead us to assume that we are subject to the whims of judicial temperament. First, this recognition enables a more effective approach to improving judicial decisionmaking, precisely because it is more realistic. Professor Tushnet has made this point in the context of constitutional decisionmaking, demonstrating that even though the Justices often articulate grand theories of constitutional interpretation to justify their decisions, a close examination of their opinions reveals that they were motivated by more than those theoretical concerns.[321] The theories instead served as rhetorical devices used to justify decisions reached on other grounds.[322]

This need not mean, however, that the Justices lie, deciding upon their personal preferences, rather than "the law." Instead, it may reflect their recognition that they must exercise judgment,

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Posner's slightly different spin, as reasoning about matters that cannot be verified solely by logic or exact observation, *id.* at 71–72, need not ignore other disciplines nor be bound entirely by traditional legal reasoning, *see* KRONMAN, *supra* note 315, at 360, nor give judges unbounded discretion. *See infra* text accompanying notes 348–366. It does, however, logically require that no single theory, including the theories of other disciplines, control judicial decisionmaking. It is Kronman's focus on flexible, case-specific reasoning that matters here, not who is right in the Kronman-Posner debate about whether law is (Kronman's position) or is not (Posner's position) an autonomous discipline. *Compare* KRONMAN, *supra* note 315, at 362, *with* POSNER, *supra* note 110, at 423–24.

[317] Eskridge & Frickey, *supra* note 110, at 323. "Pragmatism" underpins the modern Legal Realist Movement. *Compare* ROGER COTTERRELL, THE POLITICS OF JURISPRUDENCE: A CRITICAL INTRODUCTION TO LEGAL PHILOSOPHY 185 (1989) *with* William W. Fisher III & Morton J. Horwitz, *Introduction* to AMERICAN LEGAL REALISM xiii–xiv (William W. Fisher III & Morton J. Horwitz eds., 1993). "In an orthodox pragmatist conception knowledge is 'true' to the extent that it is useful . . . ." COTTERRELL, *supra*, at 185.

[318] Eskridge & Frickey, *supra* note 110, at 323–24.

[319] *See* KRONMAN, *supra* note 315, at 41.

[320] *Id.*

[321] Mark Tushnet, *Constitutional Interpretation, Character, and Experience*, *in* CONTEMPORARY PERSPECTIVES ON CONSTITUTIONAL INTERPRETATION 208, 217 (Susan J. Brison & Walter Sinnott-Armstrong eds., 1993).

[322] *See id.* at 221 ("I no longer believe that constitutional theory constrains, or is supposed to constrain judges. Rather, as Bobbit argued, it serves primarily to provide a set of rhetorical devices that judges can deploy as they believe effective.").

that no single theory can accomplish what good judgment can do, and that judgment requires a weighing of considerations not subject to any mechanical, purely objective test. The Justices may turn to theory because they fear that admitting the indeterminate nature of their enterprise will undermine their legitimacy.[323] But, as discussed below, their fear is unfounded: a candid admission of what they are really doing will likely promote greater legitimacy and better decisionmaking.[324] Tushnet himself recognized this: "[a]s we gain a better grasp of the judge's character, we may become more willing to accept his or her exercise of judgment."[325] Others agree.[326] No matter what theory judges purport to adhere to, their attitudes, values, and experiences—the qualities that make up their "character"—will affect their decisions.[327] Likewise, a single grand theory of statutory interpretation does not permit the Court to admit the unavoidable role of values, experience, and history in its judgment and merely invites it to develop an inconsistent and transparent jurisprudence that will not inspire trust. Because the Court would have to confront neither itself nor the public with the true bases of its decisions, its decisions might decline in quality.[328] A more flexible, dynamic approach to statutory interpretation would solve these problems.[329]

Second, that character and judgment play roles in decisionmaking, and that there is rarely, if ever, one indisputably "correct" answer to a legal question, does not mean that laws do not

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[323] *See infra* text accompanying notes 367–377.

[324] *See infra* text accompanying notes 367–377.

[325] Tushnet, *supra* note 321, at 227.

[326] *See infra* notes 372–377.

[327] *See* Tushnet, *supra* note 321, at 221–27; SEGAL & SPAETH, *supra* note 218.

[328] *See infra* text accompanying notes 367–377. One commentator defends the necessity for judicial value choice in textual interpretation:

> [I have demonstrated] the lengths the court[s] will go to in order to disguise their reasons even from themselves. The Critical Legal Studies Movement tends to see this creative use of rhetoric as nugatory; a better way to see it is as a less than candid but *nevertheless moral* effort to continue to justify the law by the retroactive application of theory to results.

FREDERIC G. GALE, POLITICAL LITERACY: RHETORIC, IDEOLOGY, AND THE POSSIBILITY OF JUSTICE 148 (1994) (emphasis added).

[329] Such a dynamic approach to law has its roots in the early 20th-century "Legal Realism Movement." This movement teaches the importance of empiricism, skepticism about the power of "paper rules" divorced from human motivations, an impatience with narrow doctrinal reasoning, an insistence upon the lawmaking power of judges, and an aspiration to expose the ambiguities in and ideological functions of the law. *See* Fisher & Horwitz, *supra* note 317.

restrain judges.[330] To the contrary, close examination of the Justices' decisions demonstrates that at least some Justices in some cases do change their votes based upon *legal* arguments.[331] Even Tushnet admits that grand theory in constitutional law has provided "a broad framework within which the justices concluded that they could exercise sound judgment."[332] Justices at least sometimes recognize institutional constraints on their behavior and act accordingly.[333] And they at least sometimes try to reach a just decision, not necessarily the one they personally "like" based upon their natural prejudices.[334] But an expanded conception of doctrine that allows for the interplay of the complex forces that affect all judges' decisions will more realistically depict what the Court is really doing and perhaps thus force the

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[330] *But see* SEGAL & SPAETH, *supra* note 218. Professors Segal and Spaeth argue that judges make all decisions based on their own attitudes. Yet even they concede that attitudes described as "liberal" or "conservative" do not explain all the Justices' votes. *Id.* at 220, 228. Second, case studies have demonstrated that some Justices change positions based on legal argument, "influenced by factors other than personal ideological preferences." LEE EPSTEIN & JOSEPH KOBYLKA, THE SUPREME COURT & LEGAL CHANGE: ABORTION AND THE DEATH PENALTY 4 (1992). Third, they argue that the Justices do vary votes based on facts, but contend that attitudes, not legal theories, interact with the facts. SEGAL & SPAETH, *supra*, at 220–21. They concede, however, that a fact-based theory is consistent with both an attitudinal and a legal model. *Id.* at 362 n.16. Fourth, they do not consider that a conscious effort by the Court to identify and articulate its values may change some Justices' positions in some cases and may increase the impact of public perceptions of decisions on those decisions. Fifth, they concede that the attitudinal model is not a guide for judges. *Id.* at 362–63. The model offered here attempts to provide a guide. Indeed, Professors Segal and Spaeth acknowledge that non-attitudinal factors may have more of an impact on lower court judges, although little research has been done, suggesting that a normative model matters more for those judges. *Id.* at 358. Sixth, evidence decisions may defy "liberal" or "conservative" labels, and an attitudinal model may not work. *See supra* text accompanying notes 202–226.

[331] *See generally* EPSTEIN & KOBYLKA, *supra* note 330 (tracing the Court's treatment of abortion and the death penalty and showing how Justices changed their positions on these issues based upon the quality, or lack thereof, of the legal arguments). *See also* GEORGE P. FLETCHER, LOYALTY: AN ESSAY ON THE MORALITY OF RELATIONSHIPS 113 (1992) (the Court's treatment of freedom of religion changed because "[t]hree Justices, Black, Douglas, and Murphy, underwent a major conversion in their thinking about the rights that should be enjoyed by 'small and helpless minorities.'"); RONALD KAHN, THE SUPREME COURT AND CONSTITUTIONAL THEORY 1953–1993 (1994) (debunking the "political" approach of social scientists like Spaeth and Segal in favor of a "constitutive" approach—emphasizing polity and rights principles, precedent and constitutional law as better explaining the data).

[332] Tushnet, *supra* note 321, at 209.

[333] Thus, even an "activist" Justice like Thurgood Marshall declared that "ninety-nine and forty-four one hundredths of the time" he decided cases based on precedent, although he emphasized that "there's no precedent that binds me unalterably." CARL T. ROWAN, DREAM MAKERS, DREAM BREAKERS: THE WORLD OF JUSTICE THURGOOD MARSHALL 390 (1993).

[334] *See id.* at 390:

Court to confront criticism based on its true motivations.[335] A theory of statutory interpretation that recognizes the complexity of factors in judicial decisionmaking is preferable to the single-minded approach of grand theory.

By now it should be clear that no one approach to statutory interpretation makes sense. Each approach has strengths and weaknesses. A "practical reason" based approach to statutory interpretation includes all the considerations discussed above—text, intent, purpose, and policy.[336] But these concerns can be placed into a structured hierarchy where they conflict.[337] Thus, statutory text deserves special weight because it is formally enacted into law and because it recognizes the primacy of legislative judgments.[338] But hermeneutics teaches us that text cannot be given meaning until it is interpreted, for the interpreter must often choose among competing meanings and inevitably draws on his own experience. The choices of the interpreter, the judge, will be controlled by no single value.[339]

Consequently, text alone will not answer most questions. Historical considerations should be weighed next because they defer to congressional will.[340] Here it becomes appropriate to inquire into the historical setting, particularly the legislative history.[341]

> "I don't know of any person who is worth their salt who goes on simple emotion, except maybe actors. When you take an oath to hand out justice, you in your own mind have to take any prejudice you have, or predilection that you might have, and push it back, out of your mind until after you decide the case . . . ."

(quoting Justice Marshall in an interview).

[335] *See* LAWRENCE M. SOLAN, THE LANGUAGE OF JUDGES 179 (1993):

> The expansion of legal doctrine to permit open debate about . . . what are considered nonlegal, political issues into legal discourse is a stated goal of the critical legal studies movement. It would be a mistake, however, to conclude that tolerance of expanded legal doctrine would lead to the adoption of a particular political agenda. Just because a judge feels comfortable writing about political and social concerns does not make him a champion of the left.

See also DWORKIN, *supra* note 175, at 329–30 (where justifications are consistent with a conventional legislative intention, statutory text, and political climate, "judges must decide which of the two competing justifications is superior as a matter of political morality, and apply the statute so as to further that justification); *cf.* David P. Leonard, *Power and Responsibility in Evidence Law*, 63 S. CAL. L. REV. 937 (1990) (judicial discretion need not necessarily be feared and can be controlled).

[336] Eskridge & Frickey, *supra* note 110, at 322–23.

[337] *Id.* at 353.

[338] *Id.* at 354–56.

[339] *Id.* at 340–45.

[340] *Id.* at 356.

[341] *Id.* at 356 ("The most authoritative historical evidence is the legislative history of the statute, because it is a contemporary record made by the enacting legislators.").

Where that is inadequate, one should try imaginative reconstruction,[342] and where that fails, purpose is the next best guide.[343]

Purpose is itself flexible, however, since it can be described at varying levels of generality, purposes may conflict, and new problems may arise that the Congress did not anticipate. This, in turn, requires consideration of evolutive concerns,[344] including current values, such as ideas of fairness.[345] This reliance on multiple sources of evidence reflects the pragmatic view that decision-making is best and most convincing when we examine the consistency of the evidence for each value of importance to us before reaching a decision.[346] This guided, hierarchical, but flexible approach more closely approximates what judges actually do, seeks to help the fair-minded judge to structure and limit his discretion, and should lead to more careful, thorough analyses.[347]

Two main implications arise from interpreting the Rules in this manner. First, it mandates inquiry into all that is part of practical reasoning, including examining the intellectual and political history of the Rules, as a whole and individually. Second, the examination of that history of the Rules as a whole shows that they were expressly designed for a practical reasoning approach to interpretation, as we will now see.

I. *The Rules' Unique Theory of Judicial Discretion*

Scholars increasingly recognize that different statutes need to be interpreted differently because they were designed for different purposes and different audiences.[348] Congress's main purpose

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[342] *Id.* at 357 (noting that imaginative reconstruction is guided by common law rules when the statute was enacted, general assumptions of law held by the enacting Congress, and contemporary statutes enacted on related subjects).

[343] *Id.* at 357–58 (purposivism's assumptions, especially its focus on context, place a statute in the evolving legal and social terrain and enable it to evolve along with the social problem it addresses).

[344] *See generally* GUIDO CALABRESI, A COMMON LAW FOR THE AGE OF STATUTES (1990).

[345] Eskridge & Frickey, *supra* note 110, at 358–60.

[346] *Id.* at 348.

[347] *See supra* text accompanying notes 312–335; *infra* text accompanying notes 348–377.

[348] *See* Edward R. Becker & Aviva Orenstein, *The Federal Rules of Evidence After Sixteen Years—The Effect of "Plain Meaning" Jurisprudence, the Need for an Advisory Committee on the Rules of Evidence, and Suggestions for Selective Revision of the Rules*, 60 GEO. WASH. L. REV. 857, 867 (1992) ("[T]here is a growing recognition that generalized, global theories of statutory interpretation are less helpful than approaches

in passing the Federal Rules of Evidence was to adopt the views of the Supreme Court and the Advisory Committee;[349] the Rules should be interpreted accordingly. But the Advisory Committee intended to create a system of guided discretion for trial judges, limited appellate review, and room for case-by-case growth of the law of evidence.[350]

The form and approach of the Rules were based upon two earlier codification efforts, the Model Code of Evidence[351] and the Uniform Rules of Evidence.[352] The American Law Institute (A.L.I.) adopted its Model Code in 1942.[353] The ALI considered three code forms at its 1940 meeting:[354]

> [T]o canvass all the situations in which pertinent questions have been answered by the courts and to devise a mandate to the trial judge for each such case . . . ; to frame a very few, very broad general principles, and direct the trial judge to apply them . . . ; [or] to draw a series of rules in general terms covering the larger divisions and subdivisions of the subject without attempting to frame rules of thumb for specific situations and to make the trial judge's rulings reviewable *for abuse of discretion* . . . . [T]he choice is between a catalogue, a creed, and a Code. The Institute decided in favor of a Code.[355]

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tailored to individual statutes."); *supra* note 167, at 87 (noting that probable audience affects statutory meaning).

[349] *See* Weissenberger, *The Supreme Court*, *supra* note 112, at 1307 (1992) ("Congress' primary function was to enact into law the will and intent of the Supreme Court and its Advisory Committee.").

[350] *See id.* at 1310 ("[T]he Federal Rules of Evidence were consciously drawn with a recognition that the federal trial judiciary possess substantial inherent discretion in interpreting, expanding upon, and applying the Rules."); Gold, *supra* note 214, at 921 ("[I]mplicit in every undefined [Rules'] term is the hope that the courts will finish the job of rulemaking"); Mengler, *supra* note 216, at 414. (arguing that appellate courts should not interpret the Rules to take away their flexibility). *See also infra* text accompanying notes 360–366 (regarding guided discretion and role of the common law).

[351] AMERICAN LAW INSTITUTE, MODEL CODE OF EVIDENCE (1942).

[352] NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAW, UNIFORM RULES OF EVIDENCE (1953).

[353] *See id.* at 859. This discussion focuses on the more important Model Code because the Uniform Rules expressly adopted the Code's general approach while rejecting some of its more radical departures from the common law. *See* UNIF. R. EVID. prefatory note at 162 (1953) (National Conference of Commissioners on Uniform State Law); *see* Michael S. Ariens, *The Law of Evidence and the Idea of Progress*, 25 LOY. L.J. 853, 861 (1992) (noting Uniform Rules' abandonment of Code's radical substantive changes while retaining its grant of trial judge discretion).

[354] *See* Mengler, *supra* note 216, at 413.

[355] Edmund H. Morgan, *Foreword* to MODEL CODE OF EVIDENCE 12–13 (1942) [hereinafter Morgan, *Foreword*] (emphasis added). *Compare id. with* JOHN HENRY WIGMORE, CODE OF EVIDENCE (1st ed. 1910) (attempting a catalogue-type evidence

Morgan had argued for this intermediate form of evidence code because it offered more guidance than a creed but allowed for flexibility. He believed judges needed latitude to act quickly when facing new situations and seeking to individualize justice.[356]

Members of the Advisory Committee on the Rules indicated at various times and in various places that they shared Morgan's drafting philosophy.[357] That philosophy—which imparted substantial but guided discretion to the trial judge—was reflected in testimony by members of the Advisory Committee before Congress.[358] The design of the Rules also reveals Morgan's drafting philosophy: the Rules intentionally included gaps and ambiguous language that could only be given meaning on a case-by-case basis and by reference to the common law.[359]

Indeed, several courts have found that the Rules' drafters intended that the common law continue to be relevant to interpretation of the Rules.[360] And Congress, granting the Supreme Court

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code) *and* Edmund H. Morgan, *Discussion of Code of Evidence Tentative Draft No. 1*, 17 A.L.I. PROC. 81–84 (1940) [hereinafter Morgan, *Tentative Draft Discussion*] (critiquing Judge Charles E. Clarke's proposal for a creed-type evidence code as little better than common law).

[356] *See* Mengler, *supra* note 216, at 414 ("Each trial tells its own tale, raises unique evidentiary concerns, and consequently calls for individual treatment."); Andrew E. Taslitz, *Myself Alone: Individualizing Justice Through Psychological Character Evidence*, 52 MD. L. REV. 1, 60–63 (1993) (exploring value of individualized justice in evidence law). Morgan also recognized that trials seek goals other than truth. Morgan, *Foreword*, *supra* note 355. Trial judge discretion helps to achieve those goals, enabling them "to check the overall fairness of a trial . . . ." Mengler, *supra* note 216, at 414.

[357] *See* Mengler, *supra* note 216, at 437 (detailing drafters' beliefs that the variety of trials argued against the feasibility of mechanical rules; that a code needed to be compact and accessible to facilitate rapid decisionmaking; that some detail would avoid unpredictability; and that evidence law could grow better by codification rather than appellate rulemaking).

[358] For example, Professor Cleary explained why the Rules did not create unbridled judicial discretion, *see Proposed Rules of Evidence: Hearings Before the Subcomm. on Reform of Federal Criminal Laws of the House Comm. on the Judiciary*, 93d Cong., 1st Sess. 91, 547 (1973), by quoting Professor Davis' statement that, "at the middle of the scale" between rigid rules and unbridled discretion is guided or limited discretion, a middle ground less likely than either pole to lead to injustice. *See* KENNETH DAVIS, DISCRETIONARY JUSTICE: A PRELIMINARY INQUIRY at v (1971). *See generally* Mengler, *supra* note 216, at 430–31 (discussing congressional proceedings).

[359] *See id.* at 438–57 (illustrating the many provisions in the Rules that invite use of discretion, either expressly or through broad language). Even Professor Imwinkelried concedes that "the courts may certainly turn to common law precedents to help them resolve ambiguities in the text of the individual rules." Edward J. Imwinkelried, *A Brief Defense of the Supreme Court's Approach to the Interpretation of the Federal Rules of Evidence*, 27 IND. L. REV. 267, 281 (1993) [hereinafter Imwinkelried, *Brief Defense*].

[360] *See supra* text accompanying notes 21, 38–39 (discussing Supreme Court's recent reliance on the common law in Tome v. United States, 115 S. Ct. 696, 702, 706 (1995)); Taslitz, Daubert*'s Guide*, *supra* note 1, at 8–11 (discussing the Court's reference to common law in United States v. Abel, 469 U.S. 45 (1984)); Werner v. Upjohn Co., 628

the authority to design and promulgate the Rules, and modifying only a few discrete provisions while leaving others intact, indicated it adopted the will of the Advisory Committee as its own.[361]

This procedural history helps courts to interpret the Rules. For Rules Congress has changed, a reviewing court should undertake a traditional search for legislative intent as part of the interpretive process.[362] Such a search may include a special emphasis on text as a guide to intent. But for the many unchanged provisions and those that contain gaps and ambiguities, the court should seek guidance from the Advisory Committee Notes, from a special attention to the policies underlying the particular rule, from a reference to common law antecedents and developments, and from a sensitivity to the need for rules that allow for case-by-case fine-tuning by trial judges exercising their sound discretion. For the latter type of rules—and there are many such rules in the Federal Rules of Evidence—the new textualism makes especially little sense.[363] While the text of a rule may (and should)

F.2d 848, 856 (4th Cir. 1980) ("Congress did not intend to wipe out the years of common law development in the field of evidence."). Professor Imwinkelried, applying the maxim "*expressio unius est exclusio alterius*," has argued that because Rule 402 lists various authoritative sources that may modify the rules, but does not include the "common law" among those sources, Congress meant to disallow use of the common law. *See* Imwinkelried, *Brief Defense*, *supra* note 359, at 273–75. But, as Professor Weissenberger has pointed out, the maxim does not appear in the Rules, undermining the notion that text alone answers every question. *See* Weissenberger, *Rules as a Statute?*, *supra* note 98, at 399. Furthermore, "rules" of construction are guidelines that should give way to contrary indications of intent, *see* BARBARA CHILD, DRAFTING LEGAL DOCUMENTS: MATERIALS AND PROBLEMS 204 (1988). *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 14–15.

[361] *See* Weissenberger, *The Supreme Court*, *supra* note 112, at 1309, 1320, 1323–24.

[362] *See id.* at 1324–25.

[363] Professor Imwinkelried has argued precisely the opposite: that only the new textualism can protect trial judge discretion. Imwinkelried, *Brief Defense*, *supra* note 359, at 289–92. He argues, first, that newly crafted exclusionary rules (which flexible interpretation might create) replace discretion with mechanical rules; second, that appellate courts (which may be busy under a flexible regime) intervene in prescribing evidentiary rules far more often than do legislatures; and third, in at least one state, California, the appellate courts have vigorously intervened to limit trial judge discretion. Because new textualism purportedly prevents new exclusionary rules, it blocks intervention with such discretion. But this analysis is fundamentally flawed. Appellate intervention can be in the form of guidelines, rather than rigid new exclusionary rules. *See* Leonard, *supra* note 73, at 1179; Jon R. Waltz, *Judicial Discretion in the Admission of Evidence Under the Federal Rules of Evidence*, 79 NW. U.L. REV. 1097, 1103 (1984–85) ("*Guided* discretion . . . identifies areas in which a judge has some flexibility and choice in decision-making but is restrained by more or less specific standards or guidelines to which he visibly must adhere.") (emphasis added). Indeed, such a guidelines approach was followed in *Daubert* and *Williamson v. United States*. *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 75.

Furthermore, that appellate courts intervene more often than do legislatures does not mean that the appellate courts intervene nearly enough. To the contrary, appellate review of most discretionary matters is usually quite hollow, eliminating any incentive

set the outer boundaries for interpretation, it can be no more than a starting point.

The Supreme Court took this approach in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*[364] The result is a rule that provides guidance for the exercise of discretion by trial judges.[365] The Court purported to use textualism to explain its holding, but the window-dressing failed to hide its true method. The Court should acknowledge its implicit adoption of a more flexible approach to the Rules of Evidence.[366] Furthermore, it should apply the approach consistently, placing greater emphasis on text only for those rules actually altered by Congress. Even for such rules, however, an entirely textualist approach is unwise and unworkable.

IV. Conclusion: A Call for Judicial Candor

In a 1989 article, Nicholas Zeppos argued that judicial candor in statutory interpretation is not a desirable goal.[367] According to Zeppos, in cases where courts apply a flexible approach that balances numerous factors, candor is unlikely to improve the predictability of the Court's decisions.[368] In addition, he argues, candor may be an elusive goal. Judges may intertwine the "real" reasons for their decisions with reasons that are more acceptable to the public and then convince themselves that they really believe in the publicly acceptable reasons.[369] Finally, candor may create the appearance of judicial policymaking, blurring the distinction between courts and legislatures and potentially undermining the legitimacy of the courts.[370]

While candor may not necessarily improve the predictability of decisions, it may improve their quality. When a court is forced

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or guidance in trial judge care in exercising discretion, the purported California experience notwithstanding. *See* Leonard, *supra*, at 1176, 1179, 1220, 1227–28.

Finally, a trial court's freedom to be creative in meeting new challenges, subject to appellate guidelines, creates precisely the kind of opportunity for growth that the Rules contemplate.

[364] 113 S. Ct. 2786 (1993).

[365] *See* Taslitz, Daubert*'s Guide*, *supra* note 1, at 66–68.

[366] As it seems well on its way to doing in much of its post-*Daubert* jurisprudence. *See supra* text accompanying notes 63–75, 105–107.

[367] *See* Nicholas S. Zeppos, *Judicial Candor and Statutory Interpretation*, 78 Geo. L.J. 353, 400–13 (1989).

[368] *See id.* at 402–03.

[369] *See id.* at 406–12.

[370] *See id.* at 404.

to articulate the real reasons behind its decisions, it must wrestle with those reasons. Identifying the underlying reasons for a decision is a challenging, but not impossible, task.[371] Some of a judge's reasons will be policy-driven: views about economics, politics, and morality. Other assumptions, values, and attitudes resulting from personality and upbringing may be more difficult to identify but are not wholly beyond judicial recognition. Having to defend the wisdom of a choice in a particular case can help one to identify the underlying values.

But if the "real" reasons for a decision are candidly stated, the author faces the challenge of articulating those reasons in a way that will be persuasive to others and to herself. Every writer has had the experience of changing a position after finding herself unable to articulate a clear, thorough, and convincing rationale on paper. She must confront opposing viewpoints and may discover better reasons for her original position in the process.

Candor should promote better decisions, and improve legitimacy. Lack of candor may lead to logically flawed, inconsistent, and unpersuasive opinions. Reliance on linguistic argumentation to create the appearance of objective, rational decisionmaking leads to "incoherence [as] the rule—not the exception . . . ."[372] since few matters can be resolved easily by linguistic analysis.[373] The disingenuousness of linguistic arguments are quickly perceived by native speakers of English.[374] And people who have been lied to come to distrust the liar and the system he represents.[375]

Candid recognition by the Court of the limitations of linguistic analysis, and the corresponding need to abandon the new textualism, will not undermine the Court's legitimacy. A more flexible approach to statutory interpretation will still serve legislative intent. It may even better serve that intent by furthering broad

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[371] In fact, argues Steven Burton in a new book, the task is not only possible but quite common and indeed the essence of good judging. *See* STEVEN BURTON, JUDGING IN GOOD FAITH 36–37, 81–103, 164–65 (1994). Burton acknowledges that law does not rigidly determine results, but law does limit the legitimate reasons a judge may take into account and guides the judge on how to weigh those reasons. *Id.* at 50–68, 92–93, 100–02.

[372] SOLAN, *supra* note 177, at 178 ("And this lack of candor is sufficient to rob the opinions of their rhetorical force . . . .").

[373] *See id.* at 117, 186 (Solan is an attorney with a doctorate in linguistics).

[374] *Id.* at 29–37 (giving examples of linguistic analyses by courts that violate the intuitive sense of grammar of native English speakers).

[375] *See id.* at 27. *See also* David Shapiro, *Courts, Legislatures, and Paternalism*, 74 VA. L. REV. 519, 556, 569 (1988) (arguing for candor in judging); David Shapiro, *In Defense of Judicial Candor*, 100 HARV. L. REV. 731 (1987).

legislative purposes where Congress did not consider a particular matter in detail. This approach maintains the distinction between the legislature and the judiciary and demonstrates appropriate deference to the legislature. In the case of the Rules, since Congress's role was "to approve the internal rules of a coordinate branch of government where such rules originated within that coordinate branch,"[376] separation of powers has less meaning. Here deference to Congress really means acceptance of the Court's own intentions, which, in turn, means ratification of the intentions of the Advisory Committee.[377]

Greater candor will lead to greater trust in the Court by both the public and lawyers. That the interpretive method involves some judicial policymaking does not mean it leads to a series of ad hoc, inconsistent decisions. The theory of practical reason relies on a hierarchy of sources for statutory interpretation, which includes a hierarchy of legislative history, and retains a sensitivity to the broad purposes of the Rules. This theory will create a structured, coherent, and, to some degree, predictable pattern of interpretation for the Rules. Such an approach would reduce—though not eliminate—the need for frequent revision of the Rules. It will foster a living, growing evidence law pursuant to a coherent philosophy—a result much more consistent with the true intent of the Rules' framers.

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[376] Weissenberger, *The Supreme Court*, *supra* note 112, at 1323.
[377] *Id.* at 1323–24.

ARTICLE

COMPULSORY LICENSING OF BLACKED-OUT PROFESSIONAL TEAM SPORTING EVENT TELECASTS (PTSETS): USING COPYRIGHT LAW TO MITIGATE MONOPOLISTIC BEHAVIOR

ALAN M. FISCH*

Federal copyright law now prohibits sports bars and other commercial establishments from displaying blacked-out telecasts of professional sporting events, thus enabling professional sports leagues to hold related monopolies over live and televised access to these events. In this Article, Mr. Fisch proposes a compulsory license for blacked-out telecasts and analyzes its potential economic effect. He concludes that a compulsory licensing scheme should be considered as one means of mitigating the monopolistic behavior of professional sports leagues.

The 1984-85 St. Louis Cardinals[1] ("Cardinals") football season may be remembered more for its off-field legal effect than its on-field heroics.[2] Three "blacked-out"[3] Cardinals games played during that season were the basis of *Nat'l Football League v. McBee & Bruno's*,[4] a copyright infringement lawsuit brought by the National Football League ("NFL") against a group of St. Louis restaurants and bars. The NFL contended that these com-

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[1] In 1987, the St. Louis Cardinals moved to Arizona and became the Phoenix Cardinals. Douglas S. Looney, *One Touchy Love Affair*, SPORTS ILLUSTRATED, Aug. 22, 1988, at 28. In 1994, the Phoenix Cardinals changed their name to the Arizona Cardinals. David Aldridge, *NFL Adds 2-Pointer After TD; Kickoff Moved Back Five Yards*, WASH. POST, Mar. 23, 1994, at C1.

[2] The Cardinals finished the 1984-85 season with a dismal record of 5 wins and 11 losses. *Sour End For the Cardinals*, N.Y. TIMES, Dec. 23, 1985, at C3.

[3] The term "blacked-out" refers to two distinct situations: (1) the decision not to televise a sporting event in the geographic area the event is occurring; and (2) a decision not to televise a sporting event in a geographic area distinct from where the event is occurring. Thomas M. Torrens, Comment, *Professional Football Telecasts and the Blackout Privilege*, 57 CORNELL L. REV. 297, 297 n.4 (1972). For this discussion, the term "blacked-out," and its natural grammatical derivations, describes a league decision not to televise a sporting event in the home team's geographic area.

[4] Nat'l Football League v. McBee & Bruno's, 621 F. Supp. 880 (E.D. Mo. 1985), *aff'd in part and rev'd in part*, 792 F.2d 726 (8th Cir. 1986) [hereinafter *NFL I*].

mercial establishments' use of satellite equipment[5] to televise blacked-out games violated applicable copyright law.[6] In ruling on the matter, the United States Court of Appeals for the Eighth Circuit held that the restaurants and bars infringed the telecasts' copyright.[7] This decision effectively ended the profitable practice[8] of commercial establishments' televising blacked-out games.[9]

Recently, legislators and commentators have recommended that Congress overrule the Eighth Circuit by modifying copyright law to include a compulsory license[10] for the public showing of blacked-out professional team sporting event telecasts ("PTSETs").[11] This Article analyzes whether sufficient justification exists to enact such a compulsory licensing scheme. Part I sets forth some basic copyright law pertinent to this debate. Part II describes one PTSET compulsory license proposal. Part III analyzes the proposed compulsory license's legality. Part IV concludes that a compulsory license for PTSETs could mitigate the monopolistic behavior of professional sports leagues.

I. Background Copyright Law

The United States Constitution grants Congress the authority to enact legislation "[t]o promote the progress of science . . . by securing for limited times to authors . . . the exclusive right to their . . . writings."[12] In 1790, Congress enacted the first United

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[5] Satellite equipment refers to all of the hardware necessary to receive television signals from communications satellites in geosynchronous earth orbit.

[6] Nat'l Football League v. McBee & Bruno's, 792 F.2d 726, 727 (8th Cir. 1986) [hereinafter *NFL II*].

[7] *Id.* at 732.

[8] *See, e.g., id.* at 729 n.5 ("The owner of one of the defendant restaurants testified that when a blacked-out game was shown, he served 190 patrons, as opposed to 30 customers" on the same day of the week without a blacked-out game.) (citations omitted).

[9] Although a probable violation of copyright law, televising of blacked-out PTSETs remained a practice at some commercial establishments even after the ruling for the NFL.

[10] *See also infra* notes 47–50 and accompanying text.

[11] *See, e.g.*, H.R. 935, 104th Cong., 1st Sess. (1995) (introduced by Rep. William O. Lipinski, D-Ill.); H.R. 1988, 103d Cong., 1st Sess. (1993) (same); Andrew Zimbalist, Baseball and Billions: A Probing Look Inside the Big Business of Our National Pastime 176 (1992). Since proposing the compulsory license, Professor Zimbalist has become a principal in an upstart professional baseball league. Frederick C. Klein, *Is One More Baseball League What Fans Want?*, Wall St. J., Apr. 14, 1995, at B10.

[12] U.S. Const. art. I, § 8, cl. 8. This clause is often termed the copyright clause of the Constitution. *See, e.g.*, Karl Fenning, *The Origin of the Patent and Copyright Clause of the Constitution*, 17 Geo. L.J. 109 (1929).

States copyright law.[13] The current copyright law,[14] the Copyright Act of 1976 ("Copyright Act"),[15] grants protection to "original works of authorship fixed in any tangible medium of expression."[16] Works of authorship include, *inter alia*, motion pictures and other audiovisual works,[17] including PTSETs.[18] Accordingly, PTSETs are afforded all the rights and protections that copyright

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The Supreme Court has broadly interpreted the term "writings." *See* Goldstein v. California, 412 U.S. 546 (1973) ("[A]lthough the word 'writings' might be limited to script or printed material, it may be interpreted to include any physical rendering of the fruits of creative intellectual or aesthetic labor."). *See also* Melville B. Nimmer, *The Subject Matter of Copyright Under the Act of 1976*, 24 UCLA L. REV. 978 (1977).

[13] DONALD S. CHISUM & MICHAEL A. JACOBS, UNDERSTANDING INTELLECTUAL PROPERTY LAW § 4B (1992). For additional discussions on the history of U.S. copyright law, see R.R. BOWKER, COPYRIGHT: ITS HISTORY AND ITS LAW (1912); BRUCE W. BUGBEE, GENESIS OF AMERICAN PATENT AND COPYRIGHT LAW (1967); HARRY RANSOM, THE FIRST COPYRIGHT STATUTE (1956).

[14] "United States copyright law evolved through three major eras: (1) from adoption of the Constitution and the first copyright statute in 1790 to enactment of the 1909 Act; (2) the 1909 Act; (3) the current Copyright Act of 1976." CHISUM & JACOBS, supra note 13, at § 4B.

[15] 17 U.S.C. §§ 101–1010 (1988 & Supp. V 1993).

[16] 17 U.S.C. § 102(a) (1988 & Supp. V 1993). Neither the threshold requirement of originality nor fixation presents a barrier to the copyright of PTSETs.

Originality is comprised of two elements: (1) independent creation; and (2) "some minimal degree of creativity." Feist Publications, Inc. v. Rural Telephone Service Co., 499 U.S. 340, 345 (1992) (citation omitted). Independent creation "means little more than a prohibition of actual copying." Hoague-Sprague Corp. v. Frank C. Meyer Co., 31 F.2d 583, 586 (D.C.N.Y. 1929). PTSETs are independent creations because each PTSET is unique. The requirement of "some minimal degree of creativity" is met for PTSETs in the selection of camera angles, scenes, and accompanying audio and video information. *See* Time Inc. v. Bernard Geis Associates, 293 F. Supp. 130, 143 (S.D.N.Y. 1968) (holding that Mr. Zapruder's film of the assassination of President Kennedy is original because Zapruder exercised creativity in the selection of location, camera type, and film type). For additional treatment of the originality requirement, see 1 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT §§ 1.08[C], 2.01[A]–[B] (1994); Dale P. Olson, *Copyright Originality*, 48 MO. L. REV. 29 (1983).

As for the threshold requirement of fixation, the Copyright Act states that "[a] work is 'fixed' in a tangible medium of expression when its embodiment in a copy . . . is sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory duration." 17 U.S.C. § 101 (1988). A live sporting event telecast is fixed for purposes of copyright law when simultaneous to transmission there is a recording made of the event. H.R. Rep. No. 1476, 94th Cong., 2d Sess. 52 (1976) *reprinted in* 1976 U.S.C.C.A.N. 5659, 5665 [hereinafter 1976 House Report].

[17] 17 U.S.C. § 102(a)(6) (1988). Other works explicitly included are literary works; musical works, including any accompanying words; dramatic works, including any accompanying music; pantomimes and choreographic works; pictorial, graphic, and sculptural works; sound recordings; and architectural works. 17 U.S.C. § 102(a) (1988 & Supp. V 1993). This list of works is "illustrative and not limitative." 1976 House Report, *supra* note 16, at 53.

[18] *See, e.g.*, 1976 House Report, *supra* note 16, at 52 ("When a football game is being covered by four television cameras, with a director guiding the activities of the four cameramen and choosing which of their electronic images are sent out to the public and in what order, there is little doubt that what the cameramen and the director are doing constitutes 'authorship.'").

law offers.[19]

The rights and protections of copyright law vest with the owner of the copyrighted work.[20] In *Baltimore Orioles, Inc. v. Major League Baseball Players Ass'n*,[21] the Seventh Circuit held that ownership belongs to the teams, not the participating athletes.[22] Since the passage of the Sports Broadcasting Act of 1961,[23] professional sports leagues[24] have represented individual teams in national telecast matters. Accordingly, this Article refers to owners of copyrights on PTSETs as leagues.

Copyright law affords copyright owners specific exclusive rights to the copyrighted work.[25] One of the exclusive rights applicable to PTSETs is the right "to perform the copyrighted work

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[19] The sporting event itself, however, is not copyrightable because it is not a work of authorship. J. THOMAS MCCARTHY, THE RIGHTS OF PUBLICITY AND PRIVACY § 11.13[C]4 (1987); see also *Copyright Law Revision: Hearings on H.R. 2223 Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary*, 94th Cong., 1st Sess. 1832 (1975) [hereinafter *Hearing on H.R. 2223*] (Register of Copyrights, Barbara Ringer, doubting that sporting events, or the athletes' participatory actions, are copyrightable).

[20] *See* 17 U.S.C. § 201(a) (1988); *see also* Meltzer v. Zoller, 520 F. Supp. 847, 857 (D.N.J. 1981) ("[A]uthorship [is] the *sine qua non* of copyright.").

Once an exclusive license is granted, the holder of it is a copyright owner. 17 U.S.C. § 101 (1988).

[21] 805 F.2d 663 (7th Cir. 1986).

[22] *Id.* at 673. For a discussion criticizing the court's holding, see David E. Shipley, *Three Strikes and They're Out at the Old Ball Game: Preemption of Performers' Rights of Publicity Under the Copyright Act of 1976*, 20 ARIZ. ST. L.J. 369 (1988).

The court, however, did not state whether teams jointly own a PTSET copyright with the producers of the PTSET, or whether the copyright is exclusively owned by the teams. 805 F.2d at 673 n.18.

[23] *See infra* notes 107–110 and accompanying text.

[24] This Article uses the terms "professional sports league" and "league" to refer to a voluntary organization providing institutional structure for member teams to determine a league champion, regardless of its self title. See James Quirck, *An Economic Analysis of Team Movements in Professional Sports*, 38 LAW & CONTEMP. PROBS. 42, 43 (1973). Part of the institutional structure provided includes determining playing rules, player eligibility, and contest schedules. *Id.*

[25] Subject to §§ 107–120 of the Copyright Act, a copyright owner has the exclusive right to do and to authorize any of the following:

> (1) to reproduce the copyrighted work in copies or phonorecords;
> (2) to prepare derivative works based upon the copyrighted work;
> (3) to distribute copies or phonorecords of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending;
> (4) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and motion pictures and other audiovisual works, to perform the copyrighted works publicly; and
> (5) in the case of literary, musical, dramatic, and choreographic works, pantomimes, pictorial, graphic, or sculptural works including the individual images of an audiovisual work, to display the copyrighted work publicly.

17 U.S.C. § 106 (1988 & Supp. V 1993).

For additional discussion of these exclusive rights, see Paul Goldstein, *Derivative Rights and Derivative Works in Copyright*, 30 J. COPYRIGHT SOC'Y 209 (1983); John M. Kernochan, *The Distribution Right in the United States of America: Review and*

publicly."[26] The terms "perform" and "publicly" are further defined by the Copyright Act. "Perform" means "[t]o show [the telecast's] images in any sequence or to make the sounds accompanying it audible."[27] With respect to PTSETs, "publicly" means "to perform or display [the telecast] at a place open to the public or at any place where a substantial number of persons outside of a normal circle of a family and its social acquaintances is gathered."[28] Given these definitions, televising blacked-out PTSETs at a commercial establishment violates a league's exclusive right to perform the copyrighted work publicly.

Section 110(5) of the Copyright Act provides an exception to the exclusive right of public performance.[29] Under this exception, commercial establishments may publicly perform a copyrighted work without the permission of the copyright owner, provided the audiovisual equipment used by the establishment is "a single receiving apparatus of a kind commonly used in private homes."[30] In interpreting "commonly used in private homes," the Eighth Circuit stated in *Nat'l Football League v. McBee & Bruno's* that satellite equipment does not qualify, based on the district court's factual conclusions.[31] The district court, citing no source for its data, found that there were "less than 1,000,000 dish systems in use, and many of these [were] confined to commercial establishments."[32] The Eighth Circuit stated that it would not reverse because the district court's factual findings were "not clearly erroneous."[33] The court did state, however, that "some day" this technology "may be commonplace."[34]

Reflections, 42 VAND. L. REV. 1407 (1989); David E. Shipley, *Copyright Law and Your Neighborhood Bar and Grill: Recent Developments in Performance Rights and the Section 110(5) Exemption*, 29 ARIZ. L. REV. 475 (1987); Michael Wurzer, Note, *Infringement of the Exclusive Right to Prepare Derivative Works: Reducing Uncertainty*, 73 MINN. L. REV. 1521 (1989).

[26] 17 U.S.C. § 106(4) (1988).

The right to public display is not applicable in the case of PTSETs. *See* 17 U.S.C. § 101 (1988) ("To 'display' a work means . . . in the case of a motion picture or other audiovisual work, to show individual images nonsequentially.").

[27] 17 U.S.C. § 101 (1988).

[28] *Id.* A second definition of "publicly" is found in § 101, but this definition is not applicable to this discussion.

[29] 17 U.S.C. § 110(5) (1988).

[30] *Id.*

[31] 792 F.2d at 731.

[32] *NFL I*, 621 F. Supp. at 887 (citing no authority for the relied upon data).

[33] *NFL II*, 792 F.2d at 731.

[34] *Id.* For a discussion critical of the district court's finding that satellite equipment is not commonly used in private homes, see Francis M. Nevins, Jr., *Antenna Dilemma:*

In the seven years since *McBee & Bruno's*, no United States Circuit Court has found that satellite equipment has become commonly used in private homes for copyright law purposes. Such a finding would allow a commercial establishment the opportunity to televise blacked-out PTSETs provided it meets the other requirements of section 110(5): (1) no direct charge is made to see or hear the performance; and (2) the transmission received must not be further transmitted to the public.[35] Commercial establishments could easily satisfy such requirements.

Until a court finds that satellite equipment is commonly used in private homes, a commercial establishment using satellite equipment to televise a PTSET without the owning league's permission would likely violate the league's exclusive right of public performance as provided by section 106 of the Copyright Act.[36] Violating any of a copyright holder's exclusive rights constitutes copyright infringement.[37] Copyright infringement may be redressed by injunction,[38] damages and profits,[39] costs and attorney's fees,[40] or even criminal proceedings.[41] To avoid copyright infringement, a commercial establishment could obtain a license from the league authorizing public performance of a blacked-out PTSET. A license "in essence is nothing more than a promise by the licensor not to sue the licensee" for infringement.[42] Leagues, however, view

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The Exemption from Copyright Liability for Public Performance Using Technology Common in the Home, 11 COLUM.-VLA J.L. & ARTS 403, 407–11 (1987).

[35] 17 U.S.C. § 110(5)(A)–(B) (1988). For an analysis of the technical aspects of Section 110(5), see Robert Cash, Note, *Sailor Music: Exposing the Gaps in 17 U.S.C. § 110(5)*, 9 RUTGERS J.L. & TECH. 133 (1982).

[36] *See supra* note 25 (listing exclusive rights).

[37] 17 U.S.C. § 501(a) (1988 & Supp. V 1993).

[38] 17 U.S.C. § 502 (1988) (A court "may . . . grant temporary and final injunctions on such terms as it may deem reasonable to prevent or restrain infringement."). See also Timothy J. McClimon, *Denial of the Preliminary Injunction in Copyright Infringement Cases: An Emerging Judicially Crafted Compulsory License*, 10 COLUM.-VLA J.L. & ARTS 277 (1986); James L. Oakes, *Copyrights and Copyremedies: Unfair Use and Injunctions*, 38 J. COPYRIGHT SOC'Y 63 (1990).

[39] 17 U.S.C. § 504 (1988). Actual damages and profits are both recoverable only when double recovery does not occur. 1976 House Report, *supra* note 16, at 161. *See also id.* at 162–63 (discussing statutory damages); RUSSELL L. PARR, INTELLECTUAL PROPERTY INFRINGEMENT DAMAGES: A LITIGATION SUPPORT HANDBOOK (1993); Wendy K. Breuninger, *Statutory Damages and Right to Jury Trial in Copyright Infringement Suits*, 24 IDEA 249 (1983).

[40] 17 U.S.C. § 505 (1988). *See also* Elden Dale Golden, *The Discretionary Award of Attorney's Fees Under the Copyright Act*, 13 HASTINGS COMM. & ENT. L.J. 411 (1991).

[41] 17 U.S.C. § 506 (1988 & Supp. V 1993). *See also* James Lincoln Young, *Criminal Copyright Infringement and a Step Beyond*, 30 COPYRIGHT L. SYMP. (ASCAP) 157 (1983).

[42] Spindekfabrik Suessen-Schurr v. Schubert & Salazar, 829 F.2d 1075, 1081 (Fed. Cir. 1987), cert. denied, 484 U.S. 1063 (1988) (defining the parallel patent concept). *See also* 17 U.S.C. § 106 (1988 & Supp. V 1993) (permitting "the owner of [a]

the licensing of public performance rights to their blacked-out PTSETs as economically undesirable.[43] Unsurprisingly, leagues have been reluctant to grant licenses allowing commercial establishments to televise their blacked-out PTSETs,[44] and some leagues have vigorously worked to curtail infringement through court action.[45] In response to league reluctance to license blacked-out PTSETs to commercial establishments, legislators and commentators suggest that the Copyright Act should be modified to include a compulsory license provision for the public performance of blacked-out PTSETs.[46]

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copyright . . . the exclusive rights to do and *to authorize*" reproduction, preparation of derivative works, public performance, and public display) (emphasis added); *supra* note 25. The exclusive rights must be licensed through a written instrument, whereas a non-exclusive license need not be in writing. *See* 17 U.S.C. §§ 201(d)(2) (1988) (stating that a transfer of a copyright, or individual exclusive rights of the copyright, is permissible), 204 (1988) (stating that a transfer of copyright ownership must be in writing), 101 (1988) (defining transfer of copyright ownership to include exclusive licenses).

[43] A league's decision to black-out a home area is traditionally predicated on a belief that a black-out would increase local ticket sales and foster development of the local team's following. *See, e.g.*, Nat'l Football League v. The Alley, Inc., 624 F. Supp. 6, 8 (S.D. Fla. 1983); *NFL I*, 621 F. Supp. at 883. *See also infra* part II.C.

Some argue that black-outs are financially misguided because PTSETs increase league interest. *See, e.g.*, David M. Rice, *Calling Offensive Signals Against Unauthorized Showing of Blacked-Out Football Games: Can the Communications Act Carry the Ball?*, 11 COLUM.-VLA J.L. & ARTS 413, 426–28 & n.94 (1987). These arguments, however, are tangential to addressing compulsory licensing of blacked-out PTSETs because the decision to black-out is only based on a league's perceptions concerning profit maximization.

[44] *See generally* Franco Modigliani & Merton H. Miller, *The Cost of Capital, Corporation Finance and Theory of Investment*, 48 AM. ECON. REV. 261, 288 (1958) (concluding that profit-maximizing organizations will place their resources where they find the greatest return on investment).

Recently, the NFL began offering commercial establishments a license for the public performance rights to all their PTSETs, with the specific exclusion of offering a license to blacked-out PTSETs in the blacked-out area. Len Pasquarelli, *NFL Suit Has 3 Bars Scrambling: Intercepted Broadcast of Blackout is Charged*, ATLANTA CONST., Oct. 26, 1994, at C1 (discussing the NFL's new Sunday Ticket marketing concept).

[45] *See, e.g.*, Rudy Martzke, *NFL Tackles Game Pirates*, USA TODAY, Sept. 28, 1994, at 1A (indicating that the NFL has commenced legal action against suspected infringers in a number of major cities, including, Cleveland, Detroit, Miami, and New Orleans).

[46] *See, e.g.*, H.R. 935, 104th Cong., 1st Sess. (1995); 139 CONG. REC. E1173-01 (daily ed. May 6, 1993); 139 CONG. REC. H5108-02 (daily ed. July 26, 1993). *See generally* ZIMBALIST, *supra* note 11, at 176 (addressing the concept of compulsory licensing without using the specific legal terminology).

II. COMPULSORY LICENSE PROPOSAL

A. *Fundamentals*

A compulsory license requires an owner of a copyrighted work[47] to permit any person use of the copyrighted work for an established fee.[48] The owner of the copyrighted work may not refuse to license; instead, the owner "is compelled to license at a rate thought to be 'reasonable' by the government."[49] The government official responsible for determining the reasonable rate for the existing copyright compulsory licenses is the Librarian of Congress.[50]

Compulsory licensing provisions are rare in United States intellectual property law.[51] Only five narrowly tailored compulsory licensing provisions currently exist in the Copyright Act.[52] These five provisions include: (1) public performance of musical compositions on jukeboxes;[53] (2) use of music and works of art on public broadcasting;[54] (3) secondary transmission by cable tele-

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[47] Although this discussion confines itself to copyright law, there are also provisions requiring compulsory licensing of patents. *See, e.g.*, 42 U.S.C. §§ 2183(g) (1988) (Atomic Energy Act), 7608 (1988) (Clean Air Act). The United Nations Framework Convention on Biological Diversity creates another patent compulsory license. *See* Paul J. Gormley, Comment, *Compulsory Patent Licenses and Environmental Protection*, 7 TUL. ENVTL. L.J. 131, 154 (1993).

[48] J. THOMAS MCCARTHY, MCCARTHY'S DESK ENCYCLOPEDIA OF INTELLECTUAL PROPERTY 51–52 (1991).

[49] *Id.*

[50] *See* Pub. L. No. 103-198, 107 Stat. 2304 (1993) (Copyright Royalty Tribunal Reform Act of 1993). Until December 1993, these determinations were made by the Copyright Royalty Tribunal. 17 U.S.C. §§ 801–810 (1988). For a discussion of the now-abolished Copyright Royalty Tribunal, see Frederick F. Greenman, Jr. & Alvin D. Deutsch, *The Copyright Royalty Tribunal and the Statutory Mechanical Royalty: History and Prospect*, 1 CARDOZO ARTS & ENT. L.J. 1 (1982).

[51] CHISUM & JACOBS, *supra* note 13, at § 4E[7].

[52] *Id.*; *see also* MARSHALL LEAFFER, UNDERSTANDING COPYRIGHT LAW 206 (1989). A minority of commentators find six compulsory licenses in the Copyright Act. The sixth compulsory license results from finding two separate compulsory licenses in the Section 118 compulsory license for phonorecords. *See, e.g.*, Robert Cassler, *Copyright Compulsory Licenses—Are They Coming or Going?*, 37 J. COPYRIGHT SOC'Y 231, 232–35 (1990).

[53] 17 U.S.C. § 116 (1988 & Supp. V 1993). Modifications to the compulsory license have been made to meet international treaty requirements. *See* Scott M. Martin, Comment, *The Berne Convention and the U.S. Compulsory License for Jukeboxes: Why the Song Could Not Remain the Same*, 37 J. COPYRIGHT SOC'Y 262 (1989).

[54] 17 U.S.C. § 118 (1988 & Supp. V 1993). For additional discussions on the public broadcasting compulsory license, see John J. Timmel, *Public Broadcasting and the Compulsory License*, 3 HASTINGS COMM. & ENT. L.J. 25 (1980); Eric H. Smith & James F. Lightstone, *The New Copyright Law, Public Broadcasting, and the Public Interest: A Response to "Public Broadcasting and the Compulsory License"*, 3 HASTINGS COMM. & ENT. L.J. 33 (1980).

vision systems;[55] (4) mechanical royalties for making and distributing phonorecords;[56] and (5) satellite transmission for private home viewing.[57] The fifth provision, for satellite transmission for private home viewing, permits individual home owners to view blacked-out PTSETs without violating a league copyright. This provision only applies to "private home viewing," and therefore does not include viewing in commercial establishments.[58]

B. *Proposal*

A compulsory license for the public performance of blacked-out PTSETs, potentially the sixth exception, would permit commercial establishments, such as bars, restaurants, hotels, and other similarly situated gathering places, to use satellite equipment to televise locally blacked-out PTSETs for a determined royalty. The compulsory license would be narrowly tailored to include only professional league sports.[59]

Reasonable PTSET royalty fees would be calculated by the Librarian of Congress.[60] The statutory fee calculation would consider "the average fair market price for comparable programming provided by cable systems . . . and satellite carriers . . . to other places of public accommodation . . . in the same local, geographic area."[61] As a further consideration, the fee for each commercial establishment would account for the number of pa-

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[55] 17 U.S.C. § 111 (1988 & Supp. V 1993).

[56] 17 U.S.C. § 115 (1988). Phonorecords are defined by the Copyright Act as "material objects in which sound, other than those accompanying a motion picture or other audiovisual work, are fixed . . . and from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device." 17 U.S.C. § 101 (1988). For additional information on the compulsory license for phonorecords, see Paul S. Rosenlund, Note, *Compulsory Licensing of Musical Compositions for Phonorecords under the Copyright Act of 1976*, 30 HASTINGS L.J. 683 (1979).

[57] 17 U.S.C. § 119 (1988 & Supp. V 1993). For a discussion of recent modifications to the compulsory license, see *Legislation: President Signs Bill on Satellite and Wireless TV*, 48 PAT. TRADEMARK & COPYRIGHT J. (BNA) No. 1200, at 675 (Oct. 20, 1994) (addressing an act to renew the expiring compulsory license for satellite transmission and to extend cable compulsory licensing to recently implemented forms of wireless television).

[58] *See* 17 U.S.C. § 119(a)(1) & (6) (1988).

[59] The largest impacted entities are Major League Baseball, the National Basketball Association, the National Football League, and the National Hockey League.

[60] Such a practice exists for all existing copyright compulsory licenses. *See supra* note 50 and accompanying text.

[61] This method of calculation was first suggested in H.R. 1988, 103d Cong., 1st. Sess. § 2(b) (1993). It was again recently suggested in H.R. 935, 104th Cong., 1st Sess. § 2(b) (1995).

trons viewing a blacked-out PTSET at an establishment.

To enable the proposed compulsory license, one provision of the Communications Act of 1934,[62] specifically 47 U.S.C. § 605, would require slight modification to permit the lawful display of blacked-out PTSETs by commercial establishments.[63]

C. *League Costs*

The proposed compulsory licensing scheme imposes no additional cost burden on the leagues regarding transmission. Currently, leagues use satellite technology to transmit the PTSET from the field of play to subscribing television stations.[64] Because PTSETs are already available from a satellite, and in theory an unlimited number of receivers can receive the game from the satellite without increasing costs,[65] leagues would incur no additional transmission cost under the compulsory licensing scheme.

Opponents of the compulsory licensing of blacked-out PTSETs may contend that it will decrease gate receipts.[66] Gate receipts account for a significant portion of league revenues, and therefore a reduction in game attendance would harm the league and its member teams.[67] Further, a significant decline in game attendance

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"Satellite carriers" is defined by the Copyright Act as "an entity that uses the facilities of a satellite or satellite service . . . to establish and operate a channel of communications for point-to-multipoint distribution of television station signals . . . ." 17 U.S.C. § 119(d)(6) (1988).

"Cable systems" is defined by the Copyright Act as "a facility . . . that . . . receives signals transmitted or programs broadcast by one or more television broadcast stations . . . and makes secondary transmissions of such signals or programs by wires, cables, or other communications channels to subscribing members of the public who pay for such service." 17 U.S.C. § 111(f) (1988).

[62] 47 U.S.C. §§ 151–613 (1988 & Supp. V 1993).

[63] 47 U.S.C. § 605 (1988) (specifically addressing unauthorized publication or use of communications). For a discussion of the impact of § 605, see Michael E. Di Geronimo, *Protecting Wireless Communications: A Detailed Look at Section 605 of the Communications Act*, 38 COMM. L.J. 411 (1987).

[64] *See generally* Chris McConnell et al., *FOX Adds Pages to its Technology Playbook*, BROADCASTING & CABLE, Aug. 15, 1994, at 30 (detailing the satellite transmission scheme to be used by one network in its presentation of PTSETs).

[65] *See generally* RICK COOK & FRANK VAUGHN, ALL ABOUT HOME SATELLITE TELEVISION 100 (1983) (discussing issues of signal strength).

[66] *See generally* Nat'l Football League v. The Alley, Inc., 624 F. Supp. at 8 (stating that permitting establishments to televise a blacked-out PTSET would harm ticket sales).

The most optimistic observers of the PTSET and gate receipt issue contend that showing otherwise blacked-out PTSETs would increase interest in the local team, thereby increasing the demand for tickets to view in game in person. *See, e.g.*, Rice, *supra* note 43, at 426–28 & n.94.

[67] *See* Michael K. Ozanian et al., *The $11 Billion Pasttime*, FIN. WORLD, May 10, 1994, at 50, 52, 54, 56–57.

might alter on-field performances, making the events less exciting to see on television. Understandably, leagues are concerned with protecting their ticket sales. This concern, though facially plausible, may not be warranted. For the showing of a PTSET in a commercial establishment to decrease gate receipts significantly, the in-person experience and PTSET-experience must reasonably substitute for one another.[68] For some group of consumers, the products will be interchangeable; however, experience teaches that, in fact, the two are not perfect substitutes. In 1972, one commentator noted that "[m]any fans would not trade a stadium seat at the 20-yard line for a 50-yard line television seat in an easy-chair . . . . It might be simply the bark of the 'hot dog man,' or it might be the more complex exhilaration of being part of the crowd's reaction to a big play, but there is more to be seen and heard and felt at the stadium."[69] Another distinction is the pricing of each option. A ticket to a professional football game averages over thirty dollars,[70] whereas the charge to the consumer to watch a compulsory licensed PTSET could range from a nominal cover charge to an indirect charge in higher food and drink prices.

To illustrate the failure of a PTSET to act as a substitute to attending the live sporting event, consider the experience of the NFL's Washington Redskins. When an NFL team sells out its tickets 72 hours prior to the event, the resultant PTSET is provided on a cable or broadcast outlet.[71] Because standard television sets fall within the scope of section 110(5) of the Copyright Act,[72] commercial establishments may show the PTSET without violating any of the league's exclusive rights. Because the Washington Redskins typically sell out every regular season game,[73] the resulting PTSET is lawfully shown at commercial establishments across the Washington, D.C. metropolitan area. De-

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[68] *See* ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 59 (1993).

[69] Torrens, *supra* note 3, at 300 n.18.

[70] Jillian Kasky, *America's Best Sports Buys*, MONEY, Oct. 1994, at 158, 166. The National Basketball Association average ticket price is $27.17 and the Major League Baseball average ticket price is $10.62. *Id.*

[71] *See infra* notes 135–137 and accompanying text.

[72] *See* 1976 HOUSE REPORT, *supra* note 16, at 87 ("[T]he clause would exempt small commercial establishments whose proprietors merely bring onto their premises standard radio or television equipment and turn it on for their customers' enjoyment . . . .").

[73] John Ed Bradley, *Hello, Anybody Home?*, SPORTS ILLUSTRATED, Oct. 3, 1994, at 50, 53 ("The Redskins have had sellouts in [over 200] straight games (not including those played by replacements during the 1987 strike) at RFK since 1966.").

spite this wide availability of the PTSET in commercial establishments, the Redskins had to cap the waiting list for season tickets at 50,000 people.[74] Such a waiting list would not exist unless a PTSET and a game ticket were imperfect substitutes.

III. Legal Framework of Compulsory Licensing

This Part explains that the proposed compulsory license violates neither the Constitution nor the leading international copyright law treaty.

A. *The Constitution*

The Constitution speaks of the "exclusive right" of authors to their works.[75] The proposed compulsory licensing scheme could be found unconstitutional because it deprives leagues of the "exclusive right" to their blacked-out PTSETs by requiring licensing.[76] Cogently articulating the theory, one commentator argues that "Congress is given power and authority to grant only 'exclusive rights,' not limited rights and it seems probable that if Congress endeavored to graft onto our copyright laws a . . . requirement for compulsory license, that [it] would be beyond the powers of Congress, and so unconstitutional."[77] Opponents of prior proposed compulsory licenses have repeatedly, but heretofore unsuccessfully, raised the constitutional argument.[78] Yet, this argument remains available because the Supreme Court has not definitively determined the constitutionality of copyright compulsory licensing.[79]

The general consensus among commentators is that compulsory licensing provisions are constitutional because the copyright laws are statutory, not derived directly from the Constitu-

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[74] *See* David Aldridge, *Redskins Redistribute Some Tickets*, Wash. Post, June 2, 1994, at C4; *see also* Penny Ward Moser, *A Fan of the Ages*, Sports Illustrated, Sept. 9, 1987, at 10 (asserting that the current waiting list for Redskins season tickets will take over 350 years to fulfill).

[75] *See supra* note 12 and accompanying text.

[76] *See supra* notes 47–49 and accompanying text.

[77] Karl Fenning, *Copyright Before the Constitution*, 17 J. Pat. Off. Soc'y 379, 384–85 (1935).

[78] *See, e.g.*, B.R. Pravel, *Say 'No' to More Compulsory Licensing Statutes*, 2 Am. Pat. L. Ass'n Q.J. 185 (1974) (discussing the unconstitutionality of compulsory licensing provisions).

[79] Cassler, *supra* note 52, at 237.

tion.[80] As one commentator testified to Congress in 1909, with copyright law "Congress is creating a new property right, and in creating new rights Congress has the power to annex to them such conditions as it deems wise and expedient."[81] More recently, another commentator testified before Congress that "copyright is not a constitutional right, such as trial by jury of one's peers. The Constitution simply authorizes Congress to create the right. A copyright is therefore a statutory right—one created by law—and may be changed, enlarged, narrowed, or abolished altogether by the Congress."[82] In the event that the proposed compulsory license faces a court challenge, the Supreme Court would likely continue its historic approach of following the opinions of mainstream copyright law scholars,[83] and find the proposed compulsory license constitutional.

B. *The Berne Convention*

In 1988, the United States joined The Berne Convention for the Protection of Literary and Artistic Works ("Berne Convention").[84] The Berne Convention, "the leading international copyright treaty,"[85] lists minimum protection standards for member countries to follow in their domestic copyright law regime.[86] Article 11*bis* of

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[80] 1 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 1.07 (1963); Frank I. Schecter, *Would Compulsory Licensing of Patents Be Unconstitutional?*, 22 VA. L. REV. 287 (1935).

[81] TO AMEND AND CONSOLIDATE THE ACTS RESPECTING COPYRIGHT, H.R. Rep. No. 2222, 60th Cong., 2d Sess. 8 (1909).

[82] Hearing on H.R. 2223, *supra* note 19, at 200 (remarks of Edmon Low).

[83] The Supreme Court frequently relies on mainstream copyright scholarship, including that of the late Professor Nimmer. *See, e.g.*, Stewart v. Abend, 495 U.S. 207 (1990); Fortnightly Corp. v. United Artists Television, Inc., 392 U.S. 390 (1968).

[84] The Berne Convention was initially enacted in 1886. Convention for the Creation of an Intellectual Union for the Protection of Literary and Artistic Works, Sept. 9, 1886, 168 Consol. T.S. 185. Since its inception, it has been revised six times. LEAFFER, *supra* note 52, at 348. The most recent version of the Berne Convention for the Protection of Literary and Artistic Works was created on July 24, 1971 [hereinafter all references to the Berne Convention will be to this most recent revision].

In 1988, the United States became a member of the convention with the enactment of the Berne Convention Implementation Act of 1988. Pub. L. No. 100-568, 102 Stat. 2853 (1988).

For additional information on the substantive requirements of the Berne Convention and the issues surrounding its adoption by the United States, see SAM RICKETSON, THE BERNE CONVENTION FOR THE PROTECTION OF LITERARY AND ARTISTIC WORKS: 1886–1986 (1987); Jane C. Ginsburg & John M. Kernochan, *One Hundred and Two Years Later: The U.S. Joins the Berne Convention*, 13 COLUM.-VLA J.L. & ARTS 1 (1988).

[85] MICHAEL A. EPSTEIN, MODERN INTELLECTUAL PROPERTY § 5(I)(h) (1988).

[86] HOWARD B. ABRAMS, THE LAW OF COPYRIGHT § 18.02[C] (1991); *see* MARSHALL A. LEAFFER, INTERNATIONAL TREATIES ON INTELLECTUAL PROPERTY 340 (1990).

the Berne Convention states that "[a]uthors of literary and artistic work shall enjoy the exclusive right of authorizing" public broadcast or communication of their work.[87] The Berne Convention permits a compulsory license to interfere with this exclusive right only if the compulsory license does not (1) prejudice the author's "moral rights," (2) interfere with the author's "right to obtain equitable remuneration . . . fixed by a competent authority," and (3) apply extraterritorially.[88]

The proposed compulsory license meets the Berne Convention requirements. First, moral rights recognize that the author has a right to object to uses of the work that would harm the author's reputation or honor.[89] In the United States, moral rights are essentially protected by section 106(2) of the Copyright Act and section 43(a) of the Lanham Act, a United States trademark statute prohibiting a false designation of origin.[90] The proposed compulsory license does not interfere with the functioning of either section. Second, the article 11*bis* equitable remuneration requirement is satisfied because the proposed compulsory license would rely on the Librarian of Congress to establish fair market prices, the method used by existing copyright compulsory licenses.[91] Previous uses of government entities to set compulsory licensing rates have been deemed "likely" to meet the Berne Convention's requirement of fixation by a competent authority.[92] This proposal should be no exception. Third, the article 11*bis* requirement that the proposed compulsory license not apply extraterritorially is satisfied because it creates no extraterritorial obligations.

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[87] Berne Convention, *supra* note 84, at art. 11*bis* (1)(i).

[88] *Id.* at art. 11*bis* (2).

[89] *See id.* at art. 6*bis* (1).

[90] *See Final Report of the Ad Hoc Working Group on U.S. Adherence to the Berne Convention*, 10 COLUM.-VLA J.L. & ARTS 513, 548 (1986) (addressing the relevant provisions of U.S. law) [hereinafter *Final Report on Adherence*].

For a review of § 106(2) of the Copyright Act, see *supra* note 25.

The Lanham Act is the federal trademark law. *See* 15 U.S.C. §§ 1051–1127 (1988 & Supp. V 1993). Section 43(a) of the Lanham Act forbids a seller from falsely designating a good's origin. *See id.* at § 1125 (1988 & Supp. V 1993); *see also* ABRAMS, *supra* note 86, at § 18.02[C][2]; *Final Report on Adherence*, *supra*, at 553–56.

[91] *See supra* note 50 and accompanying text.

[92] *Final Report on Adherence*, *supra* note 90, at 562–63.

IV. MITIGATING MONOPOLISTIC BEHAVIOR

The strongest argument for adoption of the proposed compulsory license is the mitigation of monopolistic behavior, a rationale used to justify a subset of the existing copyright compulsory licenses.[93] Scholars have amply studied and commented on the societal impact of monopolistic behavior. One leading group of scholars asserts that "[t]he general theory of a competitive free market economy shows that monopoly will reduce overall welfare by providing distorted price signals to consumers, causing them to purchase the wrong combination of goods and services to maximize their welfare."[94] Other mainstream commentators argue that antitrust law is concerned with preserving small businesses, protecting against oppression and unfair dealings, and controlling large corporate power.[95] For this discussion, it is sufficient to note that most commentators believe that monopolistic behavior generally harms society and should therefore be discouraged.[96]

Mitigation of monopolistic behavior provided the impetus in 1909 for Congress to enact the first copyright compulsory license.[97] A brief examination of the events prompting congressional action in 1909 provides a clearer understanding of the rationale of mitigating monopolistic behavior.

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[93] *See* Cassler, *supra* note 52, at 255. Other rationales previously used to justify establishment of existing compulsory licenses include protection of industries operating in the public interest, protection of emerging industries, and mitigation of uncontrolled copying. *Id.* at 244–57.

[94] Katherine Maddox McElroy & John J. Siegfried, *The Economics of Antitrust Enforcement*, 20 SURV. BUS. 10, 19 (1984); *see also* BORK, *supra* note 68, at 71, 89; RICHARD A. POSNER, ANTITRUST LAW: AN ECONOMIC PERSPECTIVE 18–20 (1976).

[95] *See Antitrust Jurisprudence: A Symposium on the Economic, Political and Social Goals of Antitrust Policy*, 125 U. PA. L. REV. 1128 (1977).

[96] E. THOMAS SULLIVAN & JEFFREY L. HARRISON, UNDERSTANDING ANTITRUST AND ITS ECONOMIC IMPLICATIONS 1 (2d ed. 1994). For an examination of the competing view of antitrust law, see William C. Page, *Ideological Conflict and the Origins of Antitrust Policy*, 86 TUL. L. REV. 1 (1991).

[97] *See* Standard Music Roll v. Mills, 241 F. 360, 363 (3d Cir. 1917) ("The object of these [compulsory licensing] provisos seems to be the prevention of monopoly or favoritism."); *see also* Cassler, *supra* note 52, at 252.

A. *The 1909 Compulsory License*

In 1909, Congress reacted to the monopolistic behavior of Aeolian Company, producers of player-piano rolls, the most popular form of musical reproduction at that time.[98] Congress became concerned that Aeolian's exclusive agreements with over eighty music publishers would completely restrict the marketplace entry of Aeolian's competitors.[99] To reduce the impact of Aeolian's monopolistic behavior, Congress adopted a compulsory license provision.[100]

For a license to have been compulsory under the created provision, the copyright owner must have (1) mechanically reproduced the composition; (2) permitted others to reproduce the composition; or (3) knowingly acquiesced in allowing others to reproduce it.[101] The compulsory license provided that "[a]ny person may reproduce mechanically the musical copyright, upon payment of a statutory royalty" of two cents per record or roll.[102] Continued concerns over the effects of monopolistic behavior prompted Congress to include a modified form of the 1909 compulsory license provision in the current Copyright Act.[103]

B. *Monopolistic Behavior Analysis*

Two manifestations of monopolistic behavior provide a basis for adopting a compulsory license for the public performance of blacked-out PTSETs.[104] The first focuses on an antitrust exemption that permits a league to pool its member teams' televi-

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[98] Cassler, *supra* note 52, at 252. The popularity of the player piano reached its peak in 1923, but rapidly declined due to the Depression, and the advent of radio and gramophone. Frank W. Holland, *Player Piano*, *in* 3 THE NEW GROVE DICTIONARY OF MUSICAL INSTRUMENTS 131 (Stanley Sadie ed., 1984).

[99] Cassler, *supra* note 52, at 252.

[100] *Id.* (citing H. Rep. No. 2222, 60th Cong., 2d Sess. 7–9 (1909); *Hearings on H.R. 4347, H.R. 5680, H.R. 6831, H.R. 6835 Before Subcomm. No. 3 of the Committee on the Judiciary*, 89th Cong., 1st Sess. 675–76 (1965) (statement of Recording Industry Association of America)). When adopted, this compulsory license was termed a mechanical license. *See* LEAFFER, *supra* note 52, at 212.

[101] Act of Mar. 4, 1909, § 1(e)(C).

[102] *Id.*

[103] *See* 17 U.S.C. § 115 (1988).

[104] This discussion focuses on only two of the many antitrust issues in professional sports. For a discussion of additional aspects of monopolistic behavior in professional sports leagues, see Stephen F. Ross, *Monopoly Sports Leagues*, 73 MINN. L. REV. 643 (1989) [hereinafter Ross I]. For a condensed treatment, see Stephen F. Ross, *Break Up the Sports League Monopolies*, in THE BUSINESS OF PROFESSIONAL SPORTS 152 (Paul D. Staudohar & James A. Mangan eds., 1992) [hereinafter Ross II].

sion rights.[105] The second concerns a league's use of its exclusive expansion power to extract state and municipal subsidies.[106]

1. The Sports Broadcasting Act of 1961

Enacting a compulsory license for the public performance of blacked-out PTSETs would curtail monopolistic behavior resulting from the Sports Broadcasting Act of 1961 ("SBA").[107] The SBA was the first congressional antitrust exemption granted to professional sports leagues.[108] The SBA explicitly grants an antitrust exemption to professional baseball, basketball, football, and hockey leagues, allowing each league to pool[109] its member teams' PTSETs.[110] Congress created the SBA in response to *United States v. Nat'l Football League*.[111] In this case, the district court held that a two-year, $9.3 million contract between the NFL and Columbia Broadcasting System for the pooled sale of television rights violated antitrust law.[112] The court based its decision on its finding eight years prior that the NFL constituted a group of individual entities conspiring to violate section 1 of the Sherman Antitrust Act.[113] Passage of the

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[105] *See infra* notes 107–139 and accompanying text.

[106] *See infra* notes 140–175 and accompanying text.

[107] Pub. L. No. 87-331, § 1, 75 Stat. 732 (codified as amended at 15 U.S.C. §§ 1291–1295 (1988)).

[108] PAUL C. WEILER & GARY R. ROBERTS, SPORTS AND THE LAW 415 (1993). The judicial branch had found all previous antitrust exceptions. *Id.*

[109] "Pooling" means that the league acquires the rights to its member teams' PTSETs, and then the league markets the PTSETs as a package.

[110] In relevant part, the SBA states:

> Anti-trust laws . . . shall not apply to any joint agreement by or among persons engaging in or conducting the organized professional team sports of football, baseball, basketball, or hockey, by which any league of clubs . . . sells or otherwise transfers all or any part of the rights of such league's member clubs in the sponsored telecasting of the games . . . .

15 U.S.C. § 1291.

Congress's explicit inclusion of professional baseball was curious in light of the game's existing antitrust exemption. *See* Federal Baseball Club of Baltimore, Inc. v. Nat'l League of Professional Baseball Clubs, 259 U.S. 200 (1922) (granting professional baseball its antitrust exemption); Flood v. Kuhn, 407 U.S. 258, 282–83, 285 (1972) (upholding the exemption). Inclusion, however, proved beneficial for Major League Baseball when in 1982 a United States District Court found that professional baseball's general antitrust exemption did not encompass broadcasting. Henderson Broadcasting Corp. v. Houston Sports Ass'n, 541 F. Supp. 263 (S.D. Tex. 1982).

[111] 196 F. Supp. 445 (E.D. Pa. 1961).

[112] *Id.* at 447.

[113] *Id.* (citing United States v. Nat'l Football League, 116 F. Supp. 319 (E.D. Pa. 1953)). Section 1 of the Sherman Act explicitly prohibits separate economic entities in the same marketplace from engaging in activity that restrains trade. 15 U.S.C. § 1. For a discussion supporting the premise that member teams of a league do not constitute

SBA's antitrust exemption overruled the district court's decision by permitting leagues to engage in monopolistic behavior.[114]

On the rare occasion when Congress provides an antitrust exemption, Congress promulgates concomitant legislation designed to limit the exemption's harm to consumers.[115] The SBA, however, contains no limitations designed to prevent the evils of monopoly[116]—reduced output and increased price[117]—in geographic areas with the strongest demand.[118] Thus, using black-outs, leagues have reduced the output of PTSETs and increased the licensing price.[119] Given the leagues' monopoly power over PTSETs,[120]

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a single entity for antitrust analysis purposes, see Lee Goldman, *Sports, Antitrust, and the Single Entity Theory*, 63 TUL. L. REV. 751 (1989).

For a group of scholarly articles expressing, counter to the district court's finding, that professional sports leagues are single entities, see Myron C. Grauer, *Recognition of the National Football League as a Single Entity Under Section 1 to the Sherman Act*, 82 MICH. L. REV. 1 (1983); Gary R. Roberts, *The Single Entity Status of Sports Leagues Under Section 1 of the Sherman Act: An Alternative View*, 60 TUL. L. REV. 562 (1986); Gary R. Roberts, *Sports Leagues and the Sherman Act: The Use and Abuse of Section 1 to Regulate Restraints on Intraleague Rivalry*, 32 UCLA L. REV. 219 (1984); John Weistart, *League Control of Market Opportunities: A Perspective on Competition and Cooperation in the Sports Industry*, 1984 DUKE L.J. 1013.

[114] Allowance of league-pooled television contracts has proven instrumental to the financial success of professional baseball, basketball, football, and hockey. *See Hearings on Copyright Law Revision Before the Subcomm. on Patents, Trademarks, and Copyright of the Comm. on the Judiciary*, 93d Cong., 1st Sess. 551, 552 (1973) (statement of J. Walter Kennedy, then-Commissioner of the National Basketball Association) ("In recent years, a major factor for the members of the National Basketball Association has been the NBA's ability to sell television rights . . . . The revenue received as a result of this sale of the right to broadcast certain games has kept many NBA teams alive."); Anthony Baldo et al., *Secrets of the Front Office; What America's Pro Teams are Worth*, FIN. WORLD, July 9, 1991, at 28, 30 ("TV's importance to [league] profits is well reported, but it becomes more pronounced when compared with revenue from other sources.").

[115] Ross I, *supra* note 104, at 644.

[116] *Id.*

[117] *See* Phillip Areeda, *Introduction to Antitrust Economics*, 52 ANTITRUST L.J. 523, 525 (1983) (stating the harms of monopoly).

[118] This requires an assumption that demand for a particular PTSET is strongest in the geographic area a team represents. While not always true in the event of displaced fans, its high probability makes the assumption quite reasonable.

[119] *See supra* notes 43–45 and accompanying text (discussing league reluctance to license blacked-out PTSETs). In essence, the leagues' refusal to offer PTSETs for licensing constitutes an increase in price. There exists some price at which a league may deem it profitable to license a blacked-out PTSET, but this cost is so high that no commerical establishment would consider the licensing fee profitable.

[120] In fact, the leagues maintain monopoly power on two related products: PTSETs and tickets. Black-outs limit the output of PTSETs in order to encourage consumers to substitute more expensive game tickets, as to which the leagues may price discriminate.

Price discrimination is the activity of selling similar products to different consumers at different prices. *See* O. Hommel Co. v. Ferro Corp., 659 F.2d 340, 346 (3d Cir. 1981), *cert. denied*, 455 U.S. 1017 (1982). "Price discrimination is not illegal per se." *Id.*

Although two products are related, they are not necessarily complements, such as parts and labor. Accordingly, mitigating the monopoly power over PTSETs will not

that price is closer to a monopoly price[121] than marginal cost.[122]

A compulsory license for the public performance of blacked-out PTSETs would impose the first direct safeguard on the SBA-resultant monopolistic behavior.[123] The proposed compulsory license increases current output levels by providing consumers lacking in-home satellite television an opportunity to patronize a commercial establishment and watch a PTSET previously unavailable at a commercial establishment.[124] The proposed compulsory license would make PTSET licenses available at a fair rate of return.[125] Some economists might assert that the optimal price is the marginal cost of the PTSET. Because not all sports teams are primarily operated with a profit motive,[126] however, other economists may claim that even the marginal cost of the PTSET would be too high a fee because the cost need not include the reasonable rate of return factored into the marginal cost.[127] Under either analysis, the cost is less than the current price for licensing blacked-out PTSETs.[128]

Opponents of the proposed compulsory license may maintain that adopting it based on mitigating SBA-resultant monopolistic behavior misperceives the nature of the SBA antitrust exemption.[129] While there may be little debate that the SBA qualifies as an antitrust exemption,[130] opponents would vehemently con-

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necessarily effect monopoly pricing of tickets; conversely, monopoly power over PTSETs will not necessarily persist because of monopoly pricing of tickets. *See* Glynn S. Lunney, Jr., *Another View of* Eastman Kodak v. ITS, COMPUTER LAW., Nov. 1992, at 22 (stating that possessing monopoly power over one group of complementary products is the functional equivalent of possessing monopoly power over an entire group of complementary products).

[121]Monopoly price is the price at which the balancing of lower output and higher price maximizes profits. Glynn S. Lunney, Jr., Atari Games v. Nintendo: *Does a Closed System Violate the Antitrust Laws?*, 5 HIGH TECH. L.J. 29, 36 (1990). For a detailed discussion of finding monopoly price, see POSNER, *supra* note 94, at 237–55.

[122]Marginal cost is the "extra or additional cost of producing another unit of ouput." PAUL A. SAMUELSON & WILLIAM D. NORDHAUS, ECONOMICS 463 (12th ed. 1985). It includes manufacturing and distribution costs, as well as a reasonable rate of return. Lunney, *supra* note 121, at 36 n.38.

[123]*See supra* note 118 and accompanying text.

[124]The distinction for in-home viewing is made because of the compulsory license for home use of satellite equipment. *See supra* note 58 and accompanying text.

[125]*See supra* note 61 and accompanying text.

[126]*See, e.g.*, Rick Reilly, *The Hand that Feeds Them*, SPORTS ILLUSTRATED, Sept. 10, 1990, at 122 (profiling the owner of the San Francisco 49ers, Eddie DeBartolo Jr.).

[127]*See supra* note 121.

[128]*See supra* note 119 (noting that no offer price has been established because leagues have refrained from licensing their blacked-out PTSETs).

[129]*See supra* notes 118–122 and accompanying text.

[130]*See supra* notes 108–114 and accompanying text.

tend that both formal and informal consumer-protective edicts control the SBA. They may argue that on a formal basis the SBA provision preventing a league from blacking out games except within a member team's "home territory"[131] on the day of a home game limits a league's absolute ability to control output.[132] Although the "home territory" limitation appears to create a minimum level of output, consumers located in the geographic area a specific team represents remain unprotected. Accordingly, the limitation provides incomplete consumer protection against this type of monopolistic behavior.

Further, compulsory licensing opponents would contend that on an informal basis, leagues abide by an expired statute specifically designed to protect consumers in the geographic area most harmed by a specific black-out. The law was enacted in 1972 after Washington Redskins fans in Congress were outraged that the team's playoff game would not be televised.[133] As one commentator has observed: "[b]lacking out games in Minneapolis or Dallas largely annoyed only the citizens living in those communities, but blacking out the first Redskins playoff game in the nation's capital in several years affected the politically powerful."[134] Among other things, the enacted law prohibited a black-out of a local PTSET in a team's "home territory"[135] when all of the tickets to the event are sold 72 hours prior to the event.[136] The statute's own terms provided for its expiration on December 31, 1975,[137] which it did. Nevertheless, leagues, spe-

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[131] 15 U.S.C. § 1292. "The term 'home territory' is not susceptible of a single definition that will be suitable for all professional football, baseball, basketball and hockey leagues. By 'home territory' the [Senate] means such home territory as is recognized by a particular league's bylaws or custom and usage." H.R. REP. No. 1178, 87th Cong., 1st Sess. 2 (1961). For example, the NFL defines home territory as a 75-mile radius from the site of the game. CONSTITUTION AND BY-LAWS FOR THE NATIONAL FOOTBALL LEAGUE, art. 4.1 (1976 & Supp. 1993). NFL rules further dictate that when two NFL teams' home cities are closer than 100 miles to one another, their home territory boundary becomes equidistant. *Id.*

[132] Another limitation exists in the SBA to control total PTSET output by preventing professional football from scheduling games as to directly compete with Friday night high school football games or Saturday college football games. 15 U.S.C. § 1293. Although this provision does control output, it does not address the SBA's failure to control monopolistic harms. *See supra* notes 115–122 and accompanying text.

[133] Gary R. Roberts, *Pirating Satellite Signals of Blacked-out Sports Events: A Historical and Policy Perspective*, 11 COLUM.-VLA J.L. & ARTS 363, 370 (1987).

[134] *Id.*

[135] Pub. L. No. 93-107, 87 Stat. 305 (codified as amended at 47 U.S.C. § 331) (expired Dec. 31, 1975).

[136] 47 U.S.C. § 331(a).

[137] *Id.* at § 331(b).

cifically the NFL, continue to abide by the 72 hour rule, fearing that a failure to do so would result in passage of new, harsher legislation, or reintroduction of the original law, including other original provisions that leagues found highly objectionable.[138] As such, the modicum of consumer protection informally provided exists only as long as a league believes that the cost of congressional action would outweigh the additional revenue from further monopolistic behavior.[139] Allowing a primary antitrust limitation to exist in such a tenuous state means that consumer protection exists only when it is in the monopolist's best interests. Enacting a compulsory license for the public performance of blacked-out PTSETs would ensure sustained consumer protection from SBA-resultant monopolistic behavior, regardless of the monopolist's best interests.

As the above SBA-based analysis demonstrates, existing restraints on the SBA do not sufficiently restrict potential exploitation of the SBA-granted antitrust exemption. Because no meaningful rigid limits or safeguards exist, leagues may continue to engage in unrestricted monopolistic behavior, thereby generating monopolistic evils. Congress could rectify this situation by implementating the proposed compulsory license.

2. State and Municipal Subsidies

Federal antitrust exemptions demonstrate one form of monopolistic behavior; state and municipal subsidies to professional sports teams demonstrate another. State and municipal subsidies have included millions of dollars for construction of new facilities,[140] expansion of existing facilities,[141] loans and loan

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[138] Interview with Gary R. Roberts, Vice-Dean and Professor at Tulane Law School, in New Orleans, La. (Jan. 18, 1994).

[139] *See generally* Modigliani & Miller, *supra* note 43 (noting that profit-maximizing organizations will undertake activities they perceive will provide the greatest economic return).

[140] *See, e.g.*, Rob Karwath, *Comiskey Makes State a Winner*, CHI. TRIB., Aug. 25, 1992, at C1 (reporting that the state of Illinois issued $150 million in bonds to build a new stadium for the Chicago White Sox).

[141] *See, e.g.*, Dan Rottenberg, *Goode was Right in Saving Eagles in the Long Run, Those Skyboxes Will be a Cash Cow for the City*, PHILA. INQUIRER, Oct. 9, 1989, at A9 (stating that the city of Philadelphia provided the Philadelphia Eagles with $8 million to build skyboxes in Veterans Stadium; although the skyboxes are city property, the football team retains all revenues generated by the skyboxes until year 2000).

guarantees,[142] free rent on playing facilities,[143] and guaranteed income.[144] These types of subsidies have become the norm with professional league sports.[145]

Legislative subsidies result from the tight control each league maintains over expansion. For example, both the NFL and the National Hockey League require a three-fourths affirmative vote of existing league member teams to admit a new team to each respective league.[146]

Using its power, each league limits the number of its member teams to ensure that the number of areas able to support a professional team[147] eclipse the number of professional teams.[148] By limiting the supply, leagues implicitly encourage areas to vie

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[142] *See, e.g.*, Jeff Jacobs, *Keeping Hockey in Hartford*, HARTFORD COURANT, Oct. 2, 1992, at A1 (stating that the state of Connecticut lent the Hartford Whalers $4 million and provided a $10 million loan guarantee).

[143] *See, e.g.*, Rob Hotakainen, *Twins Win 10-year Rent Free Lease and Will Get Bigger Cut of Concessions*, STAR-TRIB. (Minneapolis), May 18, 1989, at 1B (reporting that Minnesota Twins' lease was amended to allow them to play rent-free at the Hubert H. Humphrey Metrodome for 10 years).

[144] Jane Leavy, *Colts' 20-year Lease Approved Formally*, WASH. POST, Apr. 1, 1984, at D4 (reporting that city of Indianapolis enticed the Baltimore Colts to move with $7 million-per-year guaranteed income from ticket sales, for 12 years; pre-season television rights; and regular-season radio rights).

[145] *See generally* CHARLES C. EUCHNER, PLAYING THE FIELD (1993) (detailing the methods used by teams and leagues to extract subsidies).

[146] CONSTITUTION AND BY-LAWS FOR THE NATIONAL FOOTBALL LEAGUE, art. 3.1(b) ("The admission of a new member club . . . shall require the affirmative vote of three-fourths of the existing member clubs of the [National Football] League."); NATIONAL HOCKEY LEAGUE CONST. art. 3.3 (three-fourths vote of member teams of the National Hockey League is required for admission of a new team).

[147] No precise formula exists to gauge whether a city is able to support a professional team. *See* Ross I, *supra* note 104, at 661–62. Several factors, however, are instrumental in this respect, including population, size of television market, proximity to competing franchises, local demographics, and local interest. In an attempted assessment, one commentator argued that enough cities will be able to support a baseball team by 2004 for Major League Baseball to expand to 40 teams. *See* ZIMBALIST, *supra* note 11, at 123–46, 167–86.

[148] Professional Sports Community Protection Act of 1985, Hearings Before the Committee on Commerce, Science, and Transportation, 95th Cong., 1st Sess., 168 (Letter from Professor Roger G. Noll to Sen. John C. Danforth (R-Mo.), Feb. 9, 1985) [hereinafter Noll Letter]; Ross I, *supra* note 104, at 650–51.

Even when a league chooses to expand, the number of teams to be added to the league falls short of the number of communities able and ready to support a team. *See, e.g, Slim Possibility Exists for a 3-Team Expansion: Chance Encourages No. Virginia Groups*, WASH. POST, Feb. 3, 1995, at B7 (stating that there are four communities vying for the possible three expansion teams of Major League Baseball); Chris Mortensen, *Dead Heat*, THE SPORTING NEWS, Oct. 23, 1993, at 25 (stating that five communities actively sought one of two NFL expansion teams). Other factors may affect expansion, such as basic logistics and dilution of talent; nonetheless, the trend is that leagues choose to expand only when there are more available communities than there are available new teams.

for an existing or newly created team by offering subsidies.[149] In addition to the desire to maintain a greater demand for teams than there are teams to allocate, little incentive exists for any team to vote to include a new member team, because doing so would reduce each member team's share of the league marketplace and pooled league revenues.[150] The situation qualifies as "a straightforward monopoly problem: each league is a monopolist in membership in that league, and monopolists maximize profits by artificially curtailing output."[151] Accordingly, the subsidies result from the monopolistic behavior of each league.

A 1987 independent study examines the economic effects of subsidizing professional sports and sports stadiums.[152] The study, by Professor Robert A. Baade, employs statistical analysis[153] to determine the short- and long-term effects of professional sports and sports stadiums in twelve United States cities.[154] As Baade indicates, the slight differences between the long- and short-term cities and years selected for analysis are the result of finding reliable data from which to determine a trend.[155] In examining the short-term effects between 1963 and 1983 on Atlanta, Buffalo, Cincinnati, Denver, Detroit, Kansas City, Miami, New Orleans, Pittsburgh, San Diego, Seattle, and Tampa Bay, Baade found that "[i]n no instance did a positive significant correlation surface among stadiums, professional sports, and city income as a fraction of regional income."[156] In fact, the analysis indicates that in over half of the areas examined, a "significant *negative*

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[149] Ross I, *supra* note 104, at 650–51 (terming a league's use of this bargaining power "extort[ion].").

Threats to move from one geographic area to another are not idle. Between 1950 and 1984, there were a combined 68 moves by professional baseball, basketball, football, and hockey teams. WARREN FREEDMAN, PROFESSIONAL SPORTS AND ANTITRUST 79 (1987).

[150] Leagues regularly place significant conditions on expansion to offset the reduction in shared revenues. For example, the NFL required its most recent expansion teams to pay $140 million to the league as an entry fee and limited the new teams to a one-half share of pooled television revenues during their first three years of operation. Richard O'Brien, *Ouch!*, SPORTS ILLUSTRATED, June 7, 1993, at 11, 12.

[151] Noll Letter, *supra* note 148, at 168.

[152] Robert A. Baade, *Is There an Economic Rationale for Subsidizing Sports Stadiums?*, HEARTLAND INST. (1987) (on file with the *Harvard Journal on Legislation*).

[153] Statistical analysis is used by economists to correlate the economic effects of specific behavior. It neither proves nor disproves a hypothesis; it merely supports or undermines one.

[154] *Id.* at 14–17. A complete examination of Professor Baade's methods and techniques is beyond the scope of this Article.

[155] *Id.* at 17.

[156] *Id.* at 15.

impact" resulted.[157] Baade then examined the long-term effect, between 1965 and 1987, on Buffalo, Cincinnati, Denver, Miami, New Orleans, San Diego, Seattle, and Tampa Bay.[158] His results indicate that in the long run stadiums and professional teams are not the economic catalyst they are often heralded to be; rather, they divert economic development from the manufacturing sector to the service sector.[159] Baade concludes that "[c]ontrary to the claims of city officials, . . . [professional] sports and [sports] stadiums frequently had no significant positive impact on a city's economy, and, in a regional context, may actually contribute to a reduction in a sports-minded city's share of regional income."[160]

Baade's findings are supported by other economists and anecdotal evidence. In addressing the expansion of Major League Baseball into south Florida, Professor Roger G. Noll states that professional sports cause a different allocation of money in an area, but not an overall influx: "restaurants and gas stations near the ballpark do a little better, and the gas stations and restaurants in the other parts of town do a little worse."[161] Professor Noll further states that "for broad economic impact, [an area] is better off with a new Macy's" than a new professional sports team.[162] Also addressing the recent expansion of Major League Baseball into south Florida, Professor Gerald Scully states that "[i]t's a great stretch of the imagination to talk about the growth of income in the region" as a result of a new team.[163] Addressing Baltimore's subsidy of the recently constructed Oriole Park at Camden Yards, Noll states that "[w]ith $200 million [spent on stadium construction], you could go out and build an industrial park and generate 10 to 100 times as much taxes and jobs" than a stadium provides.[164] Echoing this theme is one Baltimore community leader's experience, who states that "[w]hat we have discovered is that the jobs available at the ballpark are mostly low wage, largely temporary and seasonal . . . ."[165]

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[157] *Id.*
[158] *Id.* at 17.
[159] *Id.*
[160] *Id.* at 18.
[161] Gregg Fields, *For the Local Economy, It's a Solid Hit But Hardly a Home Run*, MIAMI HERALD, June 24, 1991, at 22BM.
[162] *Id.*
[163] *Id.* at 23BM.
[164] Chris Kraul, *Field of Dreams*, L.A. TIMES, July 11, 1993, at 1D.
[165] *Id.* (quoting Kathleen O'Toole, organizer for Baltimoreans United in Leadership Development).

Because these league subsidies generally do not benefit the subsidizing area[166] and are attained through monopolistic behavior, the subsidies represent a reduction of consumer surplus.[167] The proposed compulsory license may mitigate the negative economic effect of the leagues' monopolistic behavior toward expansion by providing the subsidizing areas a means to recover a portion of the extracted subsidy.[168] The recovery would result by providing an opportunity for more of the subsidizing area's taxpayers to view the blacked-out PTSET.

Opponents of the compulsory license may note that some economists find a positive correlation between subsidies and local economic gain.[169] In one specific contrasting example, Baade found that subsidies to the Louisiana Superdome in New Orleans have a negative economic effect on the subsidizing area,[170] while another group of academics found that the same subsidies result in an economic gain to the area.[171] Such conflicts may lead some opponents to argue that economic modeling yields arbitrary results, and arbitrary results should not be used as a basis to alter a well-established intellectual property right. Arguments against modeling, however, are misplaced because conflicting model results serve only to illustrate the complexity of developing an accurate economic model of state and municipal subsidies, not modeling's hollow value. Existing economic models should be refined to better reflect economic reality, with an emphasis on eliminating internal transfers of wealth as an economic gain.

The opponents may further argue that determining the most representative economic model is moot because subsidies are justified in order to allow a professional sports team or league to internalize their externalities. An externality is any "activity that affects others for better or worse, without those others paying or being paid for the activity."[172] Although correcting an

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[166] *See supra* notes 152–165 and accompanying text.

[167] *See generally* 3 ALFRED MARSHALL, PRINCIPLES OF ECONOMICS ch. 6 (9th ed. 1961).

[168] *See supra* notes 140–151 and accompanying text.

[169] *See, e.g.*, Edward B. Shils, Report to the Philadelphia Professional Sports Consortium on its Contributions to the Economy of Philadelphia (1985) (on file with the *Harvard Journal on Legislation*).

[170] Baade, *supra* note 152, at 7.

[171] *See* Eddystone C. Nebel et al., The Economic Impact of the Louisiana Superdome: 1975–1985 (1985) (on file with the *Harvard Journal on Legislation*).

[172] SAMUELSON & NORDHAUS, *supra* note 122, at 905; *see also* RONALD H. COASE, THE FIRM, THE MARKET, AND THE LAW 24 (1988) ("An externality is . . . usually defined as the effect of one person's decision on someone who is not a party to that decision."). One author provides the following example: "If a smoker does not bear

externality is a legitimate purpose of the law,[173] the law should allow only a recovered sum that approximates the value of the unrecovered benefit. Although league sports capture much of the value they generate through gate receipts, television contracts, promotional agreements, and increased team value, opponents would correctly note that some externalities exist. The externalities, such as increased civic pride, national recognition, and increased tourism,[174] are all areas in which leagues and teams do not recover for the benefits provided. These values are not easily recaptured because it is often impossible to prevent individuals or organizations from enjoying the benefits without paying for them.[175]

Subsidies established by a legitimate calculation of unrecovered benefits would qualify as economically efficient. With current subsidies, however, no effort exists to establish a subsidy at an appropriate level of recovery. Absent such effort, subsidies plainly reflect the flexing of monopolistic muscle. To mitigate the decline in consumer surplus wrought by monopolistic behavior, a compulsory license for the public performance of blacked-out PTSETs could be enacted. Enacting such a compulsory license would permit more taxpayers in the subsidizing area to view blacked-out PTSETs, thereby offsetting the decline in consumer surplus.

V. CONCLUSION

A compulsory license for the public performance right to blacked-out PTSETs would mitigate the monopolistic behavior of professional sports leagues. Such a mitigating effect is consistent with prior uses of compulsory licensing,[176] thereby pro-

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the costs that her habits impose on others, this is a 'negative' externality that may lead to overconsumption; if a homeowner cannot charge for the benefits her beautiful outdoor garden brings to her neighbors, this is a 'positive' externality that may lead to underproduction." Edward J. McCaffery, *Taxation and the Family: A Fresh Look at Behavioral Gender Biases in the Code*, 40 UCLA L. REV. 983, 1048 (1993)

[173] RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 254 (4th ed 1992) ("[T]he most dramatic economic function of the common law is to correct externalities."); Harold Demsetz, *Toward a Theory of Property Rights*, 57 AM. ECON. REV. 347, 348 (1967) ("A primary function of property rights is that of guiding incentives to achieve a greater internalization of externalities.").

[174] *See, e.g.*, Donn Esmonde, *Point After: The January Thaw*, SPORTS ILLUSTRATED, Feb. 1, 1993 at 64 (describing the civic benefits resulting to Buffalo from their professional football team's entry in the Super Bowl).

[175] *See* JOSEPH E. STIGLITZ, ECONOMICS OF THE PUBLIC SECTOR 219 (2d ed. 1986).

[176] *See supra* notes 97, 101 and accompanying text.

viding a legitimate basis for proponents to advocate its adoption.

In 1981, the Register of Copyrights stated that "copyright owners should fully enjoy all their property rights, and that compulsory licensing schemes . . . should be employed sparingly and only where necessary."[177] Mitigation of monopolistic behavior represents one area in which compulsory licensing has been deemed necessary.[178] Although league divestiture[179] or forced expansion[180] may be the most pointed solution, mitigating effects of monopolistic behavior using copyright law represents one intermediate alternative.[181] This analysis, however, concludes that the proposed compulsory license should be considered an option. This conclusion does not imply that the compulsory license represents the most economically desirable option. Rather, the compulsory license proposal should be evaluated on its own merits and in conjunction with other options to determine its overall effect.[182]

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[177] Oversight of the Copyright Act of 1976: Hearings on Cable Television Before the Senate Comm. on the Judiciary, 97th Cong., 1st Sess. 3, 6 (1981) (statement of David Ladd). Mr. Ladd is the only person to have served as both Commissioner of Patents (1961–1963) and Register of Copyrights (1980–1985). *David Lowell Ladd Dies at 68*, WASH. POST, Oct. 13, 1994, at C4.

In a statement made almost 25 years earlier, in 1966, then-Register of Copyrights Abraham Kaminstein testified to Congress that "[a] compulsory license provision has to be used in a very guarded fashion, that is, only when it is absolutely necessary." *Copyright Law Revision-CATV, Hearings Before the Subcomm. on Patents, Trademarks, and Copyright of the Comm. on the Judiciary*, 89th Cong., 2d Sess. 6, 12 (1966).

[178] *See supra* notes 97, 101 and accompanying text.

[179] *See generally* Ross I and Ross II, *supra* note 104 (discussing divestiture as an option to mitigate monopolistic behavior).

[180] *See, e.g.*, Mark Asher, *Senate Bill Amendments Would Require the NFL and Baseball to Expand*, WASH. POST, Sept. 6, 1984, at E7 (noting that a bill before Congress would require the NFL to add four teams and Major League Baseball to include two additional teams).

[181] *See generally* Barbara Ringer, *Copyright and the Future of Authorship*, 101 LIB. J. 229, 231 (1976) ("Now, and even more in the future, [congressional intellectual property] compromises seem likely to consist of compulsory licensing.").

The Supreme Court has stated that when Congress attempts to solve a problem, it may proceed "one step at a time" and address "the phase of the problem which seems most acute" to Congress. "The legislature may select one phase of one field and apply a remedy there, neglecting the others." Williamson v. Lee Optical of Oklahoma, 348 U.S. 483, 489 (1955) (citations omitted). In the event Congress perceives that the professional sports leagues were exploiting monopoly power in regards to PTSETs, implementation of a compulsory license would prove far more expedient in solving the problem than an antitrust-based action.

[182] *See, e.g.*, Alan M. Fisch, *Compulsory Licensing of Pharmaceutical Patents: An Unreasonable Solution to an Unfortunate Problem*, 34 JURIMETRICS J. 295 (1994) (finding through economic analysis that compulsory licensing of pharmaceutical patents would likely be detrimental to society).

ARTICLE

THE RIGHT TO KNOW: AN ARGUMENT FOR INFORMING EMPLOYEES OF THEIR RIGHTS UNDER THE NATIONAL LABOR RELATIONS ACT

PETER D. DECHIARA*

Under current law employers must post notices informing employees of rights granted under a variety of statutes. In this Article Mr. DeChiara proposes that a brief outline of the right to organize granted under the National Labor Relations Act should be added to this list. He argues that employee ignorance of their rights combined with the ability of employers to wage misleading campaigns deters concerted activity among employees. A National Labor Relations Board rule providing for mandatory notice with adequte penalties, according to the author, would help curb the decline of unions in the American workforce while imposing little cost on employers.

The precipitous decline of collective bargaining in this country[1] has triggered numerous proposals to amend the National Labor Relations Act (NLRA or the Act),[2] both from academic commentators[3] and from labor's allies in Congress.[4] Indeed, Presi-

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[1] As of 1989, unions represented just 12% of the employees in the private-sector workforce, down from 24% in 1978 and 38% in 1954. *See* Joel Rogers, *In the Shadow of the Law: Institutional Aspects of Postwar U.S. Union Decline*, *in* LABOR LAW IN AMERICA: HISTORICAL AND CRITICAL ESSAYS 283, 288 (Christopher L. Tomlins & Andrew J. King eds., 1992). If current trends continue only seven percent of private-sector workers in this country will have union representation in the year 2000, according to Rutgers University economist Leo Troy. *See Causes of Loss of Union Membership Debated at New York University Conference on Labor*, DAILY LAB. REP. (BNA), June 8, 1992, at A16. For an analysis of the decline of unions in the private sector, see generally MICHAEL GOLDFIELD, THE DECLINE OF ORGANIZED LABOR IN THE UNITED STATES (1987).

[2] 29 U.S.C. §§ 151–169 (1988).

[3] *See, e.g.*, PAUL C. WEILER, GOVERNING THE WORKPLACE: THE FUTURE OF LABOR AND EMPLOYMENT LAW 241–73 (1990) (proposing amendments to the Act, including tort-like damages for unfair labor practices, greater protections for strikers, and greater tolerance of secondary boycotts); WILLIAM B. GOULD IV, AGENDA FOR REFORM: THE FUTURE OF EMPLOYMENT RELATIONSHIPS AND THE LAW 177–78 (1993) (suggesting changes to the NLRA, including increased union access to employer premises, arbitration of first contracts, and elimination of the mandatory/permissive distinction in subjects of bargaining); CHARLES B. CRAVER, CAN UNIONS SURVIVE? THE REJUVENATION OF THE AMERICAN LABOR MOVEMENT 139–55 (1993) (suggesting, *inter alia*, expansion of the Act's coverage).

[4] Following President Clinton's election, labor's highest legislative priority was to

dent Clinton's 1992 election appeared to return labor law reform to the national agenda.[5] Now, however, the Republican control of both houses of Congress has effectively eliminated, for the foreseeable future, any chance for substantive improvements of the Act.[6]

Therefore, rather than formulate yet another suggestion for increasing workers' rights under the NLRA, this Article addresses a more modest, yet achievable reform: using the rulemaking authority of the National Labor Relations Board (NLRB or the Board) to require employers to inform their employees, through posted notices, of the rights they already enjoy under the Act. Indeed, a petition requesting such a rule is now pending before the Board.[7]

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deny employers the right to hire permanent replacements for strikers. *See Labor Law Reform Gaining Interest on Capitol Hill*, DAILY LAB. REP. (BNA), Dec. 13, 1993, at C1. Other bills sought to expedite representation elections; expedite the resolution of employee discharge cases; increase monetary awards for wrongfully discharged employees; prohibit law firms and consulting firms from encouraging violations of the NLRA; increase unions' right of access to employer premises; provide for mandatory arbitration of first contracts; increase the certification of unions based on employee authorization cards; and limit the right of employers in mining and construction to engage in double-breasted operations. *See id.* at C2.

[5] *See* Joel Rogers, *Reforming U.S. Labor Relations*, *in* RESTORING THE PROMISE OF AMERICAN LABOR LAW 15, 17 (Sheldon Friedman et al. eds., 1994) [hereinafter AMERICAN LABOR LAW]; *see also Labor Law Reform Gaining Interest on Capitol Hill*, *supra* note 4, at C1 (predicting intensified debate over need for labor law reform).

[6] *See Labor Expresses Disappointment in Results of Mid-term Elections*, DAILY LAB. REP. (BNA), Nov. 10, 1994, at AA5 (quoting officer of National Right To Work Committee who stated that with the results of the mid-term elections, organized labor's legislative agenda "has run aground").

[7] *See* Charles J. Morris, *Renaissance at the NLRB—Opportunity and Prospect for Non-Legislative Procedural Reform at the Labor Board*, 23 STETSON L. REV. 101, 110–12 (1983) (referring to petition filed by law professor Charles Morris in February 1993). A copy of the petition, entitled "Petition Of Charles J. Morris, An Interested Person, For The Amendment Of Proposed Regulations Or, In The Alternative, For The Issuance Of A New General Rule Regarding Information Posting," [hereinafter *Morris Petition*] is on file with the NLRB in Washington, D.C. The petition calls for a rule "providing for the posting of conspicuous notices where employees congregate at all employer establishments and labor organizations subject to the jurisdiction of the Board, which notices shall advise employees of their general rights and duties under the National Labor Relations Act." *Morris Petition* at 4.

Professor Morris filed the petition as part of the Board's proposed rulemaking concerning the means to provide notice to employees of their rights under the Supreme Court's decision in Communications Workers v. Beck, 487 U.S. 735 (1988). *See* 57 Fed. Reg. 43,635 (1992) (to be codified at 29 C.F.R. pt. 103) (proposed September 22, 1992). For a discussion of *Beck* and notice to employees of their rights under *Beck*, see *infra* notes 101–108 and accompanying text.

As the author confirmed in an October 26, 1994 telephone conversation with David Parker, the Board's director of information, Professor Morris' petition is still pending.

Federal law already requires employers to notify employees of their rights under a variety of statutes, including the Fair Labor Standards Act,[8] the Occupational Safety and Health Act,[9] Title VII of the 1964 Civil Rights Act,[10] the Americans With Disabilities Act,[11] the Age Discrimination In Employment Act,[12] the Family and Medical Leave Act,[13] and even the relatively obscure Employee Polygraph Protection Act.[14] On bulletin boards in workplaces throughout the nation, government-mandated posters inform workers of their rights under these statutes.

Except in certain limited circumstances,[15] however, no government-mandated poster tells workers of their fundamental rights under section 7 of the NLRA: the rights to organize, to bargain collectively through representatives of their own choosing, to engage in concerted activity for mutual aid and protection, and also to refrain from any such activities.[16] This absence of a general notice requirement under the NLRA is remarkable given the significance of the Act as the cornerstone of private-sector labor law in this country. As Professor Charles Morris has noted, "the NLRA is the only law governing the relationship between an employer and its employees as a group in most private sector establishments in this country."[17]

American workers are largely ignorant of their rights under the NLRA,[18] and this ignorance stands as an obstacle to the effective exercise of such rights. For example, during union

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[8] 29 U.S.C.A. §§ 201–219 (West 1978 & Supp. 1995). For a discussion of the notice requirement, see *infra* notes 75–77 and accompanying text.

[9] 29 U.S.C.A. §§ 651–678 (West 1985 & Supp. 1995). For a discussion of the notice requirement, see *infra* notes 78–79 and accompanying text.

[10] 42 U.S.C.A. §§ 2000e to 2000e-17 (West 1994). For a discussion of the notice requirement, see *infra* notes 57–60 and accompanying text.

[11] 42 U.S.C.A. §§ 12101–12213 (West 1985 & Supp. 1995). For a discussion of the notice requirement, see *infra* notes 65–67 and accompanying text.

[12] 29 U.S.C.A. § 621–634 (West 1985 & Supp. 1995). For a discussion of the notice requirement, see *infra* notes 61–64 and accompanying text.

[13] 29 U.S.C.A. §§ 2601–2654 (West Supp. 1995). For a discussion of the notice requirement, see *infra* notes 72–74 and accompanying text.

[14] 29 U.S.C.A. §§ 2001–2009 (West Supp. 1995). For a discussion of the notice requirement, see *infra* notes 68–71 and accompanying text.

[15] The Board requires employers to post notices to employees of their rights under the Act three days before a representation election and also, in some cases, after the employer has been found to have violated the Act. For a more complete discussion, see *infra* notes 80–100 and accompanying text.

[16] *See* 29 U.S.C. § 157 (1988).

[17] Charles J. Morris, *NLRB Protection in the Nonunion Workplace: A Glimpse at a General Theory of Section 7 Conduct*, 137 U. PA. L. REV. 1673, 1675–76 (1989).

[18] *See infra* notes 27–33 and accompanying text.

organizing campaigns, employees' ignorance of the law hinders their ability to assess employer anti-union propaganda, thus diluting their right to organize.[19] In the non-union setting, employees' ignorance leads to the underutilization of legitimate workplace protests, of the voicing of group grievances, and of requests for outside help from government agencies or other third parties.[20] In sum, lack of notice of their rights disempowers employees.

In the past, requiring employers to notify employees of their NLRA rights may have been viewed as unnecessary because unions had an incentive to tell workers their rights. Now, however, with unions increasingly limited to isolated pockets of the economy,[21] they can no longer be counted on to perform this function. Accordingly, this Article proposes that the Board enact a rule requiring employers covered by the Act to post in the workplace at all times a list of employees' NLRA rights, as well as appropriate explanations or illustrative examples. Under the rule, an employer's failure to post such a notice would result not only in a fine, but also in the potential re-running of representation elections and in the tolling of the limitations period on employee-initiated unfair labor practice charges against the employer.

The notices proposed here would not only inform employees of their rights to organize and to act concertedly, but would also help deter employers from unlawfully retaliating against workers who exercise these rights: the vast number of employer unfair labor practices now committed[22] may diminish if managers had reason to believe employees knew of their right to seek relief from the Board. Moreover, the proposed posting requirement would impose a negligible burden on employers, who are already required by federal law to post notices of other employment statutes.

Part I of the Article explores the extent to which American workers know their legal rights at the workplace. Part II surveys existing notice requirements under various labor and employment statutes and under the NLRA. Part III discusses the decline of America's collective bargaining system, and the various ways

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[19] *See infra* notes 139–155 and accompanying text.
[20] *See infra* notes 163–172 and accompanying text.
[21] *See supra* note 1.
[22] *See infra* notes 124–126 and accompanying text.

in which employees' ignorance of their NLRA rights hinders their ability to exercise those rights. Part IV outlines the Article's proposal for a Board rule requiring notice of NLRA rights, and Part V explores how such a notice might empower American workers and encourage collective bargaining. Part VI analyzes and rejects possible arguments against a rule requiring notice under the NLRA. Finally, Part VII concludes that the Board has the authority to promulgate such a rule and that such a rule would easily withstand judicial scrutiny.

I. EMPLOYEE IGNORANCE OF LABOR LAW RIGHTS

Americans are largely ignorant of their legal rights.[23] Moreover, studies have found that knowledge of law tends to correlate with a person's socioeconomic position; the lower a person's social status, the less likely the person knows her or his rights.[24] Levels of legal knowledge also vary by subject; researchers have found that Americans tend to know less about civil law than about certain basic criminal law principles that are emphasized by the media and popular culture.[25] However, even knowledge

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[23] *See* Stan L. Albrecht & Miles Green, *Cognitive Barriers to Equal Justice before the Law*, 14 J. RES. CRIME & DELINQUENCY 206, 213 (1977) (finding a "very serious lack of knowledge on what must be viewed as questions of basic legal rights"); *see also* Note, *Legal Knowledge of Michigan Citizens*, 71 MICH. L. REV. 1463, 1468 (1973) (finding low level of legal knowledge among Michigan residents); Eric Schnapper, Note, *Consumer Legislation and the Poor*, 76 YALE L.J. 745, 752 (1967) ("Most laymen lack more than a superficial knowledge of their rights and liabilities in a post-sale legal conflict . . . ."); EJAN MACKAAY, ECONOMICS OF INFORMATION AND LAW 194 (1982) (reporting that consumers tend to be unaware of consumer protection laws).

[24] *See* Albrecht & Green, *supra* note 23, at 215, 218–19 (reporting that non-poor respondents had more legal knowledge than poor respondents); Schnapper, *supra* note 23, at 752–53 (reporting that low-income consumers have less knowledge of their rights than other consumers); Martha Williams & Jay Hall, *Knowledge of the Law in Texas: Socioeconomic and Ethnic Differences*, 7 LAW & SOC'Y REV. 99, 113 (1972) (finding that knowledge of law among residents of Austin increased with economic rank and/or majority group membership); *Family Leave: Majority of Workers are Unaware of FMLA Provisions, BNA Survey Finds*, DAILY LAB. REP. (BNA), Dec. 12, 1994, at CC2 (reporting poll that found employees' knowledge of Family and Medical Leave Act, 29 U.S.C. §§ 2601–2654, correlated positively with their income).

But see John Griffiths & Richard E. Ayres, Faculty Note, *A Postscript to the Miranda Project: Interrogation of Draft Protestors*, 77 YALE L.J. 300, 305–06 (1967) (survey of 21 Yale University faculty, graduate students and undergraduate students interviewed by the FBI for suspected draft law violations, finding that "[i]n spite of their superior education, few of the suspects knew their rights in even the grossest outline").

[25] *See* Austin Sarat, *Support for the Legal System: An Analysis of Knowledge, Attitudes and Behavior*, 3 AM. POL. Q. 3, 12 (1975) (reporting public's lower level of knowledge about civil law than about certain elements of criminal law that are widely

of criminal law does not always filter down to lower socioeconomic ranks.[26]

In particular, evidence suggests that American workers remain largely ignorant of their labor law rights.[27] Studies of high school students have repeatedly found a low level of knowledge about labor relations and labor law.[28] For example, a 1989 study of high school students in Pennsylvania concluded that three-quarters of the students surveyed "[did] not understand the basic tenets of the Taft-Hartley Act and, by implication, the major labor legislation of this century, the National Labor Relations Act."[29] One 1985–86 survey of high school students in Florida asked students who decides whether a company becomes union-

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publicized in the mass media); Note, *Legal Knowledge*, *supra* note 23, at 1479 (suggesting that the public's higher level of knowledge about criminal than consumer law is attributable to newspapers and magazines); Albrecht & Green, *supra* note 23, at 214 (reporting a high level of knowledge of two items emphasized on television: 93% of respondents correctly answered that the police must inform person they arrest of the person's constitutional rights, and 86% knew that a person has a right to an attorney when being questioned by the police); *see also* United States v. Kilgroe, 959 F.2d 802 (9th Cir. 1992) (noting that warnings mandated by Miranda v. Arizona, 384 U.S. 436 (1966), have "become part of our common awareness").

Courts also appear aware of the extent to which the law remains unknown. Contrary to popular belief, courts frequently do accept ignorance of the law as an excuse for unlawful behavior. *See* Vera Bolgar, *The Present Function of the Maxim* Ignorantia Iuris Neminem Excusat—*A Comparative Study*, 52 IOWA L. REV. 626, 641 (1967) (proliferation of laws and regulations in the modern state "poses an added burden on the presumption of the knowledge of the laws for the citizens," and has led to increasing judicial acceptance of the defense of ignorance of the law); *see also* Meir Dan-Cohen, *Decision Rules and Conduct Rules: On Acoustic Separation in Criminal Law*, 97 HARV. L. REV. 625, 646–47 (1984) (analyzing applications of the ignorance-of-the-law defense).

[26] *See* Williams & Hall, *supra* note 24, at 117 (reporting that 40% of low-income African Americans incorrectly believed that Texas law allowed the police to search a private residence at will).

[27] *See* Morris, *supra* note 17, at 1675 (noting "mass unawareness" on behalf of most employees concerning employees' NLRA rights in the non-union workplace); RICHARD EDWARDS, RIGHTS AT WORK: EMPLOYMENT RELATIONS IN THE POST-UNION ERA 2 (1993) ("In the American panoply of rights, workplace rights are . . . the least understood . . . ."); *see also infra* note 32.

[28] *See* WILLIAM J. PUETTE, THROUGH JAUNDICED EYES: HOW THE MEDIA VIEW ORGANIZED LABOR app. A (1992) (1989 study of high school students in Hawaii finding students frequently answered basic questions on labor law incorrectly); Tom Juravich, *Anti-Union or Unaware? Work and Labor as Understood by High School Students*, LAB. STUD. J., Fall 1991, at 16, 25 (1989 study of high school students in Pennsylvania finding that students "were . . . unable to answer basic questions about labor legislation . . . ."); Robert J. Amann & Ronnie Silverblatt, *High School Students' Views on Unionism*, LAB. STUD. J., Winter 1987–88, at 44, 58 (1985–86 study of high school students in southern Florida finding that "students have very little knowledge of collective bargaining rights"); Dana Bramel & Clemencia Ortiz, *Tomorrow's Workers and Today's Unions: A Survey of High School Students*, LAB. STUD. J., Winter 1987–88, at 28, 39 (1985 survey of high school students in Suffolk County, New York finding "knowledge of . . . labor relations is low").

[29] Juravich, *supra* note 28, at 25–26.

ized: the workers, the management, the government, or workers and management together? Over forty percent of the students responded that they did not know, and less than one-third correctly responded that the workers decide.[30] American workers, over half of whom have no education beyond high school,[31] may be nearly as ignorant about labor law as the high school students surveyed.[32] Indeed, even those with a college education frequently do not understand their rights in the workplace.[33]

Workers probably remain largely unaware of their labor law rights because nothing in their lives serves to inform them of these rights. The mass media, for example, which serve as a major source of the public's knowledge about law,[34] rarely address employment issues. When covering labor issues, newspapers and television focus predominantly on sensational matters such as strike violence, while paying little attention to substantive matters.[35] Nor do schools offer much information concern-

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[30] Amann & Silverblatt, *supra* note 28, at 49.

[31] *See* BUREAU OF LABOR STATISTICS, U.S. DEP'T OF LABOR, BULLETIN 2340, HANDBOOK OF LABOR STATISTICS 280 (1989) (in 1988, 54.6% of the civilian workers in the United States age 25 to 64 had no more than a high school education).

[32] *Cf.* Richard McHugh, *Fair Warning or Foul? An Analysis of the Worker Adjustment and Retraining Notification Act in Practice*, 14 BERKELEY J. EMPLOYMENT & LAB. L. 1, 60 (1993) (stating that many workers are unaware of the existence of the Worker Adjustment And Retraining Notification (WARN) Act, 29 U.S.C. §§ 2101–2109) (quoting Julie H. Hurwitz, director of the Sugar Law Center, a national clearinghouse on litigation under the WARN Act); *Family Leave*, *supra* note 24, at CC1 (reporting poll that found that more than half of American workers knew little or nothing about the Family and Medical Leave Act 20 months after it became law); Note, *Legal Knowledge*, *supra* note 23, at 1469 (finding that 30% of residents surveyed did not know that an airline may not refuse to hire a male flight attendant because of his sex).

[33] *See, e.g.*, THOMAS GEOGHEGAN, WHICH SIDE ARE YOU ON? TRYING TO BE FOR LABOR WHEN IT'S FLAT ON ITS BACK 271–72 (1991) (noting that "even bright, college-educated people" have no idea about the doctrine of employment-at-will, but believe that long tenure at a job offers protection against discharge).

[34] *See* Note, *Legal Knowledge*, *supra* note 23, at 1476–77 (noting high positive correlation between exposure to newspapers and news magazines and knowledge about law, but acknowledging that such correlation might be due to the fact that people who know about the law from other sources might just like to read such items); Sarat, *supra* note 25, at 12 (noting in regard to criminal law that "[i]t is this mass media dissemination of information which may account for the relatively high level of knowledge which the respondents displayed"); *cf.* Amann & Silverblatt, *supra* note 28, at 58 ("the media is the major source influencing student attitudes towards unions").

[35] Amann & Silverblatt, *supra* note 28, at 49–50; *see also* PUETTE, *supra* note 28, at 45 (noting that of the commentators featured on ABC's "Nightline," only one percent were labor leaders).

Fictional films and television shows similarly offer little balanced information on labor matters. William Puette writes that, with few exceptions, Hollywood movies provide a "virulently negative" portrayal of unions, often focusing "on the perceived connection between organized crime and organized labor." PUETTE, *supra* note 28, at 31, 153. Televisions shows, moreover, consistently portray "the collective bargaining process as simplistic or foolish." *Id.* at 53.

ing labor. One study of high school students in southern Florida found that only about one-quarter of the students surveyed recalled ever discussing unions in class.[36] Finally, another potential source of information about labor issues and rights—friends and family who belong to unions—has diminished as the percentage of the workforce represented by unions has shrunk.[37]

Ignorance of the law disempowers people. It prevents them from seeking redress for legal wrongs, and also causes them to shy away from taking actions to which they are legally entitled.[38] Employment law statutes generally are underenforced.[39] Evidence suggests that this lack of enforcement is due at least in part to employees' ignorance of their rights under such statutes.[40] As Professor Paul Weiler has written, "[t]o translate abstract legal rights on the books into practical guarantees in the workplace, the employee needs to be informed what his rights are . . . ."[41]

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[36] Amann & Silverblatt, *supra* note 28, at 49, 58 (concluding that schools fail to teach students adequately about unions); Bramel & Ortiz, *supra* note 28, at 31 (citing 1983 study of history textbooks used by 72% of high schools in New Jersey, and finding that the books de-emphasized or omitted mention of organized labor's contributions to American history).

[37] *See* PUETTE, *supra* note 28, at 4 ("[o]rganized labor is a remote experience to the vast majority of Americans"); Amann & Silverblatt, *supra* note 28, at 49 (finding that few of the students surveyed reported discussing unions at home, and that few students or their parents belonged to unions). For statistics on the shrinking portion of the workforce represented by unions, see *supra* note 1.

[38] *See* Sarat, *supra* note 25, at 13 ("Only people who know what their rights are and how the legal system works can defend themselves against intrusions on their freedom and use that system to achieve their goals or ameliorate undesired conditions."); Albrecht & Green, *supra* note 23, at 218 ("Individuals who are unaware of basic legal rights" are "more likely to tolerate injustice simply because of a lack of awareness . . . [of opportunity] for redress.").

[39] EDWARDS, *supra* note 27, at 124.

[40] *See, e.g.*, McHugh, *supra* note 32, at 60 (scarcity of litigation under the WARN Act is due in part to lack of employees' awareness of their rights under the statute) (quoting Congressional testimony of Julie H. Hurwitz); *see also* Edwards v. Kaiser Aluminum & Chem. Sales, Inc., 515 F.2d 1195, 1197 (5th Cir. 1975) (citing congressional finding that a relationship exists between public awareness of state age discrimination laws and the volume of complaints under those laws).

The rise in sexual harassment claims following Clarence Thomas's Senate confirmation hearings, which educated the public about legal prohibitions on sexual harassment, dramatically demonstrates how knowledge of law leads more employees to assert their rights. *See* Cathy Trost, *Labor Letter*, WALL ST. J., Feb. 25, 1992, at A1 (reporting rise in sexual harassment charges following the Thomas hearings).

[41] WEILER, *supra* note 3, at 158; *see, e.g.*, Pirone v. Home Ins. Co., 507 F. Supp. 1281, 1287 (S.D.N.Y. 1981) ("It is indispensable to the functioning of the ADEA that employees be aware of the procedural requirements of the Act.").

II. CURRENT NOTICE REQUIREMENTS

Federal law currently mandates notices in a number of contexts, both in employment law and other fields of law. This Part of the Article surveys several such notice requirements.

A. *Notice Requirements Outside the Employment Context*

Many laws require businesses to inform consumers of facts relevant to the consumer transaction.[42] For example, cigarette packages must warn consumers of the adverse health effects of smoking.[43] Similarly, businesses providing written warranties with consumer products must notify consumers, "in simple and readily understood language," of certain terms of the warranty.[44] Such notices provide the consumer with useful information that costs the business little to disclose,[45] and that, in many cases, might otherwise be difficult for the consumer to obtain.[46] Moreover, unlike compliance with other forms of regulation, compliance with notice requirements can be easily monitored by the regulating agency.[47]

In the criminal law context, *Miranda v. Arizona*[48] requires law enforcement agents to notify criminal suspects of certain rights prior to custodial interrogation.[49] When police officers give the legally required *Miranda* warnings, their compliance with the notice requirement helps assure the criminal suspect that the

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[42] *See generally* ROSS CRANSTON, CONSUMERS AND THE LAW 275 (1978) (noting that modern consumer legislation frequently requires businesses to divulge information to consumers concerning their products and practices).

[43] *See* 15 U.S.C. § 1333(a) (1988).

[44] 15 U.S.C. § 2302(a) (1988); *see also* 12 C.F.R. § 226.15(a)(ii)(3) (1994) (requiring that consumer leases state, among other things, the number of payments due, the amount of the payments, and the dates the payments are due).

[45] *See* CRANSTON, *supra* note 42, at 275.

[46] *See* Note, *Occupational Health Risks and the Worker's Right to Know*, 90 YALE L.J. 1792, 1806 (1981). For example, consumers could not easily learn the ingredients of packaged food without statutorily mandated food labels. *See* 21 U.S.C.A. § 343(e) (West 1972 & Supp. 1995).

[47] *See* CRANSTON, *supra* note 42, at 275.

[48] 384 U.S. 436 (1966).

[49] *See* Withrow v. Williams, 113 S. Ct. 1745, 1751–55 (1993); Pennsylvania v. Muniz, 496 U.S. 582, 596 (1990). In particular, the police must tell the suspect that she has the right to remain silent, that any statement she makes may be used against her, and that she has a right to the presence of an attorney. *See Muniz*, 496 U.S. at 596; *Miranda*, 384 U.S. at 444. Failure to inform the suspect of these rights may lead to the exclusion from evidence of the suspect's incriminating statements in a subsequent criminal proceeding. *See Muniz*, 496 U.S. at 600; *Miranda*, 384 U.S. at 479.

officers are law-abiding. Thus, by requiring the police to serve as the *source* of the warnings, *Miranda* not only ensures that the suspect knows his rights, but also helps assure the suspect that his rights will be honored.[50]

B. *Notice Requirements Under Employment Statutes Other than the NLRA*

A number of federal employment statutes and regulations require the disclosure of information to employees. For example, the Employee Retirement Income Security Act (ERISA),[51] which governs employee benefit plans, requires plan administrators to furnish plan participants with a summary description of the plan,[52] setting forth, *inter alia*, the eligibility requirements for receiving benefits.[53] ERISA further requires that the summary plan description "be written in a manner calculated to be understood by the average plan participant."[54] Similarly, a regulation promulgated pursuant to the Occupational Safety And Health Act (OSHA)[55]—a statute that sets safety standards in the workplace—requires employers to notify employees of hazardous chemicals in the workplace.[56]

In addition to requiring the disclosure of certain factual information, many federal employment laws compel employers to disclose to employees information regarding their statutory rights. Title VII of the 1964 Civil Rights Act (Title VII),[57] which prohibits employment discrimination on grounds such as race and sex, requires every employer to "post . . . in conspicuous places on its premises" a notice, prepared or approved by the Equal

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[50] *See* Welsh S. White, *Defending Miranda: A Reply to Professor Caplan*, 39 VAND. L. REV. 1, 6 (1986). Professor White writes that, without the *Miranda* warnings, even if a suspect "is aware of his right to remain silent, he does not necessarily know that the officer is prepared to honor that right. The warnings may be necessary to give him that assurance."

[51] 29 U.S.C.A. §§ 1001–1461 (West 1985 & Supp. 1995).

[52] *Id.* § 1024(b)(1).

[53] *Id.* § 1022(b).

[54] *Id.* § 1022(a)(1).

[55] 29 U.S.C.A. §§ 651–678 (West 1985 & Supp. 1995).

[56] *See* 29 C.F.R. § 1910.1200(f)(5) (1994). The regulation states that, with some exceptions, "the employer shall ensure that each container of hazardous chemicals in the workplace is labeled, tagged or marked with the following information: (i) Identity of the hazardous chemical(s) contained therein; and (ii) Appropriate hazard warnings . . . ." For a discussion of the "right-to-know" requirements under OSHA, see generally Note, *supra* note 46.

[57] 42 U.S.C.A. §§ 2000e to 2000e-17 (West 1994).

Employment Opportunity Commission (EEOC), that sets forth excerpts or summaries of the statute and information pertinent to filing a complaint.[58] Title VII further provides that a "willful violation . . . [of the posting requirement] shall be punishable by a fine of not more than $100 for each separate offense."[59] Employers that fail to post the EEOC notice risk not only a fine but also the loss of a timeliness defense in a Title VII action. Courts have held that the failure of an employer to post the required notice tolls the running of the limitations period for filing an employment discrimination claim under the statute, so long as the employee had no actual knowledge of, or ample opportunity to learn about, the procedures under the statute.[60]

Like Title VII, the Age Discrimination In Employment Act (ADEA),[61] which prohibits age-based employment discrimination, requires every employer to "post . . . in conspicuous places upon its premises a notice . . . prepared or approved by the . . . [EEOC] setting forth information" concerning employees' rights under the statute.[62] As one court noted, the ADEA's posting requirement "was undoubtedly created because Congress recognized that the very persons protected by the Act might be unaware of its existence."[63] Although the statute contains no specific penalty for violation of the posting requirement, courts have ruled that an employer's failure to comply may toll the running of the limitations period on an employee's age discrimination charge.[64]

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[58] *See id.* § 2000e-10(a); *see also* 29 C.F.R. § 1601.30.

[59] *See* 42 U.S.C. § 2000e-10(b) (1988); *see also* EEOC v. Anderson's Restaurant of Charlotte, Inc., 666 F. Supp. 821, 846 (W.D.N.C. 1987); EEOC v. H.S. Camp & Sons, Inc., 542 F. Supp. 411, 449 (M.D. Fla. 1982) (holding that EEOC failed to establish that employer willfully failed to display EEOC posters).

[60] *See* Robinson v. Caulkins Indiantown Citrus Co., 701 F. Supp. 208, 210 (S.D. Fla. 1988) (employer's failure to post required notice results in equitable tolling of limitations period until plaintiff learns of statutory prohibition on discrimination); *see also* Llewellyn v. Celanese Corp., 693 F. Supp. 369, 378 (W.D.N.C. 1988); Earnhardt v. Puerto Rico, 582 F. Supp. 25, 26 (D.P.R. 1983), *aff'd*, 744 F.2d 1 (1st Cir. 1984); *but see* Cruce v. Brazosport Indep. Sch. Dist., 703 F.2d 862, 864 (5th Cir. 1983) (no equitable tolling on sex discrimination claim, despite allegation that employer failed to post notice, when plaintiff had ample opportunity to learn of statute's procedures from her union).

[61] 29 U.S.C.A. §§ 621–634 (West 1985 & Supp. 1995).

[62] *Id.* § 627.

[63] Bonham v. Dresser Indus., Inc., 569 F.2d 187, 193 (3d Cir. 1978); *see also* Vance v. Whirlpool Corp., 716 F.2d 1010, 1012 (4th Cir. 1983) (noting that Congress "imposed this [notice] requirement to insure that covered employees would be informed of their rights . . . ."); Edwards v. Kaiser Aluminum & Chem. Sales, Inc., 515 F.2d 1195, 1197 (5th Cir. 1975).

[64] *See* English v. Pabst Brewing Co., 828 F.2d 1047, 1049 (4th Cir. 1987) (employer's

The Americans With Disabilities Act (ADA),[65] which prohibits handicap-based discrimination, requires that every employer covered by the statute's employment provisions[66] post notices, in a format accessible to employees, describing the statute.[67] The statute provides no specific penalty for violation of this posting requirement.

The Employee Polygraph Protection Act (EPPA),[68] which governs the use of polygraphs in the workplace, requires all employers to "post a notice [to employees] setting forth excerpts from or summaries of pertinent provisions of [the] statute."[69] The EPPA provides no penalty specifically for violation of the posting requirement, but states generally that "any employer who violates any provision of the statute may be subject to a civil penalty . . . ."[70] The statute further provides that the amount of the penalty will depend upon the gravity of the violation but will in no case exceed $10,000.[71]

The Family And Medical Leave Act (FMLA),[72] which provides employees the right to take leaves from work for certain medical or family-related reasons, requires all employers to "post . . . on the premises [a notice] setting forth excerpts from, or summaries of, the pertinent provisions of . . . [the statute] and information pertaining to the filing of a charge."[73] Like Title VII, the FMLA states that "[a]ny employer that willfully violates . . . [the notice requirement] may be assessed a civil money penalty not to exceed $100 for each separate offense."[74]

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failure to post notice tolls limitations period until plaintiff obtains an attorney or acquires actual knowledge of rights under statute); *accord Bonham*, 569 F.2d at 193; McClinton v. Alabama By-Prods. Corp., 743 F.2d 1483, 1486 (11th Cir. 1984) (employer's failure to post notice tolls statute of limitations until employee acquires knowledge of prohibition on age discrimination or acquires means to obtain such knowledge); *accord Vance*, 716 F.2d at 1012; Berry v. Joseph E. Seagram & Sons, Inc., 744 F. Supp. 214, 217 (C.D. Cal. 1990) (employer's failure to post required notice tolls limitations period until plaintiff acquires actual notice of rights under statute); *accord* Hall v. Ametek, Inc., 668 F. Supp. 417, 419 (E.D. Pa. 1987); Pirone v. Home Ins. Co., 507 F. Supp. 1281, 1287 (S.D.N.Y. 1981).

[65] 42 U.S.C.A. §§ 12101–12213 (West Supp. 1995).

[66] *See id.* §§ 12111–12117.

[67] *Id.* § 12115.

[68] 29 U.S.C.A. §§ 2001–2009 (West Supp. 1995).

[69] *Id.* § 2003.

[70] *Id.* § 2005(a).

[71] *Id.* § 2005(a)(1)–(2).

[72] 29 U.S.C.A. §§ 2601–2654 (West Supp. 1995).

[73] *Id.* § 2619(a).

[74] *Id.* § 2619(b).

A U.S. Department of Labor (DOL) regulation[75] requires employers to post in conspicuous places on their premises a notice explaining the provisions of the Fair Labor Standards Act (FLSA),[76] a statute that sets federal wage and hour standards. Failure by an employer to comply with this posting requirement tolls the running of the statute of limitations on actions brought under the FLSA.[77]

A DOL regulation under OSHA requires every employer to "post . . . a notice . . . informing employees of the protections" of the statute and also informing employees that they can contact the DOL for further information or for assistance.[78] The regulation provides that an employer may be subject to "citations and penalties" for failure to comply.[79]

C. *Notice Requirements Under the NLRA*

Unlike under the various employment statutes surveyed above, employers have no obligation to inform employees of their rights under the NLRA, except in the limited circumstances discussed below.

1. Representation Cases

The NLRB requires that three days prior to a union representation election the employer post the NLRB's official Notice of Election in conspicuous places.[80] In addition to providing information on the election such as the time and place of the balloting,[81] the Notice of Election provides employees with the following description of their rights:

> RIGHTS OF EMPLOYEES
>
> Under the National Labor Relations Act, employees have the right:

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[75] 29 C.F.R. § 516.4 (1994).
[76] 29 U.S.C.A. §§ 201–219 (West 1978 & Supp. 1995).
[77] *See* Kamens v. Summit Stainless, Inc., 586 F. Supp. 324, 328 (E.D. Pa. 1984).
[78] 29 C.F.R. § 1903.2(a)(1) (1994).
[79] *Id.* § 1903.2(d).
[80] 29 C.F.R. § 103.20(a) (1994); *see* Smith's Management Corp., 295 N.L.R.B. 983, 983 n.1 (1989).
[81] *See* Notice of Election Form NLRB-707, *reprinted in* JEFFREY A. NORRIS & MICHAEL J. SHERSHIN, JR., HOW TO TAKE A CASE BEFORE THE NLRB 209 (6th ed. 1992).

> • To self-organization
> • To form, join or assist labor organizations
> • To bargain collectively through representatives of their own choosing
> • To act together for the purposes of collective bargaining or other mutual aid or protection
> • To refuse to do any or all of these things unless the Union and Employer, in a State where such agreements are permitted, enter into a lawful union security clause requiring employees to join the Union[82]

The notice also provides illustrations of prohibited election conduct, such as "[a]n Employer firing employees to discourage or encourage union activity or a Union causing them to be fired to encourage union activity."[83] The Board's Notice of Election further states that the NLRB serves to protect employees' rights under the Act, and it explains possible remedies for violations of the Act:

> It is the responsibility of the National Labor Relations Board to protect employees in the exercise of these rights.
>
> The Board wants all eligible voters to be fully informed about their rights under Federal law and wants both Employers and Unions to know what is expected of them when it holds an election.
>
> If agents of either Unions or Employers interfere with your right to a free, fair, and honest election, the election can be set aside by the Board. Where appropriate the Board provides other remedies, such as reinstatement for employees fired for exercising their rights, including backpay from the party responsible for their discharge.[84]

The notice concludes with the words

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[82] *Id.*

[83] *Id.* The complete list of examples is as follows:
• Threatening loss of jobs or benefits by an Employer or a Union
• Promising or granting promotions, pay raises, or other benefits to influence an employee's vote by a party capable of carrying out such promises
• An Employer firing employees to discourage or encourage union activity or a Union causing them to be fired to encourage union activity
• Making campaign speeches to assembled groups of employees on company time within the 24-hour period before the election
• Incitement by either an Employer or a Union of racial or religious prejudice by inflammatory appeals
• Threatening physical force or violence to employees by a Union or an Employer to influence their votes.

[84] *Id.*

> The National Labor Relations Board protects your right to a free choice.
>
> Improper conduct will not be permitted. All parties are expected to cooperate fully with this agency in maintaining basic principles of a fair election as required by law. The National Labor Relations Board as an agency of the United States Government does not endorse any choice in the election.[85]

The Board adopted the Notice of Election "for the purpose of alerting employees to their rights under the Act and in order to warn unions and management alike against conduct impeding fair and free elections."[86] The Board considers it important that the information in the notice come from a government agency rather than from the parties; it has specifically held that an employer's provision of accurate information to the employees concerning the election cannot remedy a failure to post the Board's official notice.[87]

Under current Board policy, an employer's failure to post the notice at least three days before the election constitutes sufficient ground for setting aside the results of the election.[88] Prior to 1987, when the Board adopted the strict three-day rule,[89] an employer's failure to post the Board's notice in a timely manner was not automatic grounds for a re-run election.[90] Rather, in determining whether to set aside the election, the Board weighed factors such as whether the employer acted in bad faith in failing to post the notice, whether the lack of notice affected voter turnout, and whether the employees knew their rights under the Act despite the lack of notice.[91] The Board adopted the three-day

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[85] *Id.*

[86] Overland Hauling, Inc., 168 N.L.R.B. 870, 870 (1967) (ordering new election when Notice of Election had been posted but portion of notice setting forth employees' rights had been hidden from view).

[87] *See* Kilgore Corp., 203 N.L.R.B. 118, 119 n.5 (1973) ("By no stretch of the imagination will campaign literature of the parties take the place of an official Board notice."); *see also* Associated Air Freight, Inc., 247 N.L.R.B. 990, 991 (1980) (employer's campaign literature informing employees of the date of election cannot substitute for Board's notice).

[88] *See* 29 C.F.R. § 103.20(d) (1994); *Smith's*, 295 N.L.R.B. at 983.

[89] *See* 52 Fed. Reg. 25,213 (1987).

[90] *See* Earle Indus., Inc., 248 N.L.R.B. 67, 68 (1980) (deeming employer's failure to post notice until two days before election insufficient grounds to set aside election); Printhouse Co., Inc., 246 N.L.R.B. 741, 742 (1979) (refusing to set aside election even on assumption that employer posted notice only one day before election); Kane Indus., Inc., 246 N.L.R.B. 738, 738 (1979) (declining to set aside election when employer closed plant before election so that employees did not see notice until day of election).

[91] *See Earle*, 248 N.L.R.B. at 68 (declining to set aside election because 97% of

bright-line rule to discourage litigation over the posting requirement,[92] and to ensure that the information contained in the notice is "conveyed to the employees far enough in advance of the election so that employees will be adequately apprised of their rights."[93]

2. Unfair Labor Practice Cases

As a remedy in unfair labor practice cases, the Board requires employers to post notices informing their employees that they will cease engaging in the activity that the Board found to violate the Act.[94] Generally, the Board requires that the notices remain posted for sixty days.[95] In many cases, the Board-ordered notice does not generally inform employees of their rights under the Act, but simply states that the employer will refrain from engaging in the particular unlawful conduct at issue in the case, and that the employer will not "in any like or related manner interfere with, restrain or coerce [employees] in the exercise of the rights guaranteed by Section 7 of the Act."[96] In other cases, the Board-ordered notice also sets forth the following language:

> Section 7 of the Act gives employees these rights:
> To organize
> To form, join, or assist any union
> To bargain collectively through representatives of their

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employees on eligibility list voted and because there was "no evidence here that any employees were unaware of, or misunderstood, their rights or were prevented from voting by the fact that they did not actually see the notice until two days before the election"); *Kane*, 246 N.L.R.B. at 738 (declining to set aside election when 95% of the eligible employees voted and when there was no evidence either of bad faith by the employer or of ignorance of the employees of their rights under the Act).

[92] *Smith's*, 295 N.L.R.B. at 983 n.1.

[93] *Id.* Three days, however, is not very far in advance, when election campaigns frequently last weeks or months. *See* Kate L. Bronfenbrenner, *Employer Behavior in Certification Elections and First-Contract Campaigns: Implications for Labor Law Reform*, *in* AMERICAN LABOR LAW, *supra* note 5, at 75–76, 79 (finding in a study of 261 NLRB elections in 1986 and 1987 that average time from filing of election petition until election was 79 days).

[94] *See infra* note 97 for examples of cases containing such notices; *see generally* NLRB v. Express Publishing Co., 312 U.S. 426, 438 (1941) (recognizing that Board has authority to require employer to post notices advising employees of the Board's cease-and-desist order and announcing the employer's willingness to obey the order); NLRB v. Douglas & Lomason Co., 443 F.2d 291, 295 (8th Cir. 1971) (noting that Board-ordered notice in unfair labor practice cases should serve to inform employees that their employer will not engage in practices found to be in violation of the Act).

[95] *See* NORRIS & SHERSHIN, *supra* note 81, at 448; 1 NLRB Casehandling Manual ¶ 10132.1(a) (1989); *see, e.g.*, Civil Serv. Employees Ass'n, Inc., 311 N.L.R.B. 6, 11 (1993).

[96] *E.g.*, Bristol Farms, Inc., 311 N.L.R.B. 437, app. at 440 (1993).

own choice
To act together for other mutual aid or protection
To choose not to engage in any of these protected activities[97]

Usually, the Board orders employers that have violated the Act to post notices just at the worksite where the unfair labor practice took place.[98] However, when an employer with several facilities engages in numerous violations, thus creating a climate of fear throughout its workforce, the Board has required postings even at facilities where no violation occurred.[99] Also, when a significant portion of the employee group does not read English, the Board may require that the notices be written in languages familiar to the employees.[100]

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[97] *See, e.g.*, Civil Service Employees Ass'n, 311 N.L.R.B. at 11.

For example, of the first 50 cases printed in volume 311 of the NLRB reporter, 25 were unfair labor practice cases in which employers were found to have violated the Act. Of these, only 13 decisions required employers to post notices that listed employees' Section 7 rights. *See* DiMucci Constr. Co., 311 N.L.R.B. 413, 420–421 (1993); Lancaster Fairfield Community Hosp., 311 N.L.R.B. 401, 406 (1993); The Sharing Community, Inc., 311 N.L.R.B. 393, 397 (1993); Holly Farms Corp., 311 N.L.R.B. 273, 287 (1993); Flexsteel Indus., Inc., 311 N.L.R.B. 257, 260 (1993); R.P.C. Inc., 311 N.L.R.B. 232, 250 (1993); Upper Great Lakes Pilots, Inc., 311 N.L.R.B. 131, 140 (1993); CBC Indus., Inc., 311 N.L.R.B. 123, 130 (1993); Refuse Compactor Serv., Inc., 311 N.L.R.B. 12, 13 (1993); Juniper Indus. Inc., 311 N.L.R.B. 107, 112 (1993); The Erler Corp., 311 N.L.R.B. 1, 5 (1993); Burgess, Inc., 311 N.L.R.B. No. 1, 4 (1993); Civil Service Employees Ass'n, 311 N.L.R.B. at 11 (1993).

The other 12 cases contained notices that did not list employees' Section 7 rights. *See* Bristol Farms, Inc., 311 N.L.R.B. 437 (1993); Needell & McGlone, P.C., 311 N.L.R.B. 455, 457–58 (1993); American Warehousing & Dist. Servs., Inc., 311 N.L.R.B. 371, 391–92 (1993); Clarke's Sheet Metal, Inc., 311 N.L.R.B. 228, 228–29 (1993); Beech Aerospace Servs., Inc., 311 N.L.R.B. No. 28, at 2 (1993); Masland Indus., Inc., 311 N.L.R.B. 184, 184–85 (1993); Wachter Constr. Co., 311 N.L.R.B. 215, 222–23 (1993); Duke Univ., 311 N.L.R.B. 182, 183 (1993); Spillman Co., 311 N.L.R.B. 95, 98 (1993); AK Eng'g, 311 N.L.R.B. No. 15, at 3 (1993); BRC Injected Rubber Prods., Inc., 311 N.L.R.B. 66, 66–67 (1993); R.V.L. Corp., 311 N.L.R.B. No. 4, at 3 (1993).

[98] *See, e.g.*, *Masland*, 311 N.L.R.B. at 185, 203 (ordering notice to be posted in one of employer's three facilities).

[99] *See, e.g.*, United Steelworkers of America v. NLRB, 646 F.2d 616, 635 (D.C. Cir. 1981) ("To offset companywide effects caused by extensive unlawful conduct, courts and the Board have expanded remedial measures beyond the actual locations at which unfair labor practices were found."); *see also* Proctor & Gamble Mfg. Co. v. NLRB, 658 F.2d 968, 987–88 (4th Cir. 1982) (noting validity of Board orders that require employers "to post notices companywide even though the unlawful conduct was found to have occurred at only some company plants").

[100] *See, e.g.*, Chinese American Planning Council, Inc., 307 N.L.R.B. 410, 419 (1992) (requiring notices in English and Mandarin Chinese); Chosun Il Bo America, Inc., 303 N.L.R.B. 901, 901 n.4 (1991) (requiring notices in English and Korean); Arecibo Community Health Care, Inc., 300 N.L.R.B. 890, 890 n.2 (1990) (requiring notices in English and Spanish).

3. The Bush Administration's *Beck* Notice

In *Communication Workers of America v. Beck*,[101] the Supreme Court held that when a union's collective bargaining contract contains a union-security agreement requiring all employees—members of the union or not—to pay dues to the union, the union may only use the monies from non-members for negotiating or administering the contract or handling grievances that arise under the contract.[102] On April 13, 1992, President Bush issued an executive order that required federal contractors to post notices to their employees informing non-union members covered by union-security agreements of their right to object to a union's use of their payments for purposes prohibited by *Beck*.[103] According to a White House statement that accompanied the executive order, the order was needed because many employees were "still unaware of the rights they have under the *Beck* decision."[104]

Specifically, the executive order required federal contractors to post the following notice:

> NOTICE TO EMPLOYEES
>
> Under Federal law, employees cannot be required to join a union or maintain membership in a union in order to retain their jobs. Under certain conditions, the law permits a union and an employer to enter into a union-security agreement requiring employees to pay uniform periodic dues and initiation fees. However, employees who are not union members can object to the use of their payments for certain purposes and can only be required to pay their share of union costs relating to collective bargaining, contract administration, and grievance adjustment.

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[101] 487 U.S. 735 (1988).

[102] *Id.* at 740, 745 ("agency fees" required of non-members may not be used for organizing new employees, lobbying for labor legislation or funding community services).

For criticism of *Beck*, *see* George Feldman, *Unions, Solidarity and Class: The Limits of Liberal Labor Law*, 15 BERKELEY J. EMPLOYMENT & LAB. L. 187, 230–41 (1994) (arguing that the *Beck* decision was unsupported by the text or legislative history of the Act); Kenneth G. Dau-Schmidt, *Union Security Agreements Under the National Labor Relations Act: The Statute, The Constitution, and the Court's Opinion in* Beck, 27 HARV. J. ON LEGIS. 51 (1990).

[103] Exec. Order No. 12,800, 57 Fed. Reg. 12,985 (1992); *see also* The Labor Department, *Interim Procedural Notice on Posting of Beck Notices by Federal Contractors*, 72 DAILY LAB. REP. (BNA), Apr. 14, 1992, at D-1.

[104] The White House, *Executive Actions Protecting Workers' Rights* (Apr. 13, 1992), *reprinted in* 72 DAILY LAB. REP. (BNA), Apr. 14, 1992, at E-1.

> If you believe that you have been required to pay dues or fees used in part to support activities not related to collective bargaining, contract administration, or grievance adjustment, you may be entitled to a refund and to an appropriate reduction in future payments.
>
> For further information concerning your rights, you may wish to contact [the National Labor Relations Board].[105]

The executive order further stated that an employer's failure to comply with the notice requirement could lead not only to termination of the employer's current contracts with the government but also to a ban on any future government contracts for that employer.[106] The order even authorized the Secretary of Labor to publish a list of employers that failed to comply with the notice requirement.[107]

Shortly after taking office, President Clinton revoked the executive order requiring notice of *Beck* rights.[108]

III. Conditions Under the Current Legal Regime

A. *The Decline of the American Collective Bargaining System*

The encouragement of collective bargaining stands as one of the cornerstones of national labor policy.[109] However, the percentage of private-sector employees who enjoy collective bargaining representation has declined steadily for the last forty years.[110] By the mid-1980s the percentage—fifteen—roughly

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[105] Exec. Order No. 12,800, *supra* note 103, at § 2(a)(1). The *New York Times* noted in an editorial critical of the executive order that it "requires contractors to point out workers' right not to join a union, but not their rights *to* join a union." N.Y. Times, Apr. 15, 1992, at A26.

[106] Exec. Order No. 12,800, *supra* note 103, at § 2(a)(3).

[107] *Id.* § 6(c).

[108] *See* Exec. Order No. 12,836, 3 C.F.R. 588 (1994).

On September 22, 1992, the Board issued a notice of proposed rulemaking for a rule to require unions to notify employees of their rights under *Beck*. *See* 57 Fed. Reg. 43,635 (1992) (to be codified at 29 C.F.R. pt. 103) (proposed Sept. 22, 1992). The petition is pending.

[109] *See* 29 U.S.C. § 151 (1988) ("It is hereby declared to be the policy of the United States to . . . encourag[e] the practice and procedure of collective bargaining . . . ."); *see also* NLRB v. Pincus Bros., Inc., 620 F.2d 367, 376 (3d Cir. 1980) (a fundamental policy of the Act is to encourage collective bargaining); Bloom v. NLRB, 603 F.2d 1015, 1019 (D.C. Cir. 1979); Houston Shopping News Co. v. NLRB, 554 F.2d 739, 745 (5th Cir. 1977).

[110] *See supra* note 1.

equaled the percentage unionized prior to the enactment of the NLRA in 1935.[111] Indeed, if current trends continue, by 2000 just seven per cent of private-sector employees in the United States will be represented—a union presence comparable to that at the beginning of this century.[112]

The decline of collective bargaining is clearly detrimental to those employees who would otherwise have enjoyed union representation. Unrepresented employees lack the increased wages,[113] job-security protections,[114] and voice in both workplace matters and the political arena that union representation provides.[115]

The decline of collective bargaining also hurts the country as a whole. Studies show that unions tend to increase a firm's productivity by reducing employee turnover and by fostering more rational management policies.[116] Unions also reduce gross disparities of income between blue- and white-collar employees and between employees and shareholders.[117]

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[111] *See* WEILER, *supra* note 3, at 9–10.

[112] *See supra* note 1.

[113] On average, a union increases an employee's wages and benefits by 15%. *See* WEILER, *supra* note 3, at 233 n.8. *See also* RICHARD B. FREEMAN & JAMES L. MEDOFF, WHAT DO UNIONS DO? 43–60 (1984), for a discussion of the extent to which unions boost wages.

The decline of unions in the last 20 years has coincided with, and has to a certain extent caused, a decline in the real wages of American workers. *See Declining Real Wages, Unionization Linked, Dunlop Panel Member Says*, DAILY LAB. REP. (BNA), Apr. 22, 1994, at A7. For reports on this decline in real wages, see Cathy Trost, *Labor Letter*, WALL ST. J., Oct. 13, 1992, at A1 (noting that the average U.S. worker now has to work significantly longer than 20 years ago to buy a house or a car); KEVIN PHILLIPS, THE POLITICS OF RICH AND POOR: WEALTH AND THE AMERICAN ELECTORATE IN THE REAGAN AFTERMATH 18–19 (1990) (finding that the median real wage of American men with no more than a high school education, in 1985 dollars, was $9.90 per hour in 1973, compared with $8.62 per hour in 1987).

[114] A 1992 analysis of 400 collective bargaining agreements from around the country found that 97% contained clauses limiting the grounds upon which the employer could discharge an employee. *See* BUREAU OF NAT'L AFFAIRS, BASIC PATTERNS IN UNION CONTRACTS 7 (1992). Absent a contract with such a clause, most private-sector employees in this country remain vulnerable to discharge, with certain limited exceptions, for good cause, bad cause, or no cause at all. *See* David Hames, *The Current Status of the Doctrine of Employment-at-Will*, 39 LAB. L.J. 19 (1988).

[115] *See* FREEMAN & MEDOFF, *supra* note 113, at 8–10, 206 (noting that collective bargaining gives employees a voice in the workplace, and that unions have "considerable political power in some areas"); Thomas Kohler, *Models of Worker Participation: The Uncertain Significance of Section 8(a)(2)*, 27 B.C. L. REV. 499, 550 (1986) (noting that unions give employees an organized voice both with their employers and in the political arena).

[116] *See* FREEMAN & MEDOFF, *supra* note 113, at 164–65.

[117] *See id.* at 89, 181–90. The decline of unions has coincided with, and to a significant degree has caused, an increasingly skewed distribution of wealth in the United States. *See Inequality: For Richer, For Poorer*, ECONOMIST, Nov. 5, 1994, at 19–20 (lack of powerful unions and a deregulated labor market in the United States have contributed to an extreme gap between rich and poor); Sylvia Nesir, *Fed Gives*

B. *NLRA Representation Elections*

A variety of factors have contributed to the decline of the American collective bargaining system, including the decline of manufacturing, the movement of industry to the southern and western regions of the country, and increases in the number of women and white-collar employees in the workforce.[118] Studies show, however, that these changes fail fully to explain the decline. The greatest cause of union decline has simply been the failure of unions to win more NLRB representation elections.[119] Not only do fewer elections occur now than in the past,[120] but the rate at which employees vote for union representation has declined dramatically.[121] Prior to 1950, 75% of NLRB elections resulted in a union victory, but by the 1960s the union win rate had declined to approximately 60%, and by 1989 it had fallen below 50%.[122]

Unions now lose more representation elections in large part because employers resist union organizing campaigns more fiercely.[123] The last few decades have witnessed a sharp increase in unfair labor practices committed by employers.[124] Unfair labor

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New Evidence of 80s Gain by Richest, N.Y. TIMES, Apr. 21, 1992, at A1 (reporting that richest 1% of the population controls 37% of the nation's wealth, more than is controlled by the bottom 90% of the population).

[118] *See* EDWARDS, *supra* note 27, at 88; *see generally* William T. Dickens & Jonathan S. Leonard, *Accounting for the Decline in Union Membership, 1950–1980*, 38 INDUS. & LAB. REL. REV. 323 (1985).

[119] *See* EDWARDS, *supra* note 27, at 87, 89 (attributing union decline almost entirely to decrease in rate of union organizing); *see also* Mark A. Barenberg, *Democracy and Domination in the Law of Workplace Cooperation: From Bureaucratic to Flexible Production*, 94 COLUM. L. REV. 753, 983 n.839 (1994) ("structural and demographic changes account for only a small fraction of the decline of unionization rates").

[120] *See* JOHN L. LAWLER, UNIONIZATION AND DEUNIONIZATION: STRATEGY, TACTICS AND OUTCOMES 137 (1990) (reporting that between 1980 and 1985, the number of NLRB representation elections declined by one-half); Dickens & Leonard, *supra* note 118, at 332–33 (noting the decline in the number of representation elections from 1950 to 1980); *see also* EDWARDS, *supra* note 27, at 87 (reporting that fewer employees participate in representation elections each year).

[121] *See* GOULD, *supra* note 3, at 153; GOLDFIELD, *supra* note 1, at 23 (graph demonstrating sharp decline in union election victories); FREEMAN & MEDOFF, *supra* note 113, at 221–23 (noting sharp decline in union election victories from 1950 to 1980); Dickens & Leonard, *supra* note 118, at 332–33.

[122] *See* EDWARDS, *supra* note 27, at 87–88.

[123] *See* EDWARDS, *supra* note 27, at 90; Barenberg, *supra* note 119, at 931; *see also* Mark A. Barenberg, *The Political Economy of the Wagner Act: Power, Symbol and Workplace Cooperation*, 106 HARV. L. REV. 1381, 1494 (1993) (noting "intensified managerial resistance to union organizing campaigns"); Bronfenbrenner, *supra* note 93, at 80 (reporting that in 75% of 261 NLRB election campaigns studied, "employers engaged in active antiunion tactics").

[124] *See* GOLDFIELD, *supra* note 1, at 110.

practice charges against employers jumped from 4400 in 1955 to 22,500 in 1985, and the percentage of such charges found meritorious by the Board increased along with the number of charges.[125] Indeed, employer retaliation against employees for union activity has become so widespread that, as of 1985, for every ten employees who participated in a union representation election, one was unlawfully fired.[126] Such widespread lawlessness by employers has chilled efforts by employees to organize.[127]

Employers, however, need not resort to illegal behavior to defeat organizing drives; they possess considerable legal means to oppose unionization.[128] For example, employers have almost unlimited access to employees, and therefore can communicate their anti-union views to employees repeatedly throughout the period of a union's organizing campaign.[129] Unions, on the other hand, have no general right of access to employees at work, even in areas of the employer's premises that are open to the public.[130] Moreover, contacting employees away from the workplace poses a serious challenge for unions,[131] particularly since they have no

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[125] WEILER, *supra* note 3, at 237–38 (noting that "the increase in unfair labor practices is quite astounding"); *see also* FREEMAN & MEDOFF, *supra* note 113, at 232 (reporting that from 1960 to 1980, unfair labor practice charges against employers increased fourfold and that in the same period the number of employees awarded backpay or reinstated by the NLRB increased fivefold).

[126] WEILER, *supra* note 3, at 112.

[127] So the D.C. Circuit has suggested. *See* United Steelworkers of America v. NLRB, 646 F.2d 616, 634–35 (D.C. Cir. 1981) ("Widespread unlawful practices may create an atmosphere of fear chilling the exercise of employee rights guaranteed by the Act.").

[128] *See* EDWARDS, *supra* note 27, at 90 (noting legal framework that favors employers as reason for decline in union election victories).

[129] Bronfenbrenner, *supra* note 93, at 82 (noting that "employers have virtually unlimited opportunities to communicate aggressively with their employees during union campaigns"). The only limitation on employers' right to communicate their views to employees is the prohibition on "captive audience" meetings within 24 hours of the election. *See* P.E. Guerin, Inc., 309 N.L.R.B. 666, 670 (1992); Peerless Plywood Co., 107 N.L.R.B. 427, 429 (1953).

[130] *See* Lechmere, Inc. v. NLRB, 112 S. Ct. 841, 849 (1992) (denying union organizers access to parking lot in front of employer's store, and indicating that generally unions only have the right to enter an employer's premises in those rare cases where the employees live on the premises); Oakwood Hosp. v. NLRB, 983 F.2d 698, 702–03 (6th Cir. 1993) (holding that union organizer has no right to sit in hospital cafeteria open to public to discuss unionization with hospital employees when other means of access are available).

For a discussion of how the Supreme Court's *Lechmere* decision limits employees' opportunities to hear the union's message, *see generally* Peter D. DeChiara, *No Solicitation Allowed: Union Organizer Access After* Lechmere, Inc. v. NLRB, 43 LAB. L.J. 593 (1992).

[131] *See* JULIUS GETMAN ET AL., UNION REPRESENTATION ELECTIONS: LAW AND REALITY 90–92 (1976) (finding, in a study of organizing campaigns, that unions were able to get only about one-third of the workforce to attend union-sponsored meetings

right to a name and address list of the employees eligible to vote in the election until after an election date has been determined.[132] Such determinations often come weeks or months after an election petition has been filed.[133]

During a union organizing drive, an employer's announcement of its opposition to unionization, without more, would probably be enough to stir apprehension among the employees.[134] However, employers typically take an aggressive approach to countering organizing campaigns and use their almost unlimited access to employees to persuade them to vote against the union.[135] Employers commonly emphasize that collective bargaining may lead to strikes,[136] during which employees lose pay and are also subject to replacement.[137] To stir employees' fear of unions, em-

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held away from the employer's premises); Jay Gresham, Note, *Still As Strangers: Nonemployee Union Organizers on Private Commercial Property*, 62 TEX. L. REV. 111, 151–61 (1983) (discussing inadequacy of various means of union communication with employees away from company property).

[132] *See* Excelsior Underwear, Inc., 156 N.L.R.B. 1236, 1239–40 (1966) (holding that employer must submit to NLRB list of names and addresses of all eligible voters within seven days after election agreement or direction of election, after which the list will be made available by the NLRB to all parties). See CRAVER, *supra* note 3, at 142, for an argument that the *Excelsior* list should be made available to unions earlier.

[133] *See* 55TH ANNUAL REPORT OF THE NLRB 196 (1990) [hereinafter 1990 NLRB REPORT], reporting that in fiscal year 1990, the median period between the filing of an election petition and the election determination by the NLRB Regional Director was 44 days. The median was 314 days in cases where the election determination was made by the NLRB in Washington, D.C. *Id.* at 196.

[134] *See* Julius G. Getman, *Ruminations on Union Organizing in the Private Sector*, 53 U. CHI. L. REV. 45, 55 (1986).

[135] *See* GETMAN ET AL., *supra* note 131, at 90–91 (finding that employers held anti-union meetings at the workplace in 90% of campaigns studied); Getman, *supra* note 134, at 51 (noting that employers usually provide their employees with literature, styled as "fact sheets" or "informational bulletins," designed to persuade employees to vote against representation). For an account by a former management consultant of how "union avoidance" campaigns are conducted, see generally MARTIN J. LEVITT & TERRY CONROW, CONFESSIONS OF A UNION BUSTER (1993).

[136] *See* Getman, *supra* note 134, at 50 n.17, 52 (noting that employers often depict unions as strike-prone, and typically make statements to employees such as "'The only way a union can attempt to force your company to meet unrealistic union demands would be to pull you out on strike'"); LAWLER, *supra* note 120, at 148 (in 39.8% of organizing campaigns studied, employers made warnings of possible strikes).

Contrary to the image created by employers, collective bargaining negotiations rarely result in strikes. *See* PUETTE, *supra* note 28, at Appendix A (noting that just two percent of collective bargaining negotiations result in strikes); *see also* FREEMAN & MEDOFF, *supra* note 113, at 217 (reporting that between 1971 and 1980, just 2.6% of employees were on strike in a typical year). In recent years, strikes have become less frequent. *See Anti-Union Group Charges Ban on Replacing Strikers Would Increase Strike Activity*, DAILY LAB. REP. (BNA), Dec. 10, 1990, at A7 (reporting that 424 strikes involving over 1000 workers took place in the United States in 1974, while only 51 occurred in 1989).

[137] Getman, *supra* note 134, at 50.

ployers also typically emphasize that unions have internal by-laws that regulate the conduct of their members.[138]

C. *Employer Misrepresentations of Law*

The law, however, does not limit employers to telling the truth about these matters. Under *Midland National Life Insurance*,[139] the Board will not "probe into the truth or falsity of the parties' campaign statements."[140] On the theory that employees are sufficiently sophisticated to assess and discount misleading campaign propaganda,[141] the Board will only set aside an election based on misrepresentations if an employer uses forged documents that prevent employees from discerning the documents' source[142] or if the employer misrepresents Board ballots or Board procedures in such a way as to make it appear that the Board favors a particular election result.[143] The Board has repeatedly held that it will not set aside an election based on an employer's misstatement of law.[144] In the absence of Board regulation, employers

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[138] *See, e.g.*, ROBERT LEWIS & WILLIAM A. KRUPMAN, WINNING NLRB ELECTIONS: MANAGEMENT'S STRATEGY AND PREVENTIVE PROGRAMS 190 (1979), which advises employers to distribute literature telling employees that "[t]here are many complex rules and regulations which a member of the union must obey. You would have to live under these rules if you become a member." *Id.* Lewis and Krupman also suggest employers tell employees that "[b]eing in a union in many respects is like being in the military. You are told what to do and, if you refuse, you are disciplined." *Id.* Such statements form part of management's efforts to depict unions as bureaucratic, autocratic organizations unconcerned with employees' needs. *See* Getman, *supra* note 134, at 51 nn.21, 52.

[139] 263 N.L.R.B. 127 (1982).

[140] *Id.* at 133.

[141] *Id.* at 132. This theory is highly suspect, given most employees' ignorance of their rights under the Act. *See supra* notes 27–33 and accompanying text; *see also* CRAVER, *supra* note 3, at 141 (calling "naive" the premise that employees are not influenced by employer misrepresentations during organizing campaigns).

The Board's tolerance for campaign misrepresentations has had an uneven history. In 1962, in Hollywood Ceramics Co., 140 N.L.R.B. 221, 224 (1962), the Board held that it would set aside an election if a campaign statement substantially departed from the truth and was timed so as to deprive the other party of an opportunity to respond. In 1977, in Shopping Kart Food Market, Inc., 228 N.L.R.B. 1311, 1313 (1977), the Board ruled that it would no longer set aside an election solely because of inaccurate campaign statements. The next year, the Board abandoned *Shopping Kart* and returned to the *Hollywood Ceramics* standard. *See* General Knit, 239 N.L.R.B. 619, 623 (1978). In 1982, in *Midland National*, the Board reversed itself once again and embraced its current position in favor of the deregulation of campaign statements.

[142] *Midland Nat'l*, 263 N.L.R.B. at 133.

[143] *See* SDC Inv., Inc., 274 N.L.R.B. 556, 557 (1985) (holding altered sample ballot not objectionable when it was apparent that alteration was the work of one of the parties).

[144] *See* John W. Galbreath, 288 N.L.R.B. 876, 877 (1988); Tri-Cast Inc., 274 N.L.R.B.

often make misrepresentations to employees during organizing campaigns.[145]

In particular, employers can and do use misrepresentations of law to give employees the false impression that union representation would render them powerless to resist decisions made by the union. For example, employees have a fundamental right under the NLRA to refuse to participate in a strike.[146] In *Pattern Makers' League v. NLRB*,[147] the Supreme Court held that employees who are members of a union when a strike begins have a right to quit the union and return to work during the strike, and that a union violates the NLRA if it fines such a former member for returning to work.[148] Despite this clear right of employees not to strike, management consultants advise employers to tell their workers during union organizing drives that "[a] union is capable of calling you out on strike and making you walk a picket line."[149] Although unions have no power under law to compel employees to strike,[150] current Board law permits such a misrepresentation, and employees who are unfamiliar with the law will likely be persuaded.[151]

Similarly, it is an employee's fundamental right under the NLRA to decline to become a member of a union, even if the union serves as the employee's collective bargaining representative.[152] The most control a union can lawfully exercise over an employee who refuses to join is to require the employee to

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377, 378 (1985); County Line Cheese Co., 265 N.L.R.B. 1519, 1519 (1982); Furr's, Inc., 265 N.L.R.B. 1300, 1300 n.10 (1982).

[145] *See* Bronfenbrenner, *supra* note 93, at 82 (noting that "employer communications can and often do include distortion [and] misinformation"); LEVITT, *supra* note 135, at 1 (explaining that anti-union campaigns by employers rely heavily on a strategy of "lies" and "distortions").

[146] *See* 29 U.S.C. § 157 (1988) (giving employees the right to refrain from concerted activities); Trans World Airlines, Inc. v. Independent Fed'n of Flight Attendants, 489 U.S. 426, 436–37 (1989) (noting that NLRA protects employees' right to choose not to strike); Pattern Makers' League v. NLRB, 473 U.S. 95, 100 (1985).

[147] 473 U.S. 95 (1985).

[148] *Id.* at 106; *see also* Booster Lodge No. 405, International Ass'n of Machinists v. NLRB, 412 U.S. 84, 85 (1973); NLRB v. Granite State Joint Bd., Textile Workers Union, 409 U.S. 213, 217 (1972).

[149] CORNELIUS QUINN ET AL., MAINTAINING NONUNION STATUS 211 (1982); *see also* ALFRED T. DEMARIA, HOW MANAGEMENT WINS UNION ORGANIZING CAMPAIGNS 242–44 (1980).

[150] *See Trans World Airlines*, 489 U.S. at 436–37.

[151] *See generally* Amann & Silverblatt, *supra* note 28, at 58 (concluding that employees' ignorance of labor law "makes them susceptible to fraudulent or misleading claims and statements made by unions and/or management officials during a union organizing campaign").

[152] *See* 29 U.S.C. § 157 (1988) (giving employees the right to refrain from forming, joining or assisting labor organizations); *Pattern Makers' League*, 473 U.S. at 104–06.

pay certain fees to the union for negotiating and administering the collective bargaining agreement, and then only if the employer agrees to sign a union security agreement requiring such fees.[153] Moreover, the duty of fair representation under the NLRA prohibits a union in negotiating or administering a collective bargaining agreement from discriminating in any way against those employees who refuse to join.[154] Nonetheless, management consultants advise employers to tell their workers during organizing drives that "[a] union is run by union bosses *who have control over you.*"[155] Again, Board law permits such misleading statements and employees unfamiliar with the law will likely believe them.

D. *Employer-Created Employee Representation Plans*

Union election losses, and the resultant decline of union representation,[156] have left the vast majority of American workers without a representative on the job to advise them of their rights or to serve as their advocate. Many employers in recent years have sought to fill this void with employee representation plans of their own creation.[157] Resembling the "company unions" used by employers early in the twentieth century to discourage independent unions,[158] these representation plans frequently provide for certain selected employees to meet with management to dis-

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[153] *See supra* notes 101–102 and accompanying text; *see also Pattern Makers' League*, 473 U.S. at 106 n.16 ("the only aspect of union membership that can be required pursuant to a union shop agreement is the payment of dues").

[154] *See, e.g.*, Abilene Sheet Metal, Inc. v. NLRB, 619 F.2d 332, 347–48 (5th Cir. 1980) (finding that union breached duty of fair representation under NLRA when it failed to investigate or process employee's grievance because he was not a union member); American Postal Workers Union, 300 N.L.R.B. 34, 34 (1990) (holding that NLRA prohibits union from discriminating against non-members regarding access to grievance procedure or to union hiring hall); Teamsters Local Union 997, 298 N.L.R.B. 604, 607 (1990) (holding that a union violates Act by refusing to file grievance for employee because he was not a union member).

[155] QUINN ET AL., *supra* note 149, at 211 (emphasis added).

[156] *See supra* note 119 and accompanying text.

[157] *See* WEILER, *supra* note 3, at 191; Barenberg, *supra* note 123, at 1384, 1494 (noting that many non-union firms have implemented "collaborative" or "cooperative" workplace schemes in the past twenty years); David F. Girard di Carlo et al., *Legal Traps in Employee Committees*, 43 LAB. L.J. 671, 671 (1992) (citing 1988 study by the General Accounting Office that found 9 million American employees involved in employer-sponsored "employee involvement committees").

[158] *See* WEILER, *supra* note 3, at 213 (noting that today's "employee involvement plans" are "not fundamentally different in nature or purpose from the initial employee representation plans developed in the era of 'welfare capitalism' in the early twentieth century").

cuss a wide variety of workplace issues.[159] Although such plans are of questionable legality,[160] and may fall under the NLRA's ban on employer-dominated labor organizations,[161] they have nonetheless become a widespread phenomenon on the American industrial landscape. Because these plans in many ways imitate the operations of a worker-organized union, and indeed are frequently designed by the employer to substitute for an independent union,[162] employees involved in such plans may incorrectly believe that the plans preclude their organizing an independent union.

E. *Concerted Activity by Non-Union Employees*

Even without union representation, employees covered by the Act enjoy the fundamental right to engage in concerted activity for their mutual aid and protection.[163] Employees, for example, have the right collectively to make demands upon or voice grievances to their employer concerning terms or conditions of work, and the Act prohibits an employer from retaliating against employees for asserting such demands or grievances.[164] Employees not only have the right to make collective demands and to voice grievances, they also have a right under the Act to walk off the

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[159] *See* Comment, *The Encouragement of Labor-Management Cooperation: Improving American Productivity Through Revision of the National Labor Relations Act*, 40 UCLA L. REV. 571, 586 (1992); *see, e.g.*, Airstream, Inc. v. NLRB, 877 F.2d 1291 (6th Cir. 1989); NLRB v. Scott & Fetzer Co., 691 F.2d 288 (6th Cir. 1988); NLRB v. Northeastern Univ., 601 F.2d 1208 (1st Cir. 1979); Hertzka & Knowles v. NLRB, 503 F.2d 625 (9th Cir. 1974), *cert. denied* 423 U.S. 875 (1975); Ryder Distrib. Resources, Inc., 311 N.L.R.B. 814 (1993); Electromation, Inc., 309 N.L.R.B. 990 (1992), *enforced*, 32 F.3d 1147 (7th Cir. 1994).

[160] *See* Kohler, *supra* note 115, at 534–45; Barenberg, *supra* note 119, at 760.

[161] *See* 29 U.S.C. § 158(a)(2) (1988) (making it an unfair labor practice for an employer to dominate or interfere with the formation or administration of a labor organization). For examples of employee representation plans struck down as violative of the NLRA, *see Ryder*, 311 N.L.R.B. at 814 (striking down employer-created "wages and benefits committee" in which employees were paid to meet with management representatives to discuss wages); *Electromation*, 309 N.L.R.B. at 990 (striking down employer-created "action committees" in which employees were paid to discuss workplace issues with management representatives).

[162] *See* Kohler, *supra* note 115, at 504–05 (noting that employers frequently use employee participation schemes as a union avoidance technique).

[163] *See* 29 U.S.C. § 157 (1988).

[164] *See, e.g.*, Dayton Typographic Serv., Inc. v. NLRB, 778 F.2d 1188, 1191–93 (6th Cir. 1985) (finding that employer violated Act by discharging employee for voicing employees' demand for overtime compensation for work on Saturdays); Needell & McGlone, P.C., 311 N.L.R.B. 455 (1993) (holding that employer violated Act by discharging employee for voicing employees' concerns about preferential treatment given to another employee).

job in support of their grievances. In *NLRB v. Washington Aluminum*,[165] for example, the Supreme Court held that a group of non-union employees who walked off their job to protest the extremely cold temperatures in their workshop had engaged in protected activity under the Act, and that their employer violated the Act by firing them.[166] Other examples of protected collective action include work stoppages by non-union employees to demand a wage increase,[167] to seek a change in their work schedule,[168] or to protest having to work in inclement weather.[169]

In addition to protecting employee grievances and protests, the NLRA also protects efforts by employees to obtain information concerning their rights in the workplace when a group of employees share concern over the same issues and have voiced their concern to management. In *Salisbury Hotel, Inc.*,[170] for example, the Board held that the Act protected an employee's telephoning the Department of Labor to ask whether the employer's lunch hour policy was lawful, when the employee made the call as part of a group protest against the policy.[171]

Although these cases show that non-union employees on occasion exercise their right to engage in concerted activity, these cases are probably exceptional. Most likely, the vast majority of non-union employees remain ignorant of this right,[172] or are too fearful to exercise it. Therefore the potential power the NLRA provides them for improving their working conditions remains untapped.

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[165] 370 U.S. 9 (1962).

[166] *Id.* at 17. *See also* NLRB v. Jasper Seating Co., 857 F.2d 419, 420 (7th Cir. 1988) (holding that employer violated NLRA by firing two employees who walked off job because of cold temperatures in work area).

[167] *See* Molon Motor & Coil Corp. v. NLRB, 965 F.2d 523, 525 (7th Cir. 1992).

[168] *See* Holstead Metal Prods. v. NLRB, 940 F.2d 66, 71 (4th Cir. 1991).

[169] *See* Quality C.A.T.V., Inc., 278 N.L.R.B. 1282, 1282 (1986) (holding that employer violated Act by firing two television utility line repair workers who refused, on a rainy day, to climb wet utility poles).

[170] 283 N.L.R.B. 685 (1987).

[171] *Id.* at 685; *see also* Every Woman's Place, 282 N.L.R.B. 413, 413 (1986) (employee engaged in protected activity under the Act when she contacted DOL concerning the regulation of work on holidays on behalf of other employees who shared the same concern and had expressed the concern to management).

[172] *See* Morris, *supra* note 17, at 1675.

IV. Proposal for an Expanded Notice Requirement Under the NLRA

A. *The Proposed Notice*

The existing notice requirements under the NLRA, which mandate postings three days before an election or after an unfair labor practice determination,[173] are insufficient to inform employees of their NLRA rights. Notice under the NLRA, like notices under the numerous other statutes surveyed above,[174] should be posted in the workplace at all times. Accordingly, the Board should expand the NLRA's notice requirement by promulgating a rule that requires all employers covered by the Act to post at all times, in conspicuous places in the workplace, a notice of employee rights under section 7 of the Act.[175]

The text of the notice should be set by the Board. The proposed notice should include not only a recital of section 7 rights, but, like the Board's current Notice of Election, should also provide, in simple, concrete language, illustrations and examples of employee conduct protected by the Act and possible remedies for violations of the Act.[176] For example, the proposed notice should inform employees that they have a right to communicate to their employer grievances they share about terms and conditions of work, including grievances over pay, work schedules and physical conditions in the workplace.[177] The notice should further inform employees that they have the right to obtain information from third parties concerning their collective grievances and that they have the right to support such grievances

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[173] *See supra* notes 80–100 and accompanying text.

[174] *See supra* notes 51–79 and accompanying text.

[175] A petition for such a rule is currently pending before the Board. *See Morris Petition, supra* note 7. However, in contrast to this Article, Professor Morris's petition does not suggest illustrations and examples that should be provided in the notice. *See infra* notes 177–181 and accompanying text. Nor does it suggest any penalties that should result from an employer's failure to post the notice. *See infra* notes 182–189 and accompanying text. Furthermore, Professor Morris' petition lacks a detailed discussion of the probable benefits of, and possible arguments against, the proposed rule. *See infra* notes 190–229 and accompanying text.

[176] Like a summary plan description under ERISA, the text of the proposed notice should be written "in a manner calculated to be understood by the average employee." *See supra* note 54 and accompanying text. As with the Board's unfair labor practice notices, the notice proposed here should be posted in the language or languages known by a significant portion of the employer's employees. *See supra* note 100 and accompanying text.

[177] *See supra* note 164 and accompanying text.

with strikes.[178] The list of illustrations should also make it clear to workers that they have the right not to strike, even if their union calls a strike; that they have the right to quit a union or decline to join one; and that they have the right, even as non-members, to be fairly represented by the union that serves as their collective bargaining representative.[179] In regard to the right to organize, the notice should tell employees of their right to form or join a labor organization that is independent of their employer.

The proposed notice should state that the NLRB, an agency of the federal government, serves to protect employees' rights under the Act, and that employees who believe their rights have been violated should contact the Board.[180] Finally, the notice should inform employees that the Act requires the employer to post the notice.[181]

B. *Consequences for an Employer's Failure to Post the Notice*

To ensure compliance with the notice requirement, the Board should fine employers who fail to post the notice. Unlike Title VII and the FMLA,[182] the Board's rule should require a fine whether or not the employer's failure to post the notice was willful. Allowing employers a lack-of-willfulness defense would only invite litigation.[183] A strict liability standard for employers who fail to post the notice would make violations easier to detect,[184] make liability more certain, and make the Board's threat of a fine more credible.

If the employer's failure to post the notice occurs after a union files for a representation election which the union then loses, the

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[178] *See supra* notes 170–171 and accompanying text.

[179] *See supra* notes 146–148, 152–154 and accompanying text.

[180] Similar information is now provided by the Board's Notice of Election. *See supra* notes 84–85 and accompanying text.

[181] The notice requirement proposed here would be in addition to, not in lieu of, the Board's existing notice requirements. Accordingly, employers would still have to post the Board's Notice of Election before an election and post a cease-and-desist notice following an unfair labor practice determination.

[182] *See supra* notes 57, 72 and accompanying text.

[183] For examples of litigation under Title VII's posting requirement, *see supra* note 59 and accompanying text. Similar litigation occurred when the Board entertained a lack-of-bad-faith defense by employers who failed to post the Board's Notice of Election. *See supra* notes 90–91 and accompanying text.

[184] *Cf.* CRANSTON, *supra* note 42, at 275 (noting, in consumer law context, that a benefit of notice requirements as a form of regulation is that compliance can easily be checked).

failure should be deemed sufficient grounds for setting aside the election. As with the Board's strict three-day rule on the posting of its Notice of Election,[185] such a remedy would help ensure that employers notify employees of their rights under the Act. Finally, if an employer fails to post the proposed notice and then violates an employee's rights under the Act, such as by firing the employee for union activity, the employer's failure to post the notice should toll the six-month limitations period for the employee to file an unfair labor practice charge against the employer.[186] However, as the case law under Title VII and the ADEA suggests,[187] tolling should not apply if the employee can be presumed to have known her rights—if, for example, the employee is already represented by a union.[188]

These measures—fines, re-run elections and tolling of the limitations period—would probably be sufficient to obtain most employers' compliance with the notice requirement. The harsher measures outlined in President Bush's executive order concerning the *Beck* notice, such as publishing a list of employers who fail to comply or banning non-complying employers from federal contracts,[189] probably would be unnecessary.

V. The Benefits of a Rule Expanding the Notice Requirements Under the NLRA

A. *Concerted Activity*

As discussed above, the NLRA provides employees, whether represented by a union or not, the right to engage in concerted activity for their mutual aid and protection.[190] However, most employees covered by the Act, the vast majority of whom lack union representation,[191] are probably unaware of their right to engage in concerted activity.[192] The notice proposed here would inform such employees that they have a right to voice shared

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[185] *See supra* notes 89, 92–93 and accompanying text.

[186] *See* 29 U.S.C. § 160(b) (establishing six-month limitations period for the filing of unfair labor practice charges).

[187] *See supra* notes 60, 64 and accompanying text.

[188] *Cf.* Cruce v. Brazosport Independent School Dist., 703 F.2d 862, 864 (5th Cir. 1983) (no tolling on Title VII charge when employee was represented by union).

[189] *See supra* notes 106–107 and accompanying text.

[190] *See supra* note 163 and accompanying text.

[191] *See supra* note 1.

[192] *See supra* notes 27–33 and accompanying text.

grievances about the terms and conditions of their work, that they have a right to obtain information relevant to such grievances from government agencies or other third parties, and that they have the right to protest in support of their grievances through work stoppages.[193] Moreover, the notice would inform employees that they have recourse to the Board if their employer retaliates against them for such concerted activity.[194] Thus employees who see the notice, instead of quitting or suffering in silence, would be more likely to exercise their right to act together to improve conditions such as low pay,[195] undesirable work schedules,[196] or uncomfortable or dangerous conditions in the workplace.[197]

Moreover, the notice proposed here would probably boost employees' confidence that their employer would not retaliate against them for engaging in such concerted activity. The proposed notice would state that it was government-mandated. Thus, simply by posting it, management would indicate to the employees that the employer complies with federal labor law, at least to the extent of meeting the notice requirement. This might lead the employees to believe that their employer would also comply with the NLRA's prohibition against retaliation. The notice would thus help give employees the courage to engage in lawful concerted activity.[198]

Informing workers of their right to act concertedly would also probably help deter employers from retaliating. The proposed notice would make employers aware that their employees know their rights. Managers who would engage in unlawful retaliation if they believed they could escape liability might hesitate if they had reason to believe that employees would seek protection from the Board.

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[193] *See supra* notes 177–178 and accompanying text.

[194] *See supra* note 180 and accompanying text.

[195] *See supra* note 113 for data concerning the falling real wages of American workers.

[196] See generally JULIET B. SCHOR, THE OVERWORKED AMERICAN: THE UNEXPECTED DECLINE OF LEISURE (1991), for a discussion of the lengthening of the American workday and the adverse effects long hours of work have on American workers.

[197] For examples of cases in which non-union employees exercised their rights to act concertedly, see *supra* notes 165–171 and accompanying text.

[198] Analogously, *Miranda* warnings do more than simply inform criminal suspects of their rights; just by giving the warnings, the police show the suspect that they are complying with the law and thus help assure the suspect that her rights will be respected. *See supra* note 50 and accompanying text.

Concededly, the notice's deterrent effect on employer unfair labor practices would be limited. Most employers know that the Board acts slowly,[199] that establishing violations of the Act is difficult,[200] and that Board remedies are not particularly burdensome.[201] Nonetheless, the deterrent effect would probably provide some measurable protection to employees who choose to engage in concerted activity, and would help limit the number of unfair labor practices committed by employers.

Telling employees that they have a right to walk off the job in concerted protest might also have the indirect effect of encouraging collective bargaining. Employers' tolerance for spontaneous job actions that disrupt operations would likely be minimal, and employers who are disinclined to react by unlawfully retaliating against the employees might instead seek to calm a restive workforce by agreeing to recognize a collective bargaining agent for the employees. Once in place, a union would almost certainly agree to a contractual no-strike clause relinquishing the employees' right to engage in job actions during the term of the contract.[202] Thus, simply telling workers of their right to engage in concerted activity could indirectly boost collective bargaining.

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[199] During the 1990 fiscal year, the median time for an unfair labor practice charge to be resolved by the NLRB was 688 days. *See* 1990 NLRB REPORT, *supra* note 133, at 196; *see also* Peter G. Bruce, *On the Status of Workers' Rights to Organize in the United States and Canada*, in AMERICAN LABOR LAW, *supra* note 5, at 273, 281 (comparing processing times for unfair labor practice cases in the United States and Canada and noting that the NLRB took four to five times longer to process cases that go to hearing than the Ontario Labor Relations Board).

[200] *See* Wright Line, Inc., 251 N.L.R.B. 1083, 1089 (1980) (stating that it is insufficient, to establish a violation of Act, for the Board's general counsel to prove that an employer took adverse action against an employee "in part" for the employee's union activities; the employer may avoid liability by showing that it would have taken the action even absent the employee's union activities).

[201] *See* WEILER, *supra* note 3, at 234 (explaining that an employer liable for having discharged an employee in violation of the Act faces a monetary penalty in the amount of no more than the employee's back wages, less amounts the employee earned or could have earned at other jobs after having been discharged).

[202] Of 400 collective bargaining agreements sampled from around the country, 95% either completely banned strikes or allowed strikes in only certain limited circumstances. BUREAU OF NAT'L AFFAIRS, *supra* note 114, at 93. If a union strikes in violation of a no-strike clause, a federal court has the power to enjoin the strike. *See* Boys Market, Inc. v. Retail Clerks Union, Local 770, 398 U.S. 235, 252–53 (1970).

B. *Union Organizing Campaigns*

In addition to encouraging concerted activity by non-union employees, the notice proposed here would probably encourage them to exercise their right to organize, a right of which many employees are probably ignorant.[203] Once informed of their right to organize, employees previously ignorant of that right would be more likely to seek a collective bargaining representative.[204]

A government-mandated notice posted by the employer would likely increase organization even among those employees who had already been informed by another source—such as a union—that they have the right to organize. Because the source of information often determines its impact upon the recipient,[205] a worker would probably be more likely to believe that the federal government protects her right to organize if she received such information from a government-mandated notice[206] rather than from a union organizer, whom, due to limitations on union access, she may never meet in person,[207] and whom the employer tells her is not to be trusted.[208] Indeed, as discussed above,[209] the proposed notices, which would indicate that it was government-mandated,[210] would demonstrate the employer's willingness to comply with federal labor law and would thus increase employ-

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[203] *See supra* notes 27–33 and accompanying text.

[204] As discussed above, an employer need only post the Board's current Notice of Election after an election has already been scheduled and is just three days away. *See supra* note 80 and accompanying text. It thus does not serve to help trigger organizing drives.

[205] *See* Brenda J. Nordenstam & Joseph F. DiMento, *Right-to-Know: Implications of Risk Communications Research for Regulatory Policy*, 23 U.C. DAVIS L. REV. 333, 346 (1990) ("Social psychologists have repeatedly demonstrated that the communication's source influences the information's effectiveness, including an acceptance of the message.").

In representation cases, the Board has specifically rejected notices from the parties as a substitute for its own official Notice of Election. *See supra* note 87 and accompanying text.

[206] *See* Nordenstam & DiMento, *supra* note 205, at 361 (listing government agencies as a credible source of information).

[207] *See supra* notes 130–133 and accompanying text.

[208] *See* Getman, *supra* note 134, at 51–52 ("A significant part of almost all management campaigns is the argument that the union organizers are outsiders, interested in the employees solely as a source of dues and initiation fees."); LEVITT, *supra* note 135, at 26 (describing management consultant's letter to employees that portrayed union organizers as "self-serving outsiders" who would lie to the employees); DEMARIA, *supra note* 149, at 268 (advising employers to tell employees that "you can't trust union organizers!").

[209] *See supra* note 198 and accompanying text.

[210] *See supra* note 181 and accompanying text.

ees' confidence that their employer would respect the statutory prohibitions against interference with organizing efforts.

Government-mandated notices informing employees of the right to organize would be particularly important in workplaces where the employer has instituted some form of employee representation plan. Because employee representation plans in many ways resemble worker-organized unions,[211] employees in such workplaces may incorrectly believe that the employee representation plan precludes the formation of an independent union. The proposed notices would inform the millions of employees involved in employer-created employee representation plans[212] that, despite the employer-created plan, they can still join an independent union.

Not only would a posted notice help trigger more organizing drives, but it could lead to more union election victories, and thus help fulfill the national policy of encouraging collective bargaining.[213] Employers' awareness that their employees know their rights would, at least to some extent, deter employers from retaliating against their employees for engaging in organizing activities.[214] While the Board's current Notice of Election probably produces such a deterrent effect for the last three days of the election campaign, the proposed notice would extend the deterrent effect throughout the duration of the campaign, which can continue for weeks or months.[215] Free from the chilling effects of employer retaliation, employees would be more likely to vote for a collective bargaining agent.

Informing employees of their NLRA rights throughout the course of the organizing campaign would also make them less susceptible to employer propaganda concerning the consequences of unionization. For example, when told that a "union is capable of calling you out on strike and making you walk a picket line,"[216] the employees would know that they have a fundamental right not to engage in a strike, or any concerted activity, with which they disagree.[217] Similarly, when told that a "union is run by union bosses who have control over you,"[218] informed em-

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[211] *See supra* note 162 and accompanying text.
[212] *See supra* note 157 and accompanying text.
[213] *See supra* note 109 and accompanying text.
[214] *See supra* notes 199–201 and accompanying text.
[215] *See supra* note 133 and accompanying text.
[216] *See supra* note 149 and accompanying text.
[217] *See supra* note 179 and accompanying text.
[218] *See supra* note 155 and accompanying text.

ployees would know that they have a right to quit the union if they come to disagree with its policies, and that the union has a statutory obligation to represent them fairly whether they are members or not.[219] Made aware by an official notice that they retain certain fundamental individual rights even while represented by a union, employees would probably be less fearful of opting for unionization.[220]

VI. Possible Arguments Against an Expanded Notice Requirement Under the NLRA

Employers will likely oppose the proposed rule requiring them to post notices of NLRA rights in the workplace. This Part addresses the arguments that employers might offer to justify their opposition.

First, employers might argue that having to post and continually maintain notices of NLRA rights in the workplace would be burdensome. However, the government already requires numerous postings, many for statutes, such as the Employee Polygraph Protection Act, which are less significant than the NLRA.[221] Many employers within the Act's coverage already maintain bulletin board space for these mandated notices; posting notices of NLRA rights would add only marginally to the cost and effort needed to comply with these existing posting requirements. Moreover, since the text of the proposed notice would be set by the NLRB,[222] employers would be spared the time and effort of drafting language to meet the new NLRA notice requirement.

Employers who have not engaged in unfair labor practices might also argue that it would be unfair to require them to post NLRA notices when they have never violated the Act. However, other mandated postings, including the NLRB's Notice of Election, must be displayed even if the employer has been completely law-abiding.[223] Moreover, in weighing the fairness of re-

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[219] *See supra* note 179 and accompanying text.

[220] In addition to encouraging employees to exercise their rights under the Act, the rule proposed here, by fining employers who fail to post the notice, *see supra* notes 182–184 and accompanying text, would also have the incidental benefit of generating revenue for the Board, an agency that is sorely underfunded. *See General Counsel Cites Dwindling Resources as Impairing Effectiveness of Labor Board*, Daily Lab. Rep. (BNA), July 11, 1994, at CC1 (noting that NLRB's staff declined from 3000 in 1980 to 2000 in 1994, despite 20% increase in cases per staff slot since 1985).

[221] *See supra* notes 51–79 and accompanying text.

[222] *See supra* note 176 and accompanying text.

[223] *See supra* notes 57–93 and accompanying text.

quiring all employers to post the proposed notice, one should note that law-abiding non-union employers may have benefitted from the unfair labor practices committed by others: widespread acts of employer retaliation against union supporters[224] send a chill throughout the workforce and tend to reduce the propensity for unionizing even among employees who work for law-abiding employers.[225] Since they may have benefitted from the overall chill on organizing activity, even employers who have not committed unfair labor practices should be required to share in the effort to reduce employee fear and ignorance by posting notices of NLRA rights.

Employers might also argue that posting notices of NLRA rights would provoke employee unrest, resulting in spontaneous work stoppages and other conduct detrimental to productivity. This objection exaggerates the effect that the proposed notice is likely to have on employees. Even in the unionized sector, the loss of wages from not working and the willingness of employers to hire permanent replacements[226] make employees loathe to strike.[227] In the non-union sector, where employees lack the financial support of union strike benefits and the logistical support provided by union organizers, strikes are even less likely. Thus, even if non-union employees learned of their right to engage in concerted job actions, and had the courage to attempt them, such actions would likely be limited to brief and small-scale protests.

Moreover, such protests, while perhaps causing some minor, short-term disruption to production, could in the long run be useful to employers; as manifestations of employee discontent, protests would inform an employer of problems in the workplace, giving the employer the chance to remedy them and thus improve employee morale and productivity.

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[224] *See supra* notes 123–127 and accompanying text.

[225] Analogously, the Board has determined that widespread unfair labor practices by a multi-plant employer chill organizing efforts even at the plants where no labor violations have occurred. *See* United Steelworkers of America v. NLRB, 646 F.2d 616, 635 (D.C. Cir. 1981). In such cases, the Board has ordered postings at all of the employer's facilities. *Id.* ("To offset companywide effects caused by extensive unlawful conduct, courts and the Board have expanded remedial measures beyond the actual locations at which unfair labor practices were found."); *see also* Procter & Gamble Mfg. Co. v. NLRB, 658 F.2d 968, 987–88 (4th Cir. 1981).

[226] *See* GOULD, *supra* note 3, at 186 (reporting General Accounting Office's estimate that in 1989, 35% of employers faced with strikes announced they would permanently replace strikers, and that, of these, 46% actually did). While President Clinton recently issued an executive order to limit the use of permanent replacements, the order only affects federal contractors. *See infra* note 230.

[227] *See supra* note 136.

In any case, even if postings of NLRA rights were to generate some labor unrest, such unrest would be no reason to deprive employees of knowledge of their rights. Should labor unrest ever become a major problem in this country, Congress could respond by changing the law. However, so long as the law of the land gives employees the right to engage in concerted activity, employees should know about it.

Finally, citing the adage that "a little knowledge is a dangerous thing," employers might argue that postings could induce employees to take actions that they incorrectly believe constitute protected activity, but in fact could subject them to discipline or discharge. What constitutes protected activity under the NLRA is a question that lawyers, Board members, judges and scholars have pondered since the Act became law, and the answers have evolved and changed, with innumerable permutations and wrinkles, for nearly sixty years.[228] Surely, one could argue, a simple posting could not sufficiently inform a lay person of his or her legal rights under the Act.

Clearly, a posting could not begin to explicate all of the fine doctrinal threads woven over the years concerning what does or does not constitute protected activity under the Act. Nonetheless, a posting would benefit employees by setting forth the basic rights contained in the Act and by providing illustrations of protected activity, such as the right of employees to communicate to their employer shared grievances over terms and conditions of work.[229] While the posting would not provide complete information on employees' rights under the NLRA, it would provide a starting point, and employees with further questions could contact a union, lawyer, or other third-party for advice before taking an action about which they are uncertain.

VII. Mandating Notices Through NLRB Rulemaking

Rather than seeking amendment of the Act, this Article proposes that the NLRB establish the expanded notice requirement through its rulemaking authority. Amendment of the Act itself

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[228] *See Chairman Gould Lists Goals for NLRB: Highlights Clarity and Practicality*, Daily Lab. Rep. (BNA), Apr. 8, 1994, at AA-1 (quoting NLRB Chairman William Gould's observation that the Board has often become "bogged down in complex doctrine and dogma," raising issues that sound like "[h]ow many angels can stand on the head of a legal needle?").

[229] *See supra* note 177 and accompanying text.

would be exceedingly difficult, given the resistance in Congress to legislative reform that would empower employees.[230] Therefore, an expanded notice requirement would likely have to come not from Congress but from the Board itself.[231]

There is little doubt that the Board has the power to promulgate the proposed rule and that such a rule would pass judicial muster. As the Supreme Court has noted, the Board has the "authority to develop and apply fundamental labor policy."[232] In particular, section 6 of the Act gives the Board authority "to make . . . such rules and regulations as may be necessary to carry out the provisions of [the Act]."[233] In reviewing an NLRB rule, the courts show considerable deference to the Board's expertise, upholding the rule so long as it is (1) rational and (2) consistent with the Act.[234] Since it would have the benefits discussed above,[235] the rule proposed here would clearly meet the rationality test. Moreover, since the proposed notice would inform employees of rights they have under the Act, the rule would

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[230] *See* Morris, *supra* note 7, at 106 (noting the difficulty of achieving labor law reform because "[i]t is a simple fact of political life that most labor issues are too controversial, Republican filibusters are too likely, and the prospect of achieving sufficient consensus as to what major law changes will be deemed necessary or desirable is too remote.").

The most notable recent example of an unsuccessful effort to amend the Act was the defeat of the proposed ban on the hiring of permanent replacements. *See* CRAVER, *supra* note 3, at 145; Asra Q. Norman, *Senate Ban of Permanent Replacement of Strikers Is Stalled, in Labor Defeat*, WALL ST. J., July 13, 1994, at A2. Unable to achieve a legislative ban on the hiring of permanent replacements, President Clinton in 1995 issued an executive order prohibiting federal government agencies from contracting with employers that permanently replace lawful strikers. *See President Clinton's Executive Order Sanctioning Federal Contractors that Hire Permanent Striker Replacements*, DAILY LAB. REP. (BNA), Mar. 9, 1995, at D28.

In 1978, a modest labor law reform bill failed even with a Democratic president and Democrats controlling both houses of Congress. *See* FREEMAN & MEDOFF, *supra* note 113, at 202–04; *see generally* BARBARA TOWNLEY, LABOR LAW REFORM IN U.S. INDUSTRIAL RELATIONS (1986).

[231] Indeed, current NLRB Chairman William Gould has announced his plan to increase the Board's use of its rulemaking procedures. *See* DAILY LAB. REP. (BNA), *supra* note 228, at AA-1.

[232] Beth Israel Hosp. v. NLRB, 437 U.S. 483, 500 (1978); *accord* Local 1384, UAW v. NLRB, 756 F.2d 482, 486 (7th Cir. 1985).

[233] 29 U.S.C. § 156 (1988); *see* American Hosp. Ass'n v. NLRB, 499 U.S. 606, 609 (1991). For examples of Board rulemaking pursuant to section 6, see *id.* (upholding Board rule defining bargaining units for acute care hospitals); New York Racing Ass'n, Inc. v. NLRB, 708 F.2d 46 (2d Cir. 1983) (upholding Board rule declining to assert Board jurisdiction over horse- and dog-racing industries). In making rules pursuant to section 6 of the Act, the Board must follow the procedures set forth in the Administrative Procedure Act. *See* 29 U.S.C. § 156 (1988); *New York Racing Ass'n*, 708 F.2d at 49.

[234] NLRB v. Curtin Matheson Scientific, Inc., 494 U.S. 775, 787 (1990); NLRB v. Bakers of Paris, Inc., 929 F.2d 1427, 1440 (9th Cir. 1991).

[235] *See supra* notes 190–220 and accompanying text.

most likely be deemed consistent with the Act. Finally, the fact that the Board has mandated other notices, such as its Notice of Election, without express statutory authorization,[236] shows its authority to mandate the notice proposed here.

VIII. CONCLUSION

While federal law requires employers to post notices in the workplace of employees' rights under numerous employment statutes, no such general posting requirement exists under the NLRA, which is arguably the most important labor statute of all. As a result, most employees covered by the Act probably remain ignorant of their NLRA rights, such as the right to organize and to engage in protected concerted activity, including airing shared grievances, seeking relevant information from government agencies or other third parties, and engaging in work stoppages to support such grievances.

To remedy this anomaly among federal employment posting requirements, this Article proposes that the NLRB use its rulemaking authority to promulgate a rule that would require all employers covered by the Act to post and maintain notices to their employees informing them of their NLRA rights. Such a notice, which would impose a negligible burden on employers already required to post other employment law notices, would have tangible benefits for American workers. Employees' knowledge of their rights under the Act would not only encourage them to exercise those rights, including the right to organize, but also could help deter employer unfair labor practices, which have reached alarmingly high levels. Informed employees would also be better able, during union organizing drives, to evaluate employer campaign propaganda, which is now largely unregulated by the Board. Thus, by helping employees learn about their rights to organize, to engage in concerted activity and to refrain from such activity, the Board's promulgation of the rule proposed here would constitute a modest but achievable step to-

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[236] *See supra* note 80 and accompanying text. In NLRB v. Express Publishing, Co., 312 U.S. 426 (1941), the Supreme Court held that the Board has the authority to require employers to post cease-and-desist notices following unfair labor practice determinations. Similarly, the required notices to employees of their rights under the FLSA and OSHA stem not from express mandate in those statutes, but from the Department of Labor's own regulations. *See supra* notes 75–79 and accompanying text.

wards shoring up the nation's eroding collective bargaining system.

REVIEW ESSAY

A SQUARE PEG IN A VICIOUS CIRCLE: STEPHEN BREYER'S OPTIMISTIC PRESCRIPTION FOR THE REGULATORY MESS

ERIC J. GOUVIN*

BREAKING THE VICIOUS CIRCLE: TOWARD EFFECTIVE RISK REGULATION. By *Stephen Breyer*. Cambridge, Mass.: Harvard University Press, 1993. Pp. 3, 124, notes, index. $22.95 cloth, $14.95 paper.

Long before his appointment to the United States Supreme Court, Stephen Breyer established his academic credentials as a scholar of the regulatory process.[1] His most recent book on regulatory reform, *Breaking the Vicious Circle: Toward Effective Risk Regulation*,[2] undoubtedly will attract attention from the legal and regulatory communities on the basis of his academic and legal background alone.[3] Nonetheless, his recent ascension to the high court is certain to spark public interest in his views

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[1] *See, e.g.*, STEPHEN G. BREYER, REGULATION AND ITS REFORM (1982) [hereinafter BREYER, REGULATION]; STEPHEN G. BREYER & RICHARD B. STEWART, ADMINISTRATIVE LAW AND REGULATORY POLICY: PROBLEMS, TEXT AND CASES (3d ed. 1992); Stephen G. Breyer, *Analyzing Regulatory Failure: Mismatches, Less Restrictive Alternatives, and Reform*, 92 HARV. L. REV. 547 (1979); Stephen G. Breyer, *Antitrust, Deregulation, and the Newly Liberated Marketplace*, 75 CAL. L. REV. 1005 (1987).

[2] STEPHEN G. BREYER, BREAKING THE VICIOUS CIRCLE: TOWARD EFFECTIVE RISK REGULATION (1993) [hereinafter BREYER].

[3] Justice Breyer has an impressive resume. He studied at Stanford, Oxford, and Harvard Law School; clerked for Justice Goldberg of the Supreme Court; and served on the Harvard Law School faculty. He has held several positions in Washington: in 1973 he served on the Watergate prosecution team; in 1974–75 he was a special counsel to the Senate Judiciary Committee Subcommittee on Administrative Practices; and in 1979–80 he served as counsel to the Senate Judiciary Committee. Breyer was appointed to the United States Court of Appeals for the First Circuit in 1981, elevated to Chief Judge of that court in 1990, and ultimately appointed to the United States Supreme Court in 1994. For a tidy summary of his professional accomplishments, see David Margolick, *Man in the News: The Supreme Court; Scholarly Consensus Builder: Stephen Gerald Breyer*, N.Y. TIMES, May 14, 1994, at A1; and Paul M. Barrett, *High Court Choice Is Strong Thinker Who Offers Something for Everyone, No Distinct Agenda*, WALL ST. J., May 16, 1994, at A20.

on regulation. Whether expert or layman, anyone alarmed by the current state of the regulatory process and concerned with prospects for its improvement will find that Justice Breyer's ideas and observations merit serious consideration. Fortunately, Justice Breyer has written an exceptionally accessible book.

The book says much more about the regulatory process generally than its title suggests. While it certainly can stand on its own as an analysis of health and safety regulation, the book's true significance lies in the warnings it sounds concerning the regulatory process in general. Although Breyer's earlier work regarded "generic" approaches to regulatory reform with suspicion and argued instead that reform should proceed on a "step by step, program by program" basis,[4] much of the discussion in *Breaking the Vicious Circle* is generic in the sense that it can be applied to substantive areas other than health and safety regulation without losing much in translation. Thus, with his current extrapolation from the specific example of risk regulation to regulation generally, Justice Breyer sees himself following the admonition of Oliver Wendell Holmes "to look for the 'general' in the 'particular.'"[5]

With characteristically clear insight, Justice Breyer identifies several systemic problems that plague the regulatory process in the United States. He discusses how public (mis)perceptions, congressional (over)reaction, and technical (un)certainty create a "vicious circle" that increasingly undermines the legitimacy of the regulatory process. However, Breyer does more than merely criticize from the sidelines. He presents a thought-provoking proposal for the reform of the regulatory process that deserves full and fair consideration.[6]

This Review outlines the systemic problems and the "vicious circle" identified by Justice Breyer and then proceeds to review his proposed solution. The final part presents several criticisms of his proposal and concludes that, while Breyer's modest suggestions may help at the margin, they settle for tinkering with the system instead of giving it the overhaul it really needs.

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[4] BREYER, REGULATION, *supra* note 1, at 341.

[5] BREYER, *supra* note 2, at ix.

[6] *See* BREYER, *supra* note 2, at 59–61; *see also infra* notes 34–46 and accompanying text.

I. SYSTEMIC PROBLEMS AND THE VICIOUS CIRCLE

In the first section of his book, Justice Breyer describes three pervasive problems that plague the regulatory system. Using apt, real-world illustrations, Justice Breyer identifies and discusses what he calls the "tunnel vision" or "last 10 percent" problem,[7] the "random agenda" problem,[8] and the "inconsistency" problem.[9]

The first of these problems, the "tunnel vision" or "last 10 percent" problem, arises when regulators, either through their own zeal or because they are carrying out a legislative directive, seek to eradicate a given hazard entirely, even though cleaning up the "last" ten percent is inordinately expensive compared to the increase in public safety it provides.[10] Essentially, the problem is that regulators do not know when to stop. Using fitting examples from the regulation of polychlorinatedbiphenyls, asbestos, and benzene, Justice Breyer shows how targeting the last ten percent not only costs too much, but might even create more safety hazards than it cures.[11]

Breyer next identifies what he calls the "random agenda" problem.[12] In examining some of the hazards the Environmental Protection Agency (EPA) has chosen to target, he finds that the agency's regulatory priorities are not determined by detached experts who carefully spend scarce resources to get the greatest benefit at the lowest cost. Instead, the agency's agenda is often driven by public fears, politics, history, and even chance.[13] Thus,

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[7] BREYER, *supra* note 2, at 11–19.

[8] *Id.* at 19–21.

[9] *Id.* at 21–28.

[10] *Id.* at 11.

[11] *Id.* at 12–15. For example, "cleaning up" asbestos in public buildings causes asbestos fibers that would have remained harmlessly in place to become airborne, increasing significantly the chance of those fibers lodging in workers' lungs and creating medical problems. *Id.* at 12.

[12] *Id.* at 19. Breyer's concern with agendas comports with the concern of other scholars who have studied the role of agendas in the legislative and regulatory process. The control of agendas can have a profound impact on the outcome of the policy process. *See generally* DANIEL A. FARBER & PHILIP P. FRICKEY, LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION 38–42 (1991); SHAUN H. HEAP ET AL., THE THEORY OF CHOICE: A CRITICAL GUIDE 249–58 (1992); Kenneth A. Shepsle, *Prospects for Formal Models of Legislatures*, 10 LEGIS. STUD. Q. 5 (1985); Barbara Sinclair, *Agenda Control and Policy Success: Ronald Reagan and the 97th House*, 10 LEGIS. STUD. Q. 291 (1985).

[13] BREYER *supra* note 2, at 20. Consistent with Justice Breyer's anecdotal reports on the hazardous substance regulatory agenda, an empirical study examining the EPA's rulemaking agenda concluded that pressure from Congress "distorts priorities and prevents realistic agenda setting and deadline compliance." Steven J. Groseclose,

not only does the agenda fail to address the problems that experts consider the most serious, but the problems that it does address change with the political winds. For example, the agenda reflects the public's obsession with cancer to the exclusion of other serious maladies, such as neurological damage.[14]

The third systemic ill that Justice Breyer identifies is the "inconsistency" problem that results from the lack of coordination among the many agencies and experts whose efforts are brought to bear on a particular issue.[15] In the area of hazardous material regulation, for instance, the EPA found chlorofluorocarbons (CFCs) to be a hazardous substance. That determination, and the consequent threat of liability under the Comprehensive Environmental Response, Compensation, and Liability Act[16] (CERCLA), severely undermined the efforts of the EPA's Office of Air and Radiation to encourage the recycling of refrigerators because few recycling companies wanted to assume the potential liability of a CERCLA clean-up.[17] While the EPA classified CFCs as hazardous, the Food and Drug Administration (FDA) continued to condone the use of CFCs in asthma inhalers.[18] The widely disparate treatment of CFCs by different branches of the EPA and between the EPA and the FDA sent confusing messages to the public.

In the second section of the book, Justice Breyer explores the role played by these systemic problems in the "vicious circle" that is created by the complex interaction of public perceptions, congressional reaction, and uncertainties in the technical regulatory process.[19] The public's perception of problems starts the vicious circle in motion. Justice Breyer describes how the public frequently misperceives the gravity of risks because, as Oliver Wendell Holmes observed, "most people think dramatically, not quantitatively."[20] As a result of sloppy thinking, the public con-

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Reinventing the Regulatory Agenda: Conclusions From an Empirical Study of EPA's Clean Air Act Rulemaking Progress Projections, 53 MD. L. REV. 521, 533 (1994).

[14] BREYER, *supra* note 2, at 20.

[15] *Id.* at 21–28.

[16] Comprehensive Environmental Response, Compensation and Liability Act of 1980, Pub. Law No. 96-510, 94 Stat. 2767 (1980), as amended by the Superfund Amendments and Reauthorization Act of 1986, Pub. Law No. 99-499, 100 Stat 1613 (1986) (codified as 42 U.S.C. §§ 9601–9675 (1988 & Supp. 1993).

[17] BREYER, *supra* note 2, at 22.

[18] *Id.*

[19] *Id.* at 33–51.

[20] *Id.* at 37. Breyer catalogs several factors that tend to confuse the public and cause them to reach incorrect conclusions, including the use of rules of thumb, overreaction

sistently overestimates the risk of certain hazards, such as getting cancer, and underestimates the risk of other hazards, such as contracting tuberculosis.[21] In the public's mind, the absolute regulation of risks that are perceived to be great (though they are actually remote) takes precedence over the regulation of truly serious risks that are not as well-known.

The vicious circle continues when the public communicates its fears and concerns to Congress.[22] In Breyer's view, Congress contributes to the vicious circle by responding to public perceptions of risk with detailed statutes. These statutes appear to give discretion to agencies but actually tie their hands and prevent flexible responses to the public's perceived "problem."[23] While there may be political reasons for Congress to act in this manner,[24] Breyer believes that Congress is poorly suited to the task of writing specific regulatory language because, for various structural and political reasons,[25] it cannot take a coherent view of the various problems it considers.[26]

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to prominent or sensational news, protective feelings for family and friends, inability to differentiate between conflicting expert opinions, preconceived opinions, and math anxiety. *Id.* at 35–37. His list certainly is not exhaustive. He could have added to it other basic analytical infirmities of the general public such as: lack of basic reading skills, *see* IRWIN S. KIRSCH ET AL., NATIONAL CENTER FOR EDUCATION STATISTICS, ADULT LITERACY IN AMERICA (1993); inability or unwillingness to process data that has been disclosed, *see* William N. Eskridge, Jr., *One Hundred Years of Ineptitude: The Need for Mortgage Rules Consonant with the Economic and Psychological Dynamics of the Home Sale and Loan Transaction*, 70 VA. L. REV. 1083, 1112–18 (1984); and susceptibility to "information overload," *see* Jeff Sovern, *Toward a Theory of Warranties in Sales of New Homes: Housing the Implied Warranty Advocates, Law and Economics Mavens, and Consumer Psychologists Under One Roof*, 1993 WIS. L. REV. 13, 27–30 (1993).

[21] BREYER, *supra* note 2, at 37.

[22] *Id.* at 39–42.

[23] *Id.* at 39–40. Helen Garten described a similar problem in federal banking regulation where congressional action has frequently impeded the efforts of regulators to fashion a coherent regulatory policy. *See* HELEN A. GARTEN, WHY BANK REGULATION FAILED: DESIGNING A BANK REGULATORY STRATEGY FOR THE 1990S (1991).

[24] Such political considerations might include congressional distrust of the executive branch to carry out a broadly worded statute or congressional desire to take political credit for a "tough" law. BREYER, *supra* note 2, at 41–42.

[25] For example, because Congress typically enacts one statute at a time, it rarely considers an entire regulatory program at once. In addition, bills originate in different committees, many of which have overlapping jurisdiction. Committees may also have radically different ideas about what should be addressed and how. Finally, Congress's need to reflect and respond to public opinion makes it a poor candidate for establishing a rational regulatory agenda, given the public's difficulty with understanding risks. *Id.* at 42.

[26] *Id.* Regarding the structural deficiencies of Congress in addressing regulatory matters, see also Eric J. Gouvin, *Truth in Savings and The Failure of Legislative Methodology*, 62 U. CIN. L. REV. 1281 (1994); Edward L. Rubin, *Legislative Methodology: Some Lessons from the Truth-in-Lending Act*, 80 GEO. L.J. 233 (1991).

Congress probably plays an even greater role in Breyer's vicious circle than he acknowledges. While Breyer sees the institution as merely reflecting misguided public notions, Congress itself is at least as great a source of misinformation and misperceptions as the public at large. It seems only fair to assume that members of Congress are subject to the same analytical weaknesses as the public when it comes to risk perception. Because so much legislation begins in congressional offices and does not in fact spring from a great public outcry, the misperceptions of members of Congress, not their constituents, may become enshrined in the law.[27] If that is the case, then the vicious circle may begin and end in Congress, and public perception is either a mere adjunct to the process or a handy and easily manipulable rationalization of congressional action. Breyer fails to consider this possibility.

After Congress has acted, the vicious circle rolls into the realm of the regulatory agencies. In Breyer's view, the inherent uncertainty in the technical aspects of substantive regulation provides the last element of the vicious circle.[28] Different agencies (and even different departments within the same agency) approach similar problems from different directions leading to the formulation of inconsistent policies.

In part, uncertainty and inconsistency are a function of the many different disciplines that can be brought to bear on a particular problem. As an example, Breyer cites the enormously complex task of assessing a hazardous waste site: "A waste site evaluation . . . may require knowledge of toxicology, epidemiology, meteorology, hydrology, engineering, public health, transportation and civil defense, disciplines with different histories, different methods of proceeding, and different basic assumptions."[29] Different agencies, with different missions and different personnel who have jurisdiction over the same matter are bound to have different perspectives on the problem and prescribe different courses of action.

Unfortunately, Congress and the public are looking for *the* solution—not a range of possible approaches to the problem.

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[27] For example, when Congress passed Truth-in-Savings legislation, the bill's chief sponsor, Rep. Lehman, admitted that the impetus for the bill was a personal reaction to what he perceived to be a misleading advertisement. Gouvin, *supra* note 26, at 1321 n.160.

[28] BREYER, *supra* note 2, at 42–50.

[29] *Id.* at 43.

Asking regulators to establish *the* solution to a problem, however, is somewhat unrealistic. Because the "solution" depends to a great extent on the theoretical lens one chooses to look through, different regulators looking at the same phenomenon through different lenses will make inconsistent policy. Those inconsistent policies, while based on theoretically sound premises, will tend to suggest to the public and Congress that the regulators are hopelessly muddled and do not know how to respond to the problem.

While different theoretical approaches to similar problems cause some inconsistency in the regulatory process, other technical matters also play a role in making the regulatory scheme appear irrational. For example, all regulators must take action without complete information. In the face of incomplete information, regulators must rely on assumptions. Assumptions do not always derive from scientific principles, but might result from political considerations.[30] Reliance on conflicting assumptions causes different agencies to reach different conclusions and produce a regulatory scheme that appears irrational. As an obvious example, an agency guided by the principle that all policy should "err on the safe side" will almost always reach a different conclusion from an agency that scrutinizes the bottom line for demonstrable "cost effectiveness."

These three elements—public perception, congressional action, and technical uncertainty—make up Breyer's vicious circle. The vicious circle creates the systemic problems that plague it: tunnel vision, irrational agendas, and inconsistency. The elements of the vicious circle reinforce each other and lead to public distrust of the regulatory process, which results in greater political oversight, which aggravates the random agenda problem and in turn creates more inconsistent outcomes. Taken as a whole, the regulatory process undermines its own legitimacy.[31] While Breyer's treatment of the interrelation of the systemic problems and the elements of the vicious circle is somewhat sketchy,[32] the overall scheme nevertheless appears intuitively attractive and commonsensical.[33]

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[30] *Id.* at 49.

[31] *Id.* at 50–51.

[32] *Id.* In Justice Breyer's defense, the book was derived from a series of lectures, so one might expect a certain degree of brevity.

[33] While Justice Breyer's observations are anecdotal, many of the problems he identifies have also been identified by the National Performance Review after intensive

II. JUSTICE BREYER'S SOLUTION

Justice Breyer's proposal for breaking the vicious circle focuses on the behavior of regulatory agencies. He targets the agencies because, in his words, "any practical, institutionally oriented solution must also take account of the extreme difficulty of changing human psychology, press reactions, or Congressional politics."[34] Apparently, he sees the regulatory agencies as being somewhat amenable to change, and suggests structural modifications in the way regulations are developed that will help bring about "self-reinforcing institutional change, which will gradually build confidence in the regulatory system."[35]

To break the vicious circle, Justice Breyer proposes the creation of an elite, politically insulated group of "super-regulators" within the executive branch. These super-regulators would be given interagency jurisdiction and the authority to implement substantive changes with the aim of achieving the "mission of building an improved, coherent [regulatory scheme] . . . ; of helping to create priorities within as well as among programs; and . . . [of] comparing programs to determine how better to allocate resources . . . ."[36] The super-regulators chosen to carry out this function would be drawn from a new, special, prestigious civil service career path. They would be groomed for this service by rotation through assignments on Capitol Hill, the administrative agencies, and the Office of Management and Budget (OMB).[37]

Although Breyer does not see these structural changes as a cure-all for the regulatory woes he describes in his book, he does believe the proposal represents a "constructive approach."[38] If the goal is to make regulation better, as opposed to making it "right," Breyer's approach has great appeal.

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field work, research, and interviews. *See generally* Jeffrey S. Lubbers, *Better Regulations: The National Performance Review's Regulatory Reform Recommendations*, 1994 DUKE L.J. 1165 (1994).

[34] BREYER, *supra* note 2, at 55 (citation omitted).

[35] *Id.*

[36] *Id.* at 60–61. *See also* Robert A. Katzmann, *Wayne Morse Forum, November 10, 1992: Have We Lost the Ability to Govern? The Challenge of Making Public Policy*, 72 OR. L. REV. 231, 240 (1993) (making a similar suggestion for the creation of a function within the Office of Management and Budget to resolve conflicts and establish priorities among various policies).

[37] *Id.* at 59–60.

[38] *Id.* at 59.

While the creation of an elite institutional body within the federal government with the authority to set regulatory policy priorities and allocate resources accordingly would be a new approach (especially during peacetime),[39] the idea has a distinguished pedigree. Breyer's idea may first remind one of Plato's *Republic*, in which an elite group of philosophers are specially groomed to govern.[40] In Breyer's scheme, however, the guardians must share political power with Congress, so it is not quite as undemocratic as the republic envisioned by Plato.

More recently, John Stuart Mill suggested that technical rules, be they laws or regulations, ought to be made by persons with special understanding and expertise.[41] Mill proposed a "Commission on Legislation" that would assist Parliament in making public policy.[42] In the early twentieth century, Woodrow Wilson proposed the creation of institutional structures to move public policy out of Congress and into a body that could act more rationally.[43] Even more recently, Professor Cass Sunstein has recommended the creation of such a body in either the legislative or executive branches to coordinate and rationalize regulation.[44]

Not only has this idea been proposed before, it has been implemented to some degree. In France, for example, the Conseil d'Etat performs a function in the coordination of agency work which is similar to the role Breyer foresees for the super-regulators.[45] In fact, even in this country Breyer's proposal is no longer strictly theoretical since the National Performance Review has endorsed, and President Clinton has implemented, a Regulatory Working Group to be chaired by an OMB administrator.[46]

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[39] During World War I and World War II, the federal government exercised general control over economic resource allocation and production priorities. *See generally* DAVID BRINKLEY, WASHINGTON GOES TO WAR 50–82 (1988).

[40] PLATO, THE REPUBLIC OF PLATO (Allan Bloom trans., 1968).

[41] JOHN STUART MILL, CONSIDERATIONS ON REPRESENTATIVE GOVERNMENT 237–39 (H.B. Acton ed., 1972) (1861).

[42] *Id.*

[43] *See* Lawrence Lessig & Cass R. Sunstein, *The President and the Administration*, 94 COLUM. L. REV. 1, 45 (1994) (providing an historical inquiry into the respective roles of Congress, the executive branch and the administrative agencies).

[44] CASS R. SUNSTEIN, AFTER THE RIGHTS REVOLUTION: RECONCEIVING THE REGULATORY STATE 108 (1990).

[45] BREYER, *supra* note 2, at 70–71.

[46] Lubbers, *supra* note 33, at 1170.

III. CRITICISMS OF THE PROPOSAL

Justice Breyer does not pretend that his proposal is a panacea that will correct all of the ills facing the regulatory process.[47] Even with that disclaimer, his proposal raises at least four serious concerns that call its value into question: it ignores the body of work developed by public choice scholars; it transplants existing problems; it accepts pervasive regulation without seriously considering deregulation as an alternative; and it attempts to correct the regulatory problem too late in the process.

A. *Public Choice*

The coherence and intuitive appeal of Justice Breyer's proposal rest on the unstated assumption that regulators serve the public interest.[48] Justice Breyer seems to adopt a neo-republican outlook in which civic-minded public servants act in the public interest. However, not everyone shares his optimism that government actors, no matter how "elite," will be immune to the forces described in the public choice literature.[49]

Implicit in the book's approach to the subject is the idea that the regulatory scheme is broken but fixable or, in other words, the incoherent results produced by the system are avoidable. Public choice scholars, on the other hand, contend that the whole exercise is doomed to produce incoherent results regardless of the structure of the process.[50] While arguing that the system has

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[47] BREYER, *supra* note 2, at 59.

[48] Breyer indirectly suggests this idea when he assumes that his scheme will be adopted by a government composed of "honest, talented, and qualified" regulators. *Id.* at 59.

[49] Jonathan Macey, for example, would likely find that Breyer's formula misses "an appreciation of the frightening power of man to subvert the offices of government for what can only be described as evil ends." Jonathan R. Macey, *The Missing Element in the Republican Revival*, 97 YALE L.J. 1673 (1988).

[50] Summarizing the public choice literature in a footnote is a task doomed to failure. The scholars who make up the public choice school are a somewhat loosely knit group. Their perspectives on the law draw heavily on economics, game theory, organizational behavior and political science. *See* FARBER & FRICKEY, *supra* note 12, at 21–33; Jerry L. Mashaw, *The Economics of Politics and the Understanding of Public Law*, 65 CHI.-KENT L. REV. 123, 143 (1989); *see generally,* Daniel A. Farber & Philip P. Frickey, *The Jurisprudence of Public Choice*, 65 TEX. L. REV. 873, 878–79, 883, 901–06 (1987) (stating a general theory of "public choice" is impossible, since there are many variations on the set of core principles that have inspired many of the scholars). As a general proposition, however, a public choice scholar is likely to see statutes and regulations as products that are bought and sold in economic markets. For an overview, see Robert D. Tollison, *Public Choice and Legislation*, 74 VA. L. REV.

reached its current state because of the bureaucratic failure to make rational policy analysis, Justice Breyer makes no attempt to address any anticipated criticisms from the public choice school.[51] He completely ignores the possibility that the system has evolved into its current state as a result of an intricate web of deals, concessions and paybacks bought and sold in the legislative marketplace by interested actors. Others have eloquently attacked the public choice position.[52] Justice Breyer weakens his proposal by not adding his voice to the chorus.

B. *Transplantation of Problems*

Justice Breyer believes his proposal has appeal because it draws upon the "virtues of bureaucracy" and builds on what he sees as the traditional strengths of administrative agencies—essentially, their ability to rationalize policy, expertise and political insulation, combined with their authority to carry out the

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339 (1988). A significant school of thought within the movement owes much to the work of Kenneth Arrow, who developed the famous theorem that bears his name. Arrow's Theorem holds that under certain conditions it is impossible to aggregate the preferences of a given group because the way in which voting is conducted could result in an infinite cycling of choices. For a useful summary of Arrow's Theorem and its larger implications, see HEAP, *supra* note 12, at 209–15. Given the theoretical problems of aggregating preferences, the output of collective bodies tends to be incoherent.

[51] Breyer's earlier important book on regulatory reform was also criticized for ignoring the perspectives of the public choice literature. Ernest Gellhorn, *Rationalizing Regulatory Reform*, 81 MICH. L. REV. 1033, 1036–37 (1983) (reviewing BREYER, REGULATION, *supra* note 1.

[52] Scholars have attacked the public choice position on the grounds that it lacks empirical support. *See, e.g.*, Janet M. Grenzke, *PACs and the Congressional Supermarket: The Currency is Complex*, 33 AM. J. POL. SCI. 1 (1989) *reprinted in* THE CONGRESS OF THE UNITED STATES, 1789–1989, vol. 8, 689 (Joel Silbey ed., 1991); Mark Kelman, *On Democracy-Bashing: A Skeptical Look at the Theoretical and "Empirical" Practice of the Public Choice Movement*, 74 VA. L. REV. 199, 236–68 (1988). Other scholars have criticized the methodology of the public choice approach for failing to give weight to legitimate concerns about the public interest that legislators may have and instead constructing an *ex post* explanation for legislative behavior based on who benefitted from the legislation. *See, e.g.*, Donald C. Langevoort, *Statutory Obsolescence and the Judicial Process: The Revisionist Role of the Courts in Federal Banking Regulation*, 85 MICH. L. REV. 672, 692 (1987); Edward L. Rubin, *Beyond Public Choice: Comprehensive Rationality in the Writing and Reading of Statutes*, 66 N.Y.U. L. REV. 1, 5–30 (1992). In addition, many scholars have questioned whether a world view dominated by interest groups and excluding higher values runs the risk of becoming morally impoverished and ultimately politically illegitimate. *See, e.g.*, Farber & Frickey, *supra* note 50, at 906–07; Daniel A. Farber, *Democracy and Disgust: Reflections on Public Choice*, 65 CHI.-KENT L. REV. 161 (1989); Geoffrey Brennan & James M. Buchanan, *Is Public Choice Immoral? The Case for the "Nobel" Lie*, 74 VA. L. REV. 179, 180 (1988) (describing this criticism).

policy.[53] Ironically, Breyer's reliance on the system's perceived strengths prevents his proposal from escaping the system's fundamental problems. These systemic flaws will merely manifest themselves in a different forum.

1. Rationalization

Hopes for a coherently rationalized regulatory scheme may prove difficult to realize. As Breyer himself points out, the EPA, which has a single head, sometimes ends up working at cross-purposes with itself.[54] Although agency heads are unable to rationalize their own agency's agenda, Breyer believes the new cadre of super-regulators will be able to draft a specific regulatory agenda for *all* agencies with little difficulty. Breyer contends the super-regulators will rationalize the agenda partly by "mak[ing] explicit, and more uniform, controversial assumptions that agencies now, implicitly and often inconsistently, use in reaching their decisions."[55]

While such a rationalization scheme might be possible, it will only be accomplished if agencies defer to the particular theoretical position held by the super-regulator. This rationalization will not harmonize the different perspectives; rather, it will choose one perspective over another. By necessity, the super-regulators will have to adopt some theoretical point of view when analyzing regulatory issues. For instance, by taking the point of view of an economist over the point of view of an environmentalist, the super-regulators will produce different substantive regulations and agendas for regulatory action. However, the underlying normative foundations of the economist and the environmentalist are fundamentally different and incommensurable. Asking the super-regulator to reconcile them and come up with "the" solution to a particular regulatory problem is impossible because the different values of these disparate disciplines cannot be judged by a common measure.[56] Any solution the regulator reaches will

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[53] BREYER, *supra* note 2, at 61–63.

[54] *See supra* notes 15–18 and accompanying text; BREYER, *supra* note 2, at 22.

[55] BREYER, *supra* note 2, at 64–65.

[56] For a discussion of the myriad problems involved in attempting to deal with conflicting values in the law, see Cass R. Sunstein, *Incommensurability and Valuation in Law*, 92 MICH. L. REV. 779 (1994).

necessarily be informed by a world view that embraces some values and rejects others.

The result will be a consistent agenda, but it may be an agenda that fails to support the particular missions of particular agencies. When agencies charged with protecting the environment, for instance, are seen as failing to advocate the position of their "clients," political consequences will follow. In addition, the consistency provided by the super-regulator will last only as long as the super-regulator holds her post. When the regulators change, the agency's values will change along with its underlying substantive policies. The impermanent nature of super-regulators' tenure may not be entirely unappealing since policy changes at least will be made by someone intimately familiar with the entire regulatory scheme. Even so, the scheme is a far cry from the happy situation Justice Breyer envisions.

2. Expertise

The expertise argument in favor of administrative agency authority has paled in light of attacks that agencies are not especially expert. The idea of an all-knowing expert who can objectively perform a rational assessment and produce an objectively "right" answer seems somewhat naive.[57] On the other hand, if Breyer's super-regulator idea could be implemented, it certainly would create a group of experts who know not only the substantive regulations, but also the workings of the various branches of government. Such a group of knowledgeable career civil servants could be a valuable resource for writing more intelligent regulations.

By utilizing experts in the creation of the regulatory product, Justice Breyer's proposal has been heralded as a possible way to incorporate "total quality management" ideas from industry into the design of government regulation.[58] The creation of a highly trained and respected group of professional super-regulators could go a long way toward injecting quality into the regulatory

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[57] *See* THOMAS O. MCGARITY, REINVENTING RATIONALITY: THE ROLE OF REGULATORY ANALYSIS IN THE FEDERAL BUREAUCRACY at xvi (1991) (observing that "data analysis is expensive, cost and benefit assessment models are inaccurate, biases can subtly creep into 'objective' analyses, and the uncertainties are sometimes so huge and pervasive as to render the idea of objectivity virtually meaningless").

[58] Paul R. Verkuil, *Reverse Yardstick Competition: A New Deal for the Nineties*, 45 FLA. L. REV. 1, 16 (1993).

design process, representing a vast improvement over the current practice of checking for quality after the fact.[59] Just as industry has found that after-the-fact quality checks are a poor way to insure a quality product, government attempts at after-the-fact quality control—such as sunset provisions, law revision commissions, judicial review and congressional oversight—have met with poor results.[60]

Yet experts are not immune to sloppy thinking, zealotry, or incompetence. Even a super-regulator could fall victim to the "last 10% problem," especially if, as contemplated by Justice Breyer, the super-regulator's entire professional experience is in government and has not been tempered by the realities of industry. Perhaps the super-regulator career path should require a stint in the private sector instead of allowing a regulator to rule supreme with only inside-the-beltway experience to inform her world view. Without a reality check, a super-regulator produced in accordance with Breyer's new career path might nevertheless be the kind of regulatory zealot who spends $1,000 to get a $1 benefit.

In addition, expert regulators might nevertheless be susceptible to the same analytical infirmities as mere mortals. While Breyer correctly points out that "framing effects" often cause the general public to make poor decisions,[61] he fails to note that research has found that framing effects warp the judgments of highly educated professional decisionmakers as well.[62] Framing effects have been called the linguistic or logical equivalent of optical illusions because they make the perceiver see something

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[59] *See* E. Donald Elliott, *TQM-ing OMB: Or Why Regulatory Review Under Executive Order 12,291 Works Poorly and What President Clinton Should Do about It*, 57 LAW & CONTEMP. PROBS. 167 (1994) (advocating changes in the regulatory review process that would incorporate "total quality management" concepts from industry and focus regulatory review efforts on the beginning, not the end, of the agency rule-making process). Ultimately, the process would create knowledgeable agency bureaucrats who would be able substantially to internalize the regulatory review regime.

[60] Breyer's earlier work reveals his lack of faith in post-enactment review to bring about meaningful reform of regulation. BREYER, REGULATION, *supra* note 1, at 365–66. For a general discussion of several methods of post-enactment review and their shortcomings, see Gouvin, *supra* note 26, at 1364–70.

[61] The way in which a question is asked often influences the answer that will be given. This is called the framing effect. Breyer analyzes framing effects as a subset of mathematics anxiety, but it reaches beyond math problems. BREYER, *supra* note 2, at 36–37.

[62] *See* HEAP, *supra* note 12, at 39–40 (describing a famous framing effects experiment on the choice of treatment regimes for cancer patients and finding that both patients *and their doctors* made the same analytical mistakes based on framing effects).

that is not there.[63] Putting an expert in the role of decisionmaker does not make these effects go away.

Similarly, while Breyer points out that the general public can become befuddled by expert opinions,[64] he offers no evidence that expert decision-makers are not likewise subject to the same confusion. As anyone who has ever had to arrange for expert witnesses in a trial knows, there are experts on both sides of every issue. The experts can apply acceptable research techniques to a given problem and come up with very different conclusions and recommendations. In the end, someone has to choose between two supportable positions. There is no way for an expert decisionmaker to know if one consulting expert is "right" and the other "wrong" in any meaningful sense.[65]

3. Political Insulation

In his previous work, one of Breyer's great strengths was his realistic understanding of political forces and the role they play in any congressional action.[66] In *Breaking the Vicious Circle*, however, Breyer's political antennae seem less finely tuned. His proposal for a super-regulator clearly invites criticism that it is undemocratic, elitist and otherwise politically unacceptable. Although Breyer briefly responds to each of these anticipated criticisms, he does so somewhat cryptically.[67] The book needs a stronger defense of its position against those who maintain that Congress has already delegated too much authority to agencies without sufficient accountability.[68] Breyer could have written such a defense since the way the proposal provides for political insulation is its greatest strength. Insulation could allow the super-regulators to make decisions that politically accountable authorities never would be able to pull off. In fact, Congress has resorted

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[63] Richard L. Hasen, Comment, *Efficiency Under Informational Asymmetry: The Effect of Framing on Legal Rules*, 38 UCLA L. REV. 391, 399 (1990).

[64] BREYER, *supra* note 2, at 36.

[65] The public debate over disposable diapers provides an excellent example of the battle of experts in the public policy arena. *See* Cynthia Crossen, *How 'Tactical Research' Muddied Diaper Debate*, WALL ST. J., May 17, 1994, at B1.

[66] Louis B. Schwartz, Book Review, 35 HASTINGS L.J. 233, 237 (1983) (reviewing BREYER, REGULATION, *supra* note 1).

[67] BREYER, *supra* note 2, at 72–79.

[68] *See, e.g.*, DAVID SCHOENBROD, POWER WITHOUT RESPONSIBILITY (1993); *but cf.* Peter L. Strauss, *Legislative Theory and the Rule of Law: Some Comments on Rubin*, 89 COLUM. L. REV. 427 (1989).

to such undemocratic methods in the past precisely to break the stranglehold of political forces.[69]

Unfortunately, the benefits of depoliticization come with a serious cost. If the regulatory process is not completely depoliticized, then some actors will continue to have access to the process and shape it to their needs while others will be locked out. The prospect that super-regulators will be truly insulated from politics is remote. Breyer himself does not believe appointments that touch the political process can ever escape the taint of politics. For example, in *Regulation and Its Reform* he recognized the inherently political nature of the appointments process and the generally negative effects it has on the quality of regulation.[70] Although Breyer's super-regulators will be career civil servants and therefore less susceptible to political forces than appointees, they nevertheless will be buffeted by political forces. In the end, some argue, if the process cannot be completely and evenly depoliticized, it perhaps should not be depoliticized at all.[71]

4. Authority

Even with a super-regulator, the laws passed by Congress will remain the law of the land. If a super-regulator identifies an inconsistency between the law as written and the perceived risk it addresses (in the terms of Breyer's earlier writings, a regulatory "mismatch"), the regulator nevertheless will be bound by the law. Only Congress can weed out the inconsistent statutes and implement sufficiently flexible laws that would allow a super-regulator to reach his full potential. Relying on Congress to pass such laws, however, dooms the project to failure. Congress struggles to deal with even relatively simple problems in a rational, coherent manner.[72] If the regulatory scheme is so dis-

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[69] Warren Weaver, Jr., *New Panel Asked on Social Security*, N.Y. TIMES, Sept. 7, 1981, at A8; *see*, Michael A. Fitts, *Can Ignorance Be Bliss? Imperfect Information as a Positive Influence in Political Institutions*, 88 MICH. L. REV. 917, 952–53 (1990) (suggesting that the success of the Defense Base Closure and Realignment Commission and other *ad hoc* national commissions has been due, at least in part, to the fact that the commission structure allows the creation of an informal bargaining mechanism outside of the public eye). As another example, Congress effectively foreclosed unmitigated political bickering over Social Security reform in the early 1980s by forming the National Commission on Social Security Reform.

[70] BREYER, REGULATION, *supra* note 1, at 343–45.

[71] David A. Dana, *Setting Environmental Priorities: The Promise of a Bureaucratic Solution*, 74 B.U. L. REV. 365, 373–85 (1994) (reviewing BREYER, *supra* note 2).

[72] *See* Gouvin, *supra* note 26 (analyzing Congress' failure to address the problems raised by the proponents of Truth-in-Savings legislation).

jointed and confused as to require an apolitical super-regulator to straighten it out, the legislative enactments necessary to implement that scheme will also be fraught with political deals and brinksmanship.

C. *Failure to Consider Alternatives*

Despite his earlier passion for designing a regulatory system that consciously analyzes available alternatives,[73] Justice Breyer seems to discard them completely in his current proposal. He seems to assume the underlying necessity for regulation and pays short shrift to the idea of deregulation. This position comes as somewhat of a surprise given Breyer's eloquent discussion of deregulation of the airline industry in *Regulation and Its Reform.* There, he was skeptical of the idea that regulation was the best response for every problem.[74] At that time Breyer believed that "classical regulation ought to be looked upon as a weapon of last resort,"[75] and should be used only where less restrictive methods will not work.[76]

Breaking the Vicious Circle, on the other hand, seems to accept the inevitability of a pervasive regulatory scheme—at least for hazardous substances regulation. Breyer simply dismisses deregulation in one paragraph, labelling it a "non-solution."[77] In doing so, Breyer chooses to ignore innovative programs for the regulation of hazardous wastes adopted in Texas and other states that scale back the government's role and incorporate a significant measure of industry self-regulation.[78] More generally, some scholars have convincingly argued that private actors can be regulated in the most responsive and flexible manner by creating incentives for these actors to comply with federal regulations voluntarily, and that this method should be employed in

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[73] *See* BREYER, REGULATION, *supra* note 1, at 156–83.

[74] "Too often arguments made in favor of governmental regulation assume that regulation, at least in principle, is a perfect solution to any perceived problem with the unregulated marketplace." *Id.* at 5 (footnote omitted).

[75] *Id.* at 185.

[76] *Id.*

[77] BREYER, *supra* note 2, at 56.

[78] *See* Mary Lenz, *Environmentalists, Industry Both Praise Water Panel Chief*, HOUSTON POST, May 18, 1992, at A9; *Governor Announces Cleanup Plan, Program Aims to Cut State Pollution In Half*, HOUSTON POST, Apr. 8, 1992, at A22 (describing the Clean Texas 2000 program).

more situations.[79] Congress certainly appears to be listening to the voices calling for more flexible regulation.[80]

D. *Too Little, Too Late*

Although Justice Breyer's prescription correctly identifies the structure of the regulatory process as the problem, the primary defect in his approach is that it does not go to the root of the problem. Unfortunately, he ultimately concludes that the systemic problems may be meaningfully addressed by tinkering with the existing OMB review process.[81] While the structure of this process clearly contributes to the problems of effective regulation, by the time the regulatory mess reaches OMB, it has already proceeded too far down the wrong track. Any hope for effective regulatory reform depends on pushing the review process back to the inception of the legislative idea that gives rise to the regulatory scheme.[82] A system that encourages Congress to get legislation "right" in the first place makes more sense than a system where regulatory mandarins are charged with rationalizing inconsistent congressional directives.

In this regard, the "high noon" structural reform proposed by Justice Breyer in *Regulation and Its Reform* makes more sense and would get the regulatory process off to a better start.[83] Under that approach, executive branch commissions would be charged with the task of studying specific regulatory programs and reporting findings within a specified time-table. The commissions would have to undertake a broad review of the programs in light of other less restrictive alternatives. The recommendations of the executive commissions would then go to Congress, where the appropriate committees would consider them. If the congressional committees did not act on the recommendations within one year, the recommendation would automatically come up for

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[79] IAN AYRES & JOHN BRAITHWAITE, RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE 101–32 (1992); CHARLES L. SCHULTZE, THE PUBLIC USE OF PRIVATE INTEREST 13 (1977).

[80] *See* Craig Gannett, *Congress and the Reform of Risk Regulation*, 107 HARV. L. REV. 2095, 2100–01 (1994) (reviewing BREYER, *supra* note 2) (citing Congress's passage of the Clean Air Act amendments in 1990 as evidence of a willingness to use new "regulatory tools informed by economics and sensitive to costs and benefits").

[81] BREYER, *supra* note 2, at 71–72.

[82] For a general discussion of ways in which the legislative process might be modified to provide a feedback loop that would improve the quality of legislation, see Gouvin, *supra* note 26, at 1353–75.

[83] BREYER, REGULATION, *supra* note 1, at 366.

a vote on the floor of each house of Congress. By starting the review process with a deliberate and thoughtful study, the high noon idea would encourage informed decisionmaking based on a coherent agenda—assuming the executive branch could put together such a thing. The adherence to strict timetables would tend to overcome legislative inertia.[84]

If Breyer's high noon idea falls short, others have recommended ways to make the legislative process more amenable to the promulgation of effective, rational and coherent laws. For instance, Professor Edward Rubin has suggested that Congress prevent members and staff from drafting statutory language until the issues and goals supposed to be addressed by the legislation have been identified with some specificity.[85]

On a different tack, Professor Robert Seidman has suggested putting additional responsibilities on legislative drafters to justify their proposed bills with a comprehensive legislative memorandum. The memorandum would have to analyze the problem at which the legislation is aimed and show why the proposed solution is the best solution.[86]

Finally, I have suggested the creation of an Office of Public Policy that would bring together existing policy analysis resources in the Congress, such as the Congressional Research Service, General Accounting Office, Office of Technology Assessment and the Congressional Budget Office, and extend those analytical services to all important legislation. The Office of Public Policy would do nothing more than consciously identify the issues and the alternative approaches available for action. Adoption of a given course of action would remain a political decision for Congress.[87]

Any one of these pre-enactment reforms likely will do more to improve the regulatory product than the post-enactment dam-

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[84] The high noon idea received mixed reviews from legal commentators. *See* Lloyd N. Cutler, *Regulatory Mismatch and Its Cure*, 96 HARV. L. REV. 545, 553 (1982) (reviewing BREYER, REGULATION, *supra* note 1); Ernest Gellhorn, *Rationalizing Regulatory Reform*, 81 MICH. L. REV. 1033, 1038 (1983) (reviewing BREYER, REGULATION, *supra* note 1) (criticizing the idea); *see also* Louis B. Schwartz, Book Review, 35 HASTINGS L.J. 233, 235 (1983) (reviewing BREYER, REGULATION, *supra* note 1) (discussing the idea in generally positive terms).

[85] Rubin, *supra* note 26.

[86] Robert B. Seidman, *Justifying Legislation: A Pragmatic, Institutionalist Approach to the Memorandum of Law, Legislative Theory, and Practical Reason*, 29 HARV. J. ON LEGIS. 1 (1992).

[87] Gouvin, *supra* note 26, at 1371–75.

age control proposed by Justice Breyer. While he senses that changing the congressional legislative process is difficult, he must recognize that it is not impossible. His proposal instead calls for Congress to relinquish some amount of power to an unaccountable super-regulator—a situation to which Congress certainly will not accede without a struggle. On the other hand, proposals like the three just discussed that change the legislative process within Congress but keep political power in that institution seem easier to implement.

IV. Conclusion

Justice Breyer's proposal is undeniably thought-provoking. His book's most significant contribution may be to draw attention to the current regulatory regime's systemic problems, thereby encouraging serious discussion about how to "reinvent" the regulatory process. Breyer courageously points out that the political legitimacy of the process rests to some degree on the effectiveness of its product. Nonetheless, his proposal for correcting the problems he perceives will not likely win universal acceptance. At its core, however, Breyer's proposal contains a crucial insight that must be fully recognized: the current regulatory structure contains built-in flaws that contribute to a poor result, and the structure must be changed to correct, or at least ameliorate, those flaws. Although many will disagree with Justice Breyer's prescription, many more will concur in his message that the system needs fixing.

NOTE

CURING CRIB DEATH: EMERGING GROWTH COMPANIES, NUISANCE SUITS, AND CONGRESSIONAL PROPOSALS FOR SECURITIES LITIGATION REFORM

ANTHONY Q. FLETCHER*

With the advent of the Republican-controlled 104th Congress, it is apparent that the movement to stem the tide of securities class action suits waged against emerging growth companies[1] has at last attained the political consensus necessary for reform.[2] Indeed, a host of securities litigation reform measures have been introduced in the 104th Congress that would effectively eliminate many of the abuses of class action securities litigation, while indirectly protecting emerging growth companies from the imminent "crib death"[3] so often the result of nuisance

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[1] Emerging growth companies, also commonly referred to as emerging companies, are companies involved in high-technology fields such as computers, semi-conductors, biotechnology, robotics, and electronics. Typically, emerging growth companies have above-average earnings growth and therefore volatile stock prices. DICTIONARY OF FINANCE AND INVESTMENT TERMS 186 (3d ed. 1985).

[2] *See, e.g.*, Bruce Rubenstein, *Cease and Desist*, CORP. LEGAL TIMES, Sept. 1994, at 1 (reporting that a coalition of hundreds of publicly held companies, the "Big Six" accounting firms, and securities underwriters, have all combined under the name Committee to Eliminate Abusive Securities Suits (CEASE) to lobby for securities litigation reform); *Business Groups Urge Congress to Vote Yes on Securities Litigation Reform*, PR Newswire, Mar. 7, 1995, *available in* LEXIS, NEWS Library, CURNWS File. *Securities Litigation Revisions: Hearings Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs*, 104th Cong., 1st Sess. (1995) (statement of Arthur Levitt, chairman, Securities and Exchange Commission) (advocating private securities litigation reform). *But see* Steven A. Holmes, *Clinton Defines The Limits Of Compromise With G.O.P.; Gingrich Urges 'Dialogue'*, N.Y. TIMES, Apr. 8, 1995, at A1 (reporting President Clinton's resolve to reject House-passed legal reform bills). *See generally Witnesses, Lawmakers Debate Need for Securities Litigation Reforms*, 26 SEC. REG. & LAW REP. 1120 (1994); Neil A. Lewis, *House Passes Bill That Would Limit Suits Of Investors*, N.Y. TIMES, Mar. 9, 1995, at A1; Steven Budiansky et al., *How Lawyers Abuse the Law*, U.S. NEWS & WORLD REP., Jan. 30, 1995, at 52 (surveying Americans' negative views on lawyers and the civil justice system).

[3] "Crib death" is the term I use to describe the premature demise of an emerging growth company. The early period of an emerging growth company is generally characterized by a conscientious and concerted effort to raise venture capital, and is marked by the complex business decisions associated with start-up companies, such as private placement, offerings, recruiting experienced officers and directors, creating

suits.[4]

I. THE PROBLEM

Due in large part to the unique volatility of their stock on the public securities exchanges,[5] emerging growth companies are subject to a disproportionate share of securities class action suits.[6] In fact, emerging growth companies now face a volume of class action shareholder suits comparable to the volume that once plagued large, established companies.[7] A recent study of 212

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consumer markets, and eventually going public. Severe financial loss at any stage in the early development of an emerging growth company (even several years beyond the public offering of securities) may result in "crib death." *See, e.g.*, Diana B. Henriques, *House Panel Approves Shifts On Securities Fraud Suits*, N.Y. TIMES, Feb. 17, 1995, at D1 (noting that the securities litigation reform movement is supported by key members of the business and financial community who are concerned that frivolous securities class action lawsuits impede small companies from raising capital). *See also* Jack Sweeney, *Busy Plaintiffs Keep Silicon Valley on Edge*, COMPUTER RESELLER NEWS, Nov. 28, 1994, at 1; Julie Triedman, *Class Warfare*, CORP. COUNS., July-Aug. 1994, at 51. Emerging growth companies at risk of "crib death" are concentrated in the areas of genetic engineering, computers, and telecommunications. *See* Kathleen Day, *When Shareholders Sue*, WASH. POST, Jan. 31, 1994, at E1.

[4] Nuisance suits, also referred to as "frivolous" suits or "strike" suits, are suits in which a plaintiff sues hoping to force the defendant to settle rather than incur the costs of litigation, despite the defendant's awareness that the plaintiff's case is weak. Thus, a nuisance suit is an action in which the settlement value stands independent of the merits of the claim. *See, e.g.*, David M. Rosenberg & Steven M. Shavell, *A Model in Which Suits Are Brought for Their Nuisance Value*, 5 INT'L REV. L. & ECON. 3 (1985); John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law through Class and Derivative Actions*, 86 COLUM. L. REV. 669 (1986). *See also* William C. Baskin III, Note, *Using Rule 9(b) to Reduce Nuisance Securities Litigation*, 99 YALE L.J. 1591 (1990).

[5] *See, e.g.*, Udayan Gupta & Brent Bowers, *Small Fast-Growth Firms Feel Chill of Shareholder Suits*, WALL ST. J., Apr. 5, 1994, at B2 (noting that the inherent unpredictability of the stock performance of small high-technology companies prompts class action shareholder suits).

[6] *See* Carolyn Lochhead, *Shareholder Lawsuits Defended by Lawyer at House Hearing*, S.F. CHRON., Jan. 20, 1995, at A4 (reporting that one of every four high-technology companies has been charged in a shareholder class action suit and has paid out $440 million to settle "strike suits" over the last two years); Brent Bowers & Udayan Gupta, *Shareholder Suits Beset More Small Companies*, WALL ST. J., Mar. 9, 1994, at B1 (suggesting that lawyers deliberately target small companies for class action shareholder suits because these companies are more likely to show "big swings" in their stock prices); *See also* Paul Sweeney, *Full Siege Ahead: Class-Action Lawsuits*, ACROSS THE BOARD, Nov. 1994, at 30 ("Companies are vulnerable even when they suffer a momentary drop in stock price; some say that a 10 percent loss share price is the trigger . . . ."); *see generally* FREDERICK C. DUNBAR & VINITA M. JUNEJA, NATIONAL ECONOMIC RESEARCH ASSOCIATES, INC., RECENT TRENDS II: WHAT EXPLAINS SETTLEMENTS IN SHAREHOLDER CLASS ACTIONS? (1993).

[7] *See* Ross Kerber, *Shareholder Suits Prompt Reform Push; Company Officials Seek Laws to Limit Their Vulnerability*, WASH. POST, Aug. 8, 1993, at H1 (reporting that after declining during the late 1980s, shareholder class action claims, often against high-technology companies, have nearly tripled since 1988). *See also* Wade Lambert,

venture-backed firms that had been in operation since 1986 found that one in six had been sued at least once.[8] The same study also found that these firms had spent, on average, $692,000 in legal fees and approximately 1055 hours of management time per case defending class action shareholder suits.[9] As a result of this high incidence of litigation, many emerging growth companies have witnessed a significant rise in their Directors and Officers (D&O) liability insurance premiums[10] and have also experienced increased difficulty in recruiting and retaining outside directors.[11]

Class action shareholder suits impose costs on emerging growth companies that have adverse consequences not only for the development of new markets but also for economic recovery. Empirical data evinces that the confidence of venture capitalists in the securities markets is critical to the overall health and stability of the economy.[12] For example, the employment rate of companies backed by venture capital increased by an average of nineteen percent a year during the course of the last recession,[13] while Fortune 500 companies experienced an increase in lay-

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Corporate Settlement Costs Hit a Record, WALL ST. J., Mar. 10, 1995, at B3 (reporting a sharper increase in lawsuits against officers and directors of small companies, particularly high-technology companies, than against larger corporations).

[8] VENTUREONE, THE IMPACT OF SECURITIES FRAUD SUITS ON ENTREPRENEURIAL COMPANIES 1 (1994).

[9] *Id.*

[10] *See* THE WYATT COMPANY, 1994 WYATT DIRECTORS AND OFFICERS LIABILITY SURVEY 25 (1994) (concluding that in 1994 high-technology companies recorded the largest increases in D&O premiums, with typical increases exceeding 50%). The VentureOne study found that over 60% of the venture-backed companies surveyed experienced an increase in their D&O insurance. VENTUREONE, *supra* note 8, at 1. The time period surveyed covered the time of the venture-backed company's initial insurance policy date to the date of the survey, November 15, 1993. Telephone Interview with Russell Snipes, principal, VentureOne Corporation (Apr. 24, 1995).

[11] Thirty percent of the VentureOne study's respondents reported difficulty attracting and retaining outside directors. *See* VENTUREONE, *supra* note 8, at 1.

[12] Venture capitalists are investors who directly specialize in financing and proactively monitoring new business ventures. *See* PAUL MILGROM & JOHN ROBERTS, ECONOMICS, ORGANIZATION, AND MANAGEMENT 496 (1992). For instance, in 1988, an estimated 658 venture capital firms controlled approximately $31 billion in capital. Venture capital firms also employed over 2500 professionals that year. William A. Sahlman, *The Structure and Governance of Venture-Capital Organizations*, 27 J. FIN. ECON. 473 (1990), *reprinted in* ROBERTA ROMANO, FOUNDATIONS OF CORPORATE LAW 138 (1993).

[13] Press release from Daniel T. Kingsley, executive director, National Venture Capital Association, Clearing the Road for America's Growth Companies (on file with the *Harvard Journal on Legislation*). *See also* Roger S. Kaplan et al., *Labor Relations Considerations for the New High Technology Company*, 2 COMPUTER & HIGH-TECH. L.J. 19 (1986) ("[I]n the last two decades, 195,000 new jobs have been created in the Silicon Valley's electronic and computer industries alone."); Rubenstein, *supra* note 2, at 1 (reporting that young, medium-sized, high-tech companies are the greatest source of new job creation).

offs.[14] Because emerging growth companies rely heavily on venture capital,[15] any significant deterrent to raising this capital is likely to lead to an increased incidence of "crib death," and thereby strip the economy of an important source of job creation, new markets, and new technology.

Thus, proponents of the securities litigation reform movement have justifiably expressed a need to protect emerging growth companies and their integral role in economic recovery. Indeed, Congress itself has recently acknowledged the inextricable links between emerging growth companies and job creation, the development of new advanced technology, and the creation of new capital markets, as well as the incessant threat class action shareholder suits pose to such interests. Therefore, Congressional proposals to overhaul the private enforcement of the securities laws must be evaluated in terms of their ability to sufficiently address nuisance suits and the problem of "crib death."

II. PRIVATE ENFORCEMENT OF THE SECURITIES LAWS

A. *Rule 10b-5*

Private actions under Rule 10b-5[16] of the 1934 Securities Exchange Act[17] are the primary means for the private enforcement of the federal securities laws. As an enforcement tool against securities fraud, Rule 10b-5 serves the twofold purpose of providing compensation to private investors who are defrauded while also supplementing SEC enforcement actions.[18]

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[14] *See* Kingsley, *supra* note 13, at 1.

[15] In 1993, for instance, "venture capitalists supplied more than seventy percent of the equity required by high-growth companies." *Id. See also* Duncan M. Davidson & Jean A. Davidson, *Venture Capital Financing in the Computer Industry*, 6 COMPUTER L.J. 387 (1986); James J. Marcellino & Dexter L. Kenfield, *Due Diligence as a Two-Edged Sword: Potential Liability of Venture Capitalists Funding High-Tech Start-Ups*, 2 COMPUTER & HIGH-TECH L.J. 41, 42 (1986); George W. Dent, Jr., *Venture Capital and the Future of Corporate Finance*, 70 WASH. U. L.Q. 1029, 1031–32 (1992).

[16] 17 C.F.R. § 240.10b-5 (1994).

[17] 15 U.S.C. § 78(a)–(ll) (1994).

[18] Since the SEC lacks sufficient resources to police Rule 10b-5 violations on its own, private enforcement of the federal securities laws is viewed as indispensable to maintaining the fairness and efficiency of the securities markets and ensuring investor confidence. *See, e.g.*, 5A ARNOLD S. JACOBS, LITIGATION AND PRACTICE UNDER RULE 10B-5, § 8.01 (2d ed. 1992) ("Private actions are the most effective way to police 10b-5 breaches and provide the deterrent element so essential in securities transactions.") (footnote omitted); *see also* Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 310 (1985) (noting that implied private actions are effective in enforcing the

Promulgated by the SEC pursuant to its statutory authority to implement Section 10(b) of the 1934 Securities Exchange Act,[19] Rule 10b-5 bars all fraud "in connection with the purchase or sale of any security."[20] Although Rule 10b-5 does not expressly provide for a private right of action to enforce the federal securities laws, the courts have interpreted the Rule to be enforceable through an implied private right of action.[21]

B. *The Economic Rationale for Rule 10b-5: The Efficient Capital Markets Hypothesis*

The predominant theory of market efficiency, the Efficient Capital Markets Hypothesis (ECMH), maintains that the price of actively traded securities reflects relevant publicly available information.[22] Under the ECMH, relevant misrepresentations defraud investors who trade in capital markets because they un-

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federal securities laws and are an indispensable supplement to SEC enforcement action).

[19] 15 U.S.C. § 78(j) (1994).

[20] 17 C.F.R. § 240.10b-5 (1994). Rule 10b-5 states in full:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Id. Rule 10b-5 cases most often involve claims of relevant misrepresentations or omissions in public offering materials such as a prospectus or a registration statement. *See* Frank H. Easterbrook & Daniel R. Fischel, *Mandatory Disclosure and the Protection of Investors*, 70 VA. L. REV. 669 (1984).

[21] *See, e.g.*, Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350, 358–59 (1991) (recognizing that private claims arising under 10b-5 are of judicial creation and have been implied by courts for nearly fifty years).

[22] *See generally* Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 VA. L. REV. 549, 549 (1984) ("Of all recent developments in financial economics, the efficient capital market hypothesis (ECMH) has achieved the widest acceptance by the legal culture."); Daniel R. Fischel, *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities*, 38 BUS. LAW. 1 (1982) [hereinafter Fischel, *Modern Finance Theory*]; Daniel R. Fischel, *Efficient Capital Markets, the Crash, and the Fraud on the Market Theory*, 74 CORNELL L. REV. 907 (1989) (outlining the defining characteristics of "efficient" capital markets). Under the ECMH, market efficiency has been hypothesized to exist in three possible forms: the weak form, the semi-strong form, and the strong form. First, the weak form examines whether current stock prices fully reflect previous stock prices. The weak form of market efficiency would exist if investors could rely upon historical stock prices to ascertain future stock prices. Second, the semi-strong version tests whether all publicly available information is fully reflected in stock prices. Finally, the strong

fairly affect the market price of securities. In this regard, Rule 10b-5 has been viewed as an effective deterrent against securities fraud. Because efficient markets require complete and accurate information, it has been widely agreed that private actions under 10b-5 are essential to the operation of efficient capital markets, the maintenance of investor confidence, and the effective functioning of the federal securities laws.[23]

The concept that misrepresentations will unfairly affect the market price of securities is referred to as the fraud-on-the-market theory.[24] This theory presumes that the market price of a particular security reflects all available information and, therefore, accurately represents the security's intrinsic value.[25] The fraud-on-the-market theory thus creates a presumption that investors are defrauded when they rely on the market prices of securities that have been affected by relevant misrepresentations or omissions.[26]

Although the purpose of Rule 10b-5 is to deter the dissemination of incomplete and inaccurate information into the securities markets, and consequently to ensure investors that available information may be relied upon when making investment decisions,[27] Rule 10b-5 has been used by opportunistic plaintiffs to file a voluminous number of nuisance suits against emerging growth companies.[28] For this reason, the inquiry into the proper

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version tests whether all information, public and nonpublic, is fully reflected in stock prices. *See generally* Eugene F. Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383 (1970) (differentiating between the weak, semi-strong, and strong forms of ECMH). *But see* Jeffrey N. Gordon & Lewis A. Kornhauser, *Efficient Markets, Costly Information, and Securities Research*, 60 N.Y.U. L. REV. 761 (1985) (disputing the presumption that markets are efficient).

[23] *See* Fischel, *Modern Finance Theory*, *supra* note 22, at 1. *See generally* Mark L. Mitchell & Jeffrey M. Netter, *The Role of Financial Economics in Securities Fraud Cases: Applications at the Securities and Exchange Commission*, 49 BUS. LAW. 545, 572–84 (1994) (describing SEC enforcement actions using event study analysis premised on ECMH).

[24] *See, e.g.*, Zachary A. Starr, *Fraud on the Market and the Substantive Theory of Class Actions*, 65 ST. JOHN'S L. REV. 441 (1991); Fischel, *Modern Finance Theory*, *supra* note 22, at 1; Jonathan R. Macey & Geoffrey P. Miller, *Good Finance, Bad Economics: An Analysis of the Fraud-on-the-Market Theory*, 42 STAN. L. REV. 1059 (1990). *But see* Barbara Black, *Fraud on the Market: A Criticism of Dispensing with Reliance Requirements in Certain Open Market Transactions*, 62 N.C. L. REV. 435 (1984) (arguing that when the securities are "speculative" the plaintiff should bear the burden of establishing direct reliance).

[25] *See* sources cited *supra* note 24.

[26] The fraud-on-the-market theory was first employed by the Supreme Court in Basic, Inc. v. Levinson, 485 U.S. 224 (1988). *See generally* Jonathan R. Macey et al., *Lessons from Financial Economics: Materiality, Reliance, and Extending the Reach of* Basic v. Levinson, 77 VA. L. REV. 1017 (1991).

[27] *See generally* Easterbrook & Fischel, *supra* note 20, at 669.

[28] *Cf.* notes 7–11 and accompanying text.

cure to the "crib death" phenomenon must begin with a look at the unique susceptibility of emerging growth companies to nuisance suits brought under Rule 10b-5.

III. The Effects of Nuisance Suits on Emerging Growth Companies

Nuisance suits brought under Rule 10b-5 have worked a pernicious effect on emerging growth companies. Since emerging growth companies have scarce start-up resources[29] and must rely disproportionately upon venture capital to fund much of their operations,[30] emerging growth companies must place a premium on short-term profit-making in order to survive.[31] Protracted litigation during the early stages of an emerging growth company's development may result in "crib death."[32] In the interests of survival, it is not only imperative that emerging growth companies avoid full-fledged litigation but, as a general matter, these companies must prefer settlements when faced with potentially fatal litigation.[33]

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[29] While emerging companies rely heavily upon venture capital to develop operations, venture capitalists generally do not invest all external capital in a single company at one time but instead invest capital at different stages in a company's development. This practice of staging capital causes emerging companies to begin operations cautiously, with the knowledge that venture capitalists may withhold investing additional capital unless future prospects appear profitable. *See* Sahlman, *supra* note 12, at 141 ("Venture capitalists rarely, if ever, invest all the external capital that a company will require to accomplish its business plan: instead, they invest in companies at distinct stages in their development. As a result, each company begins life knowing that it has only enough capital to reach the next stage."). *See also* Michael B. Staebler & Vicki R. Harding, *Venture Capital: Who Controls the Business?*, Mich. B.J., Jan. 1990, at 32, 33 ("Most early stage venture-backed companies receive a number of rounds of financing. If an early stage company successfully meets its projections, the initial round of financing is the most expensive to the company . . . . If the entrepreneur miscalculates and significantly misses projections, not only will additional rounds of financing prove more expensive, but funding sources may require new management.").

[30] *See* sources cited *supra* note 15.

[31] *Cf.* Robert L. Frome, *Venture Capital Negotiations*, N.Y.L.J., July, 25, 1985, at 1 ("Typically, the rate-of-return expected by venture capital investors in [investor capital] pools ranges up to 20 percent.").

[32] The unique susceptibility of emerging companies to "crib death" results in the critical need for venture capital. *See id.*

[33] Unlike emerging companies, larger companies sometimes prefer litigation despite its significant costs because many of these companies view themselves as "repeat players" in securities class action suits. *See* Coffee, *supra* note 4, at 702 (explaining that repeat players often choose to litigate in order to deter future litigation).

A. *"Crib Death" by Litigation*

Nuisance suits brought under Rule 10b-5 against emerging growth companies may spell "crib death" for a variety of reasons. The main reason for an emerging growth company to avoid litigation is the costly nature of litigation itself. Generally, plaintiffs in class action shareholder suits have the benefit of lower litigation costs.[34] Defendants, for instance, must respond to sizeable discovery requests, which can be made quickly and cheaply by the plaintiff. And whereas the plaintiff class needs but one lawyer, each defendant in a derivative action needs separate counsel.[35] This cost imbalance, coupled with the fact that plaintiffs may easily take advantage of the unique capital constraints of venture-backed corporations,[36] makes emerging growth companies especially easy targets for nuisance suits.[37]

While summary judgment motions provide a modicum of protection against frivolous and meritless claims, they often fails to protect emerging growth companies from nuisance suits.[38] Because inquiries into intangible issues such as materiality, scienter, and reliance form the basis of 10b-5 actions, courts are reluctant to summarily presume that a plaintiff has not presented any material issues and prefer that the trier of fact draw the proper inferences from such inquiries.[39] Additionally, capital constraints, though smaller at the summary judgment stage than during the trial process, will still lead many emerging growth companies to favor immediate settlement over litigation.[40]

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[34] *Id.* at 701–02.

[35] *See id. See also* John C. Coffee, Jr., *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, LAW & CONTEMP. PROBS., Summer 1985, at 5.

[36] *See supra* note 15 and accompanying text.

[37] *See, e.g.*, Janet C. Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 569 (1991) ("When there has been a sharp decline in the market price of a company's stock, the mere filing of a complaint appears to be a ticket to a guaranteed and substantial recovery.").

[38] *See, e.g.*, William M. Lafferty & W. Leighton Lord III, *Towards a Relaxed Summary Judgment Standard for the Delaware Court of Chancery: A New Weapon Against "Strike" Suits*, 15 DEL. J. CORP. L. 921 (1990).

[39] *See, e.g.*, TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 450 (1976) (recognizing that issues such as materiality, scienter, and reliance require "delicate assessments of the inferences a 'reasonable shareholder' would draw from a given set of facts and the significance of those inferences to him, and these assessments are peculiarly ones for the trier of fact").

[40] *See* Anthony Aarons, *Why Them?*, CAL. L. BUS., July 11, 1994, at 26, 39 ("[M]any high-tech executives say that waiting until the summary judgment level creates a large waste of resources.").

Litigation is also undesirable for more "qualitative" reasons. First, litigation makes it increasingly more difficult for emerging growth companies to recruit and retain experienced outside directors. In general, investors prefer to invest in companies with outside directors because the "independence" of such directors, who have no financial interest in corporate revenues or in one particular management group, ensures that these directors will best monitor the company's management.[41] Thus, the presence of outside directors is often viewed by investors as indicative of a company's quality. Yet emerging growth companies, in the face of the continuous threat of nuisance suits, find it difficult to attract experienced outside directors since few directors dare risk damage to name and reputation from involvement in securities fraud litigation.[42]

Second, while companies often purchase D&O liability insurance to protect themselves against the costs of litigation, premiums for emerging growth companies have risen sharply due to nuisance litigation.[43] Moreover, D&O policies usually have limitations that are too stringent to sufficiently shield emerging growth companies from liability.[44] Some emerging growth companies cannot even find a single D&O insurer.[45] The inadequacy and unavailability of D&O insurance significantly diminishes the likelihood that emerging growth companies will successfully

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[41] *See* Committee on Corporate Laws, *Guidelines for the Unaffiliated Director of the Controlled Corporation*, 45 BUS. LAW. 429 (1989); Donald E. Pease, *Outside Directors: Their Importance to the Corporation and Protection from Liability*, 12 DEL. J. CORP. L. 25 (1987). *But see* Victor Brudney, *The Independent Director—Heavenly City or Potemkin Village?*, 95 HARV. L. REV. 597 (1982) (disputing the claim that outside directors improve corporate social responsibility). *See generally* Paul H. Zalecki, *The Corporate Governance Roles of the Inside and the Outside Directors*, 24 U. TOL. L. REV. 831 (1993).

[42] *See* David L. White, *Outside Directors Under the Federal Securities Laws: Fraudulent Actors or Innocent Victims?*, 21 SEC. REG. L.J. 297, 297–98 (1993).

[43] *See* sources cited *supra* note 10 and accompanying text. *See also* John S. DeMott, *Duck and Cover*, CHIEF FIN. OFFICER, Feb. 1994, at 40 ("Protecting officers and directors from such capricious claims—in addition to those with more merit—is always expensive and often confusing. Annual premiums can range from as little as $2,000 to as high as $70 million, for corporations with heavily litigious track records.").

[44] "[T]o protect themselves and to keep D&O insurance profitable, insurers underwrite some D&O policies with enough exclusions to effectively block payouts for many things directors and officers are actually sued over." DeMott, *supra* note 43, at 40.

[45] *See* Judy Semas, *Ripe Targets for Lawsuits*, BUS. J., Jan. 31, 1994, at 19, 19 ("[H]igh-tech companies—especially startups and smaller firms—are finding it tough to get D&O coverage. Few insurance carriers offer it to them, and those that do charge exceptionally high premiums."). *See also* Pease, *supra* note 41, at 82–83; DeMott, *supra* note 43, at 40 ("Insurers also are cutting back in some industry sectors, including financial services and high-technology.").

recruit and retain experienced outside directors.[46]

Third, litigation raises the potential of irreparable harm to a company's reputation. In fact, consumer attitudes may be so adversely affected upon the initiation of a class action shareholder suit that some consumers may begin to view a particular product and its entire industry negatively.[47] Since most consumer purchases involve potential repeat customers, a class action suit may significantly stifle future revenues.[48] Litigation has the potential to damage a company's reputation, and consequently may deter both consumer and investor interest.

Finally, raising capital, particularly venture capital, over the course of litigation is nearly impossible since investors are adverse to accepting the financial risks associated with a losing defendant. In the case of venture capitalists, who expect to garner above average profits from investments,[49] litigation may cause these financiers to "jump ship," thereby inducing "crib death."[50] Furthermore, venture capitalists typically retain control over an emerging growth company's operations by investing capital at different stages in a company's development. This capital-staging process obliges emerging growth companies to operate conservatively, especially when faced with the prospect of losing their invaluable venture capital constituency.[51] Emerging growth companies, therefore, prefer settlement to litigation, which would otherwise precipitate the loss of future capital investment.

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[46] *See* DeMott, *supra* note 43, at 38 ("A Louis Harris & Associates poll . . . showed that approximately 90 percent of outside directors believe inadequate D&O insurance is a 'disincentive' to joining a board.").

[47] *See generally* Doris Van Doren et al., *The Effect of a Class Action Suit on Consumer Attitudes*, J. PUB. POL'Y & MARKETING, Spring 1992, at 45.

[48] *See generally* Mark Peyrot & Doris Van Doren, *Effect of a Class Action Suit on Consumer Repurchase Intentions*, J. CONSUMER AFF., Dec. 22, 1994, at 361.

[49] *See also* Dent, *supra* note 15, at 1034 ("Only one-third of the companies that use venture capital financing succeed. Venture capitalists demand high returns because the successful one-third of their investments must cover the losses generated by the other two-thirds, as well as the high transaction costs that venture capitalists pay in seeking, monitoring, and evaluating their investments."). *See generally* Robert H. Mnookin & Robert B. Wilson, *Rational Bargaining and Market Efficiency: Understanding* Pennzoil v. Texaco, 75 VA. L. REV. 295, 330–34 (1989).

[50] *See, e.g.*, Sahlman, *supra* note 12, at 141; Staebler & Harding, *supra* note 29, at 33.

[51] *See, e.g.*, Frome, *supra* note 31, at 1.

B. *Settlements*

Emerging growth companies prefer immediate settlement to litigation because settlement diminishes the likelihood of "crib death." Yet, while settlement usually represents the more economical alternative for emerging growth companies,[52] settlement nonetheless offers little protection against nuisance suits. In fact, recent studies on emerging growth companies have concluded that the settlement value of a shareholder suit bears little, if any, relation to its merits.

1. Empirical Data

A recent study of seventeen high-technology companies that made initial public offerings of securities (IPOs) in 1983 suggests that settlements bear little, if any, relationship to the merits of each case.[53] The study, conducted by Professor Janet Cooper Alexander, found that twelve of seventeen high-technology companies experienced sharp declines in their stock prices and, as a consequence, nine became targets of securities fraud suits.[54] In addition, the study also revealed that five suits were settled for between 24.5% and 27.5% of the damages sought by the plaintiffs and a sixth suit was settled at 20.6%.[55] The uniformity of these settlement rates suggests that the primary motivation for the suits at issue was sharp declines in stock prices and a desire for settlement, rather than an actual securities violation.[56] This empirical data supports the proposition that securities class ac-

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[52] *See* Lafferty & Lord, *supra* note 38, at 927 ("Settlement has obvious appeal to a corporation because, in essence, a settlement purchases a *res judicata* decree and limits the corporation's potential liability.") (footnote omitted).

[53] *See* Alexander, *supra* note 37, at 497.

[54] *See id.* at 511.

[55] *See id.* at 517. The remaining suits were settled on account of extenuating circumstances. For example, one settlement was precipitated by the company entering bankruptcy. *Id.* at 517–18.

[56] *See id.* at 513 (arguing that following an initial public offering, derivative suits are filed whenever the stock price declines enough to give a reasonable expectation of substantial attorneys' fees). *See also* William S. Lerach, *Securities Class Actions and Derivative Litigations Involving Public Companies: A Plaintiff's Perspective, in* 1 SECURITIES LITIGATION 7, 92 n.82 (PLI Corporate Law and Practice Course Handbook Series No. 491, 1985); W. John Moore, *Litigators Replace Capitalists as Kings of the Silicon Valley*, LEGAL TIMES, July 2, 1984, at 1, 2; sources cited *supra* note 5. *But see* John C. Coffee, Jr., *The "New" Learning On Securities Litigation*, N.Y.L.J., Mar. 25, 1993 at 5 (arguing that Professor Cooper's empirical evidence is not conclusive because the sample companies cited were ultra-sensitive to overall downward market movement).

tion suits brought against emerging growth companies are filed and settled regardless of the merits.[57]

Another recent study, conducted by National Economic Research Associates (NERA) also supports the hypothesis that securities class action settlements bear little, if any, relation to the merits of each case.[58] In fact, the NERA study concluded that among the three main factors the merits of a case is, on average, only the third most relevant factor in explaining settlement.[59] In order to reach this conclusion, the NERA study analyzed two factors that, in theory, should increase the likelihood that a plaintiff would prevail.[60] First, the study asked whether the case involved a securities offering. Second, the study questioned whether any independent enforcement action for securities fraud was taken by a federal or state agency.[61]

The analysis of whether the securities fraud action involved a securities offering permitted an inquiry into the potential for a violation of Section 11 of the 1933 Securities Act.[62] Section 11 imposes liability for material misstatements in a registration statement, unless the defendant can establish nonnegligence.[63] Because it is a strict liability anti-fraud provision, a plaintiff in a Section 11 suit has a less stringent burden of proof in comparison to the burden of proof required under Rule 10b-5.[64] Therefore, a Section 11 claim should increase the settlement value of the case. Despite this difference, however, the NERA study concluded that the presence of a Section 11 claim was statistically insignificant compared with the actual amount of the settlement.[65]

The second factor of the NERA study also tested the purported role merit plays in the settlement value of securities claims.

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[57] *See generally* Alexander, *supra* note 37, at 505–23.

[58] *See generally* DUNBAR & JUNEJA, *supra* note 6, at 14.

[59] According to the NERA study, the three main factors that explain settlements are: (1) stock price volatility; (2) availability of assets; and (3) merits of the case. *See id.*

[60] *See id.* at 10.

[61] *See id.* at 11.

[62] 15 U.S.C. § 77k(a) (1994).

[63] *See id.* More specifically, under Section 11 an issuer is liable, and persons associated with the issuer or the distribution of securities, for material misrepresentations or omissions in a registration statement to those persons who purchased securities pursuant to that registration statement.

[64] Courts tend to ignore the usual facts in Section 11 cases, whereas 10b-5 actions necessitate inquiry into the facts and circumstances of each case in order to prove scienter, or an intent to defraud. *See, e.g.*, Herman & MacLean v. Huddleston, 459 U.S. 375, 382 (1983) (noting that Section 11 imposes a relatively minimal burden upon a plaintiff as compared to Section 10(b)). *Compare* notes 20–21 and accompanying text.

[65] *See* DUNBAR & JUNEJA, *supra* note 6, at 11.

Evidence of government enforcement would indicate a stronger basis for a private plaintiff's claim of securities violations. Yet the study again concluded that the presence of a federal or state enforcement action was statistically insignificant compare with the settlement amount.[66] Even when the government found a securities violation there was no corresponding increase in the settlement amount of a private action.[67]

Thus, as an empirical matter, settlements in class action shareholder suits often fail to account for the actual merits of the cases.[68] This ubiquity of meritless settlements frustrates the purpose and effect of the federal securities laws, which are designed to preserve the integrity of the marketplace and maintain investor confidence. Meritless settlements also encourage companies to reduce the amount of information that they disclose in order to avoid the risks of liability for fraudulent misrepresentations.[69] Because nuisance suits reduce emerging growth companies' incentives to completely and accurately disclose all relevant information, investors cannot fully account for an emerging growth company's financial position and performance.[70] This phenomenon may result in widespread underpricing of the value of emerging growth companies' securities and a decrease in investment in the securities markets altogether.[71]

The problems that nuisance suits and meritless settlements present for emerging growth companies have reached monumental proportions, both in terms of cost and in terms of their

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[66] *Id.*

[67] *Id.*

[68] *But see* Joel Seligman, *The Merits Do Matter*, 108 HARV. L. REV. 438 (1994) (claiming that sufficient evidence has yet to be established that would justify legislative changes affecting the private enforcement of the federal securities laws).

[69] *See generally* Sweeney, *supra* note 6, at 30 ("[C]orporate America is becoming stingier with information on earnings and revenues. A survey by the National Investor Relations Institute of executives at 381 companies, for example, found that 37 percent of its members had responded to 'the recent threat of shareholder litigation' by curtailing the flow of information to the investment community."). *See also* Gupta & Bowers, *supra* note 5, at B2 ("[B]iotech companies that have been sued say they . . . are less forthcoming about what work they are doing in their laboratories for fear their comments might be misconstrued.").

[70] *See generally infra* notes 108–112 and accompanying text.

[71] *See* Philip D. Drake & Michael R. Vetsuypens, *IPO Underpricing and Insurance against Legal Liability: Initial Public Offerings*, FIN. MGMT., Mar. 22, 1993, at 64 ("A potential explanation for the pervasive short-run underpricing of initial public offerings (IPOs) of equity relies on issuers' and underwriters' desire to avoid legal liabilities under federal securities laws for material misstatements in the offering prospectus or registration statement."). *See also* Seha M. Tinic, *Anatomy of Initial Public Offerings of Common Stock*, 43 J. FIN. 789 (1988) (explaining that underpricing is a form of insurance against liability).

volume and frequency. Although Rule 10b-5 has been viewed for more than half a century as a necessary and effective deterrent to securities fraud, the current imbalance between the shareholder plaintiff and the emerging growth company defendant weighs overwhelmingly in favor of shareholder litigants.[72] Indeed, the sheer magnitude of this problem has recently prompted Congress to propose substantive reforms for private securities litigation.

IV. Proposals for Reform

Because the federal securities laws are designed to ensure fully functioning, efficient securities markets, it is appropriate to analyze Congressional reform proposals for securities litigation by examining their economic consequences. Since investors end up on both sides of securities suits, proposals for reform must balance the interests of emerging growth companies, as significant conduits for economic growth, against investors' interest in not being defrauded. Congressional proposals for nonbinding alternative dispute resolution (ADR) and safe harbor for management's predictive statements will adequately protect the financial interests of investors while also mitigating the omnipresent specter of "crib death" for emerging growth companies.

A. *Benefits of Alternative Dispute Resolution (ADR)*

Alternative dispute resolution (ADR) is particularly well-suited for securities fraud actions,[73] and especially for actions arising between emerging growth companies and their investors. As a general matter, ADR is almost always more cost-effective than litigation.[74] Aside from the administrative costs and the professional fees arising from the litigation, parties to litigation must

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[72] *See supra* notes 34–40 and accompanying text. *See also* Lambert, *supra* note 7. *But see* Herbert Stein, *Letting Wall Street Off Easy*, N.Y. Times, Feb. 15, 1995, at A21 (claiming that the securities litigation reform movement downplays the effect of private securities litigation in deterring corporate dishonesty and negligence); *Overprotecting Corporations*, N.Y. Times, Feb. 22, 1995, at A18.

[73] *See* Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987) (holding that the 1934 Securities Exchange Act does not preclude enforcement of predispute arbitration agreements). *See also* Daniel R. Waltcher, *Classwide Arbitration and 10b-5 Claims in the Wake of* Shearson/American Express, Inc. v. McMahon, 74 Cornell L. Rev. 380 (1989).

[74] *See* Danny Ertel & Ralph C. Ferrara, Beyond Arbitration: Designing

bear the onerous and time-consuming logistical problems involved in a trial, such as conducting interviews and depositions, supervising discovery, and making court appearances.[75] The psychological costs of litigation may also be staggering,[76] particularly in a securities fraud suit where reputational damage to an emerging growth company, its directors, and the entire industry may be irreparable.[77] After accounting for these variables, litigation is the most costly and risky form of dispute resolution in almost every case.

ADR, however, reduces costs for both the litigants and the court system.[78] Easing overburdened court dockets[79] bolsters public confidence in the legitimacy and workability of the judicial system, while at the same time reducing public dissatisfaction with the costs of meritless litigation.[80] As the private enforcement of the federal securities laws becomes increasingly perceived as a costly endeavor that provides the taxpayer no benefit, the popular political support it has traditionally enjoyed may evaporate.[81]

ADR is also a less time-consuming forum for dispute resolution compared to litigation[82] since it avoids the formal processes of litigation, such as extensive motion practice and massive document discovery requests, which often cause substantial delays and court backlogs. Unlike litigation, ADR permits the parties to sidestep onerous discovery rules and due process require-

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ALTERNATIVES TO SECURITIES LITIGATION § 2.13 (1991) (presenting empirical evidence that arbitration is a cheaper and more speedy alternative to litigation).

[75] *See id.* § 3.02.

[76] *See id. See also* Jean Faure, Comment, *The Arbitration Alternative: Its Time Has Come*, 46 MONT. L. REV. 199 (1985) (explaining that litigation imposes emotional as well as financial costs).

[77] *See supra* notes 41–43 and accompanying text.

[78] *See* ERTEL & FERRARA, *supra* note 74, § 3.02. *See also* W.B. Rayner, *Arbitration: Private Dispute Resolution as an Alternative to the Court*, 22 U. W. ONT. L. REV. 33, 34 (1984) (suggesting that ADR avoids the costs associated with litigation, such as maintaining the judiciary).

[79] *See* RICHARD POSNER, THE FEDERAL COURTS: CRISIS AND REFORM 63–64 (1985) (observing that the number of cases filed in the federal courts between the years 1960 to 1983 "more than tripled, roughly from 80,000 to 280,000—a 250 percent increase, compared with less than 30 percent in the preceding quarter century").

[80] *See generally* Stephen Budiansky, *How Lawyers Abuse the Law*, U.S. NEWS & WORLD REP., Jan. 30, 1995, at 51 ("A new *U.S. News* poll finds that 69 percent of Americans believe lawyers are only sometimes honest or not usually honest, and 56 percent say lawyers use the system to protect the powerful and enrich themselves.").

[81] *See* Alexander, *supra* note 37, at 569.

[82] *See, e.g.*, G. Richard Shell, *Keep Broker-Client Disputes Out of Court*, WALL ST. J., Mar. 3, 1987, at 32 (noting that disputes submitted to arbitration are usually resolved within the same year); *Union Carbide Uses Mini-Trial to Settle 19 Toxic Tort Cases*, 1 ALTERNATIVES TO THE HIGH COST OF LITIG. (CPR) 1 (May 1983). *See also* ERTEL & FERRARA, *supra* note 74, §§ 2.13, 3.03.

ments by streamlining the information gathering process with negotiated rules that best suit the specifics of each dispute.[83] Whereas the formalities of litigation often impose unnecessary costs upon the parties, ADR permits each party to deploy investment resources to meet the specific exigencies at hand.[84]

In view of the aforementioned advantages, the SEC has touted ADR as the preferred method of securities dispute resolution.[85] In most situations both companies and investors will prefer the less costly and less time-consuming approach of ADR.[86] Indeed, ADR has already emerged as the predominant alternative to full-fledged securities fraud litigation.[87]

A provision for nonbinding ADR would benefit emerging growth companies in a variety of ways. First, ADR is a less time-consuming and costly form of dispute resolution, thereby enabling an emerging growth company to invest more time and resources in the daily monitoring and supervision of its business operations. As previously noted, in response to the pervasive impact of nuisance suits, emerging growth companies have expended an overwhelming amount of resources fighting securities fraud class action suits.[88] Because "crib death" is an incessant threat for emerging growth companies during early development, management has little choice but to expend considerable amounts of

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[83] *See* ERTEL & FERRARA, *supra* note 74, § 3.21 (outlining the ADR mechanisms, or "process aids," which enable the parties to a dispute to address issues and cooperate with each other more effectively). *See also id.* §§ 4.01–.13 (outlining methods for designing ADR procedures to fit the special circumstances of the dispute).

[84] *See generally* C. Edward Fletcher III, *Learning to Live with the Federal Arbitration Act: Securities Litigation in a Post-*McMahon *World*, 37 EMORY L.J. 99 (1988).

[85] *See, e.g.*, Implementation of an Investor Dispute Resolution System, Exchange Act Release No. 13,470 [1977-1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,136 (Apr. 26, 1977).

[86] *See* Leonard K. Berman, Note, *Arbitrability of Rule 10b-5 Claims*, 34 WAYNE L. REV. 245, 261 (1987). *But see* Cristy B. Bell, Comment, *Investor Protection After* McMahon: *The Arbitrability of Claims Arising Under Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5*, 13 DEL. J. CORP. L. 537, 571 (1988) (arguing that securities arbitration procedures, as currently constituted, fail to adequately protect investors). *See generally* Herbert M. Kritzer & Jill K. Anderson, *The Arbitration Alternative: A Comparative Analysis of Case Processing Time, Disposition Mode, and Cost in the American Arbitration Association and the Courts*, 8 JUST. SYS. J. 6 (1983).

[87] *See generally* David A. Lipton, *Generating Precedent in Securities Industry Arbitration*, 19 SEC. REG. L.J. 26 (1991). For a brief introduction to arbitration and how it is currently used for resolving securities disputes, see Norman S. Poser, *When ADR Eclipses Litigation: The Brave New World of Securities Arbitration*, 59 BROOK. L. REV. 1095 (1993). For a more expansive treatment of the arbitration process in securities disputes, see Constantine N. Katsoris, *The Arbitration of a Public Securities Dispute*, 53 FORDHAM L. REV. 279 (1984).

[88] *See supra* notes 7–11, 29–51 and accompanying text.

scarce start-up resources for its defense. More importantly, class action suits compel emerging growth companies into granting an inordinate amount of management's time, capital, and other corporate resources toward supervising litigation,[89] rather than committing the optimal amount of corporate resources to their business operations. As a result, investors grow increasingly wary and are more apt to reduce investment, primarily because the emerging growth company cannot optimally manage business operations and at the same time coordinate a concerted securities fraud defense.[90] Although ADR does not entirely resolve this dilemma, it considerably mitigates the problem by affording an emerging growth company's management the chance to commit less time, money, and scarce start-up resources to the dispute.

Second, ADR offers and encourages the preservation and continued development of the emerging growth company-investor relationship.[91] Since the stock prices of emerging growth companies are highly volatile,[92] it is often difficult for these companies to attract willing investors in the first place. At the very least, ADR provides a chance for emerging growth companies to preserve their relationships with investors by resolving disputes in a cost-effective and timely manner.

Third, a reform measure that includes ADR would allow emerging growth companies to avoid the negative publicity commonly associated with securities fraud suits and the perilous threat such publicity poses to their survival. Indeed, mere publicity of a single securities fraud filing against an emerging growth company can create a "race to the courthouse phenomenon" in which news of the first filing results in an onslaught of additional suits.[93] Bad publicity destroys consumer markets as well as inves-

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[89] *See id.*

[90] *See, e.g., Lawsuit Against Silicon Graphics Dismissed by US District Court*, PR Newswire, Mar. 31, 1992, *available in* LEXIS, News Library, Arcnws File (quoting Silicon Graphics' President Edward R. McCracken decrying the amount of resources spent defending against a class action shareholder suit that would have been better spent on research and innovation); Sweeney, *supra* note 6, at 30 (citing Amex study that concluded that 7 out of 10 CEOs spent a full day each week supervising lawsuits while they were pending); Joshua Lerner, EMC Corporation: Response to Shareholder Litigation (A) 11 (Apr. 11, 1994) (Harvard Business School case 2-286-106) (noting that nuisance suits may distract directors from focusing on the essential needs of a company).

[91] *See* ERTEL & FERRARA, *supra* note 74, § 3.04.

[92] *See* Gupta & Bowers, *supra* note 5 and accompanying text.

[93] *See* Linda Himelstein, *Monkey See, Monkey Sue*, BUS. WK., Feb. 7, 1994, at 112 (reporting that publicity surrounding settlements spurs bandwagon lawsuits). *See also Securities Litigation: Hearings Before the Subcomm. on Telecommunications and*

tor confidence.[94] By avoiding negative publicity, emerging growth companies may not only be able to keep their investors, but may also be able to recruit and retain outside directors who would otherwise avoid involvement with companies facing the prospect of continuous securities fraud actions.[95]

Finally, unlike litigation, ADR affords emerging growth companies the benefit of sharing information necessary for dispute resolution within a controlled environment. In cases where the information in dispute is of a specialized or sensitive character, a court's protective order may not provide sufficient protection. Since the issuing of the protective order becomes a matter of public record, the order itself alerts the public to the fact that an emerging growth company sought to protect valuable inside information.[96] ADR, however, allows the parties to control the dissemination of such information to the public.[97] This is particularly important in the high-technology industry where information concerning trade secrets, new product developments, new markets, and research and development strategies is critical to an emerging growth company maintaining its competitive advantage.[98] Although ADR cannot guarantee protection for every bit of nonpublic information, it nonetheless offers emerging growth companies more protection than is accorded in litigation, since the parties in ADR may negotiate the terms of disclosure amongst themselves.[99]

By removing the dispute from public view and avoiding public disclosure of inside information that may be damaging person-

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Finance of the House Comm. on Energy and Commerce, 103d Cong., 2d Sess. (1994) (statement of Prof. John C. Coffee, Jr., Columbia University Law School) (testifying that adverse public disclosures often cause an onslaught of securities class action filings, sometimes within hours after disclosure).

[94] In addition to destroying consumer and investor confidence, securities litigation often compounds into more litigation. *See* John E. Kennedy, *Securities Class and Derivative Actions in the United States District Court for the Northern District of Texas: An Empirical Study*, 14 HOUS. L. REV. 769, 807, 824 (1977) (presenting empirical evidence that 50% of the class action and derivative actions that were filed came on the heels of a prior SEC or bankruptcy proceeding).

[95] *See supra* notes 41–44 and accompanying text. Emerging companies must also be concerned with the recruitment and retention of employees. *See generally* Roger S. Kaplan et al., *Labor Relations Considerations for the New High-Technology Company*, 2 COMPUTER & HIGH-TECH. L.J. 19, 20 (1986).

[96] *See* ERTEL & FERRARA, *supra* note 74, § 3.06.

[97] *See id.*

[98] *See, e.g.*, Susan Orenstein, *Chipping Away at the Competition*, LEGAL TIMES, May 18, 1992, at 23 (noting how far some high-technology companies will go to protect new product developments).

[99] *See* ERTEL & FERRARA, *supra* note 74, § 3.06.

ally, professionally, or financially to a particular party to the dispute, ADR substantially reduces the risk that one party may coerce acceptance of an unfair settlement.[100] This concern takes on heightened significance within emerging growth industries in which the mere allegation of fraud, even if proven later to be meritless, may loom large in the minds of prospective officers and directors as well as skeptical investors and consumers, thereby harming public relations.

B. *Benefits of a Safe Harbor for Predictive Statements*

The optimal securities litigation reform measure would also include a safe harbor for predictive statements. Emerging growth companies are overwhelmingly concentrated within the high-technology industry, which, by definition, develops a host of new products and creates new consumer markets. Unlike most other industries, the prospects for an emerging growth company's success are generally more difficult to quantify since the more traditional criteria for assessing future profitability are usually inapplicable.[101] Hence less-than-precise disclosures concerning future profits, whether the result of an emerging growth company's miscalculation or honest mistake, are justifiably distinguishable from disclosures rising to the level of intentional securities fraud.[102]

Emerging growth companies, largely concentrated within "high-risk" industries,[103] are dependent upon what might typically be characterized as "soft information" when making predictive statements. "Soft information," which describes business activities and contingencies that will occur at some later date, is inherently unpredictable.[104] As a matter of policy, therefore, this information should be distinguished from "historical information," or

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[100] *See id.*

[101] *See* Lerner, *supra* note 90, at 5–6 (case study demonstrating the inherent unpredictability of profit-making in the high-technology industry).

[102] For instance, Rule 10b-5 provides no cause of action in alleging corporate mismanagement or poor predictions. *See, e.g.*, Santa Fe Industries, Inc. v. Green, 430 U.S. 462, 479 (1977) (recognizing that Congress did not intend § 10(b) to reach transactions that amount to nothing more than internal corporate mismanagement).

[103] Capital for emerging growth companies, because it typically involves some investment risk but presents a chance for above average future profits, is commonly referred to as "risk capital." JOHN DOWNS, DICTIONARY OF FINANCE AND INVESTMENT TERMS 503 (Jordan E. Goodman ed., 3d ed. 1991).

[104] "Soft information" may be generally defined as "statements of subjective analysis and extrapolations, such as opinions, motives, and intentions, or forward-looking

information dealing with business events and developments that have already transpired.[105] Those cases in which historical information that is incorrect as a matter of law is supplied to investors either with an intent to defraud or as a result of pure recklessness are the ones that most warrant a finding of securities fraud. But in the case of "soft information" concerning future forecasts, an emerging growth company's predictions are indeed nothing more than predictions, and as a matter of policy should not be construed by investors as an outright guarantee of a specified level of return. So long as safe harbor protection is extended only to predictive statements, rather than historical information, a safe harbor provision ensures disclosure of the optimal amount of information for investors.

A safe harbor provision for predictive statements would protect both emerging growth companies and investors in several ways. As an empirical matter, the threat of nuisance suits has retarded the flow of relevant information from an emerging growth company's management to its investors.[106] In a recent survey of publicly held venture-backed companies, approximately seventy-one percent of all respondents reported a reluctance to discuss business performance with analysts and the public, although only seventeen percent of these respondents had been defendants in shareholder suits.[107] This data evinces that even publicly held venture-backed companies that had not been sued responded to the pervasive flurry of securities fraud class action suits by disclosing less information to investors, with the objective of diminishing the likelihood of liability.

Securities suits against emerging growth companies distort incentives to supply investors with enough information to make fully informed investment decisions. An emerging growth company's fear of liability for good faith projections or honest mistakes in forecasting effectively leaves investors to their own

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statements (e.g., projections, estimates, appraisals, and forecasts)." JAMES D. COX ET AL., SECURITIES REGULATION 75 (1991).

[105] "Historical information" includes information concerning "sales, expenses, and income produced from operations for a period, as well as the assets, liabilities, and equity of the firm as of a specific date in the past." *Id.* at 82.

[106] *See* Gupta & Bowers, *supra* note 5, at B2 (reporting that small biotech companies "are less forthcoming about what work they are doing in their laboratories for fear their comments might be misconstrued."). *See also* Bowers & Gupta, *supra* note 6, at B1 ("At the advice of their lawyers, entrepreneurs and directors are discussing potential problems in their public documents more fully while toning down the hype in their discussions with analysts.").

[107] *See* VENTUREONE, *supra* note 8, at 2.

devices in evaluating future profitability.[108] Yet a safe harbor for predictive statements would remove the disincentives generated by the threat of nuisance suits, while encouraging emerging growth companies to disclose the optimal amount of information to investors.

Disclosure of relevant information is essential since investors rely heavily on management earning forecasts in making investment decisions.[109] Management has privileged access to nonpublic inside information concerning the company's financial performance, capital resources, liquidity, new products, and new markets. This access renders an emerging growth company's management best equipped to provide investors with the information necessary to estimate return on investment.[110]

In addition, management forecasts are, as an empirical matter, more accurate than forecasts made by analysts.[111] Consequently, many investors rely most heavily on management forecasts when reviewing an emerging growth company's future profitability. A safe harbor for emerging growth companies would encourage management to provide investors with the most accurate business projections possible and would also avoid rendering investors solely at the mercy of analysts with less than optimal information.[112]

Finally, the suitability of a safe harbor for predictive statements may be analyzed by reference to the unique nature of the

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[108] Investors who are left to their own devices in evaluating a company's future profitability will typically rely upon analysts' forecasts, which are less accurate than forecasts issued by management. *See infra* note 111 and accompanying text. Furthermore, small investors generally have less information than larger investors, and losing the benefit of management disclosures may heighten informational disadvantages between these two groups. *See* Kerber, *supra* note 7, at H1 (noting that in the absence of management disclosures large investors at least have access to brokers and other informational avenues, whereas small investors usually lack the resources and financial stature to gain valuable investment information).

[109] *See* John S. Poole, *Management Forecasts: Do They Have a Future in Corporate Takeovers?*, 42 SMU L. REV. 765, 803 (1988) (detailing how studies of stock returns show that the market reacts to management forecasts). *See also* Bipin B. Ajinkya & Michael J. Gift, *Corporate Managers' Earnings Forecasts and Symmetrical Adjustments of Market Expectations*, 22 J. ACCT. RES. 425 (1984) (concluding that stock price movements were directly correlated to the size and direction of investors' expectations of management's earnings forecasts). *See, e.g.*, SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (2d Cir. 1968), *cert. denied* 404 U.S. 1005 (1969) (recognizing that material facts that affect an investor's decision to buy, sell, or hold a particular security include information disclosing a company's earnings and distributions).

[110] *See* Poole, *supra* note 109, at 811.

[111] *See, e.g., id.* at 810–11 (1988). *See also* Bart A. Basi et al., *A Comparison of the Accuracy of Corporate and Security Analysts Forecasts of Earnings*, 51 ACCT. REV. 244, 249–50 (1976).

[112] *See* sources cited *supra* note 111.

emerging-growth-company/venture-capitalist relationship. Because "crib death" is more likely to occur at the early stages of development, venture capitalists, to protect their investment, actively serve as experienced "overseers" of an emerging growth company's business plan and substantively participate in, and even control, major policymaking decisions.[113] For instance, prior to making an initial investment in an emerging growth company, it is common for venture capitalists to require the right to change its management[114] and often to mandate consultation with investors prior to the consummation of any major corporate decision.[115] Venture capitalists also may require operational covenants as well as informational covenants before making their initial capital investments.[116]

Thus, investment concessions demanded by venture capitalists may profoundly impact an emerging growth company's entire business plan. This particularly holds true during the early stages of an emerging company's development, when venture capitalists infuse sizeable amounts of start-up capital to ensure the birth and growth of an emerging company.[117] The perpetual threat of venture capitalists withholding additional funding for an emerging growth company's operations encourages management to conserve capital and exercise sound business judgment.[118] A refusal on the part of venture capitalists to appropriate additional funding signals to other investors that an emerging growth company represents a poor investment.[119] Therefore, by observing the staged capital process of the venture capitalists, other investors may discern the likely outcome of investing in a particular emerging growth company.

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[113] *See* Sahlman, *supra* note 12, at 141. Venture capitalists generally have veto power over any sale, merger, or reorganization. *See* Staebler & Harding, *supra* note 29, at 34. For instance, New Enterprise Associates (NEA), the leading venture capital firm in taking companies public in 1994, had partners or associates on the boards of seven of the companies it took public. *See* Paul D. Samuel, *New Enterprise Associates Leads Venture Capitalists in Total of IPOs*, DAILY REC., Mar. 7, 1995, § 1, at 3.

[114] *See* Staebler & Harding, *supra* note 30, at 32 (since management is untested, financiers in new companies generally require the ability to change management).

[115] *Id.* at 33.

[116] *Id.*

[117] Because of the high-risks associated with financing emerging growth companies, and their unique susceptibility to "crib death," venture capitalists stage capital in order to ensure not only comprehensive control over the entire business operation but over its sustenance as well. *See* sources cited *supra* note 29 and accompanying text.

[118] *Id.* at 141–42.

[119] *Id.* at 142.

Thus, when an emerging growth company issues public securities, at which time the potential for "crib death" is at its highest,[120] venture capitalists have already substantively participated in developing the most vital aspects of that company's business plan.[121] Moreover, venture capitalists, who already hold a significant investment in the emerging growth company, largely govern the decision of whether to issue public securities in the first place.[122] An emerging growth company's decision to issue public securities should be understood by other investors as a rational business decision reached through the advice and consultation of venture capitalists who are sophisticated investors with direct information about the company's business plan.

Therefore, in view of the emerging-growth-company/venture-capitalist relationship, investors generally should presume that predictive statements are the result of a carefully designed comprehensive business plan, which is the culmination of information gathered and evaluated by the emerging growth company and its venture capitalist investors. Predictive statements are merely announcements concerning aspects of an emerging growth company's business plan that have been reviewed and often spearheaded by venture capitalists. Indeed, predictive statements are the cheapest and quickest way to disseminate information about an emerging growth company and provide potential investors with the chance to examine an investment opportunity that has already received a stamp of approval from sophisticated investors.[123]

Predictive statements should be encouraged by providing a safe harbor that induces emerging growth companies to share relevant information with investors rather than hiding it solely to avoid potential liability. Projections by emerging growth companies are more reliable than analysts' projections. Furthermore,

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[120] Emerging companies are also at risk because of the enormous expenses in planning and issuing an initial public offering. *See, e.g.*, Douglas A. Tanner, *Cost Effectiveness and Legal Compliance: An Analysis of Securities Law Compliance for the Start-Up Company*, 2 COMPUTER & HIGH-TECH. L.J. 69, 74 (1986) (arguing that federal registration costs are prohibitively high).

[121] *See, e.g.*, Ian Ayres & Peter Cramton, *Relational Investing and Agency Theory*, 15 CARDOZO L. REV. 1033, 1063 (1994) (comparing the venture capitalist to a "relational investor," who invests more resources into acquiring information concerning the effectiveness of a company's management.). *See also infra* notes 122–123 and accompanying text.

[122] *See* Staebler & Harding, *supra* note 29, at 34 (venture capitalists often negotiate for the right to demand that the company sell its stock in an initial public offering).

[123] *See supra* notes 113–116 and accompanying text.

within high-technology industries these statements are commonly reviewed by venture capitalists before an emerging company goes public. In short, a safe harbor for predictive statements provides emerging growth companies with the proper incentives to offer investors exactly what they seek: material, nonpublic, inside information that allows them to make a fully informed investment decision.

V. CONGRESSIONAL PROPOSALS FOR SECURITIES LITIGATION REFORM

Several proposals have recently been introduced in the 104th Congress to reform private securities litigation.[124] Despite their differences, salient throughout each Congressional proposal is the calculated objective, both procedural and substantive, to inhibit nuisance litigation and the filing of meritless 10b-5 class actions suits. Indeed, a review of recent proposals for private securities litigation reform demonstrates Congress's resolve to end the use of 10b-5 solely for its nuisance value and effect.

A. *The House Bill: The Securities Litigation Reform Act*

Passed by the House of Representatives on March 8, 1995, H.R. 1058 (the "House Bill"), entitled the Securities Litigation Reform Act,[125] is intended specifically to preclude the use of 10b-5 for the sole purpose of bringing nuisance actions.[126] Moreover, the House Bill also seeks to encourage the dissemination of information to investors by excepting companies from liability for predictive statements made in good faith.[127] To accomplish this end, the House Bill, among other things, contains an indispensable provision for the safe harbor of predictive statements.

One of the major innovations of the House Bill is its provision for class action plaintiff steering committees.[128] Proposed for the

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[124] *See* H.R. 1058, 104th Cong., 1st Sess. (1995); S. 240, 104th Cong., 1st Sess. (1995); S. 667, 104th Cong., 1st Sess. (1995).

[125] H.R. 1058, 104th Cong., 1st Sess. (1995). The Securities Litigation Reform Act was introduced in the House by Rep. Thomas J. Bliley (R-Va.) on February 27, 1995.

[126] *See generally* 141 CONG. REC. H2760 (daily ed. Mar. 7, 1995) (statement of Rep. Bliley).

[127] *See id.*

[128] H.R. 1058, 104th Cong., 1st Sess. § 2 (1995). Under the plaintiff steering committee proposal, each member must meet minimum threshold requirements. Spe-

specific purpose of ensuring client control over the litigation strategy, this committee is to be primarily responsible for directing counsel on behalf of the class, in addition to accepting or rejecting offers of settlement.[129] Under the House Bill, the plaintiff steering committee does not preclude the right of nonmembers to appear and address the court on issues relating to either the organization or the actions of the committee.[130]

In addition, the House Bill would establish a heightened pleading standard and a more stringent burden of proof. The new pleading requirement, for instance, demands that plaintiffs assert explicitly each statement or omission that was misleading.[131] The House Bill thus requires each plaintiff to allege the specific basis establishing scienter for each named defendant.[132]

Furthermore, in proposing a more stringent burden of proof, the House Bill codifies existing case law concerning proof of reliance and causation by retaining the fraud-on-the-market principle.[133] Under the Bill, a plaintiff who claims damages by resort to fraud-on-the-market theory may only prove reliance and causation by first establishing proof that the securities were traded in a "liquid market,"[134] which is presumed to be a market that would reflect substantially all publicly available information regarding a particular security.[135] Pursuant to this provision, the plaintiff is entitled to a rebuttable presumption that the market's fraudulent misrepresentation was impounded into the stock price.[136]

The House Bill would also establish a new liability scheme for parties found guilty of securities fraud. Under its liability

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cifically, the plaintiff steering committee will consist of at least five class members who cumulatively held during the class period no less than five percent or $10,000,000 in market value of the securities in dispute. Despite the House Bill's expressed threshold requirements, the court nonetheless reserves the right to approve a smaller percentage or dollar amount if appropriate under the circumstances. *See id.* These minimum threshold requirements are intended to exclude "professional plaintiffs" from securities fraud actions. Generally, these plaintiffs possess broad securities portfolios that contain only a few securities of each publicly traded company. By spreading themselves throughout the securities market, "professional plaintiffs" are "on-call" to serve as the lead plaintiff in securities class action suits, and have been associated mainly with nuisance litigation. *See* Coffee, *supra* note 4, at 682.

[129] *See* H.R. 1058, 104th Cong., 1st Sess. § 2(a) (1995).

[130] *See id.*

[131] *See id.* § 4.

[132] *See id.*

[133] *See* sources cited *supra* note 26.

[134] H.R. 1058, 104th Cong., 1st Sess. § 4 (1995).

[135] Essentially, the House Bill adopts the semi-strong version of the Efficient Capital Markets Hypothesis (ECMH). *See* sources cited *supra* note 22.

[136] H.R. 1058, 104th Cong., 1st Sess. § 4 (1995).

provisions, joint and several liability would run when the defendant knowingly commits securities fraud.[137] If the trier of fact finds the defendant acted recklessly, the defendant is instead proportionately liable for damages.[138]

Most importantly, the House Bill also includes a necessary safe harbor provision for predictive statements. Under the Act, predictive statements cannot form the basis for liability provided these statements were not inaccurate at the time of their publication and included citations for their authority, along with a disclaimer admonishing that future projections should not be accorded any more weight than is reasonably justified under the circumstances.[139] Additionally, the safe harbor provision delegates regulatory authority to the SEC to prescribe rules and regulations that will facilitate the operation of the safe harbor provisions.[140]

B. *The Senate Proposal: The Private Securities Litigation Reform Act of 1995*

While the Senate's Private Securities Litigation Reform Act of 1995 (the "Senate Bill")[141] includes similar proposals,[142] it is the only Congressional proposal to date that includes salutary provisions for both nonbinding alternative dispute resolution (ADR) and safe harbor for predictive statements.[143] To date, the Private

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[137] *Id.* § 4(e).

[138] *See id.*

[139] *See id.* § 5. Under Section 5 of the House Bill, the establishment of a safe harbor for predictive statements would except from liability any forward-looking statement if the statement "contains a projection, estimate, or description of future events" and "refers clearly . . . to such projections, estimates, or descriptions as forward-looking statements," provided "the risk that such projections, estimates, or descriptions may not be realized." *Id.* It should further be noted that this safe harbor for predictive statements would operate in conjunction with any safe harbor that the SEC might establish by rule or regulation. *Id.*

[140] *Id.* The House Bill would permit the SEC to "include clear and objective guidance" and to "prescribe such guidance with sufficient particularity" so that compliance therewith would be readily ascertainable by issuers prior to the issuance of their securities. *Id.*

[141] S. 240, 104th Cong., 1st Sess. (1995). Introduced in the Senate on January 18, 1995, the Private Securities Litigation Reform Act of 1995 was sponsored by Senators Pete V. Domenici (R-N.M.) and Christopher J. Dodd (R-Conn.). *See also* 141 CONG. REC. S1075 (daily ed. Jan. 10, 1995) (statement of Sen. Domenici).

[142] *See* S. 240, 104th Cong., 1st Sess. §§ 101, 104, 203 (1995).

[143] *See id.* §§ 102, 201, respectively. Although Senate Bill 667, introduced on April 4, 1995 by Senators Richard H. Bryan (D-Nev.) and Richard Shelby (R-Ala.), contains a safe harbor provision for predictive statements, it does not provide for nonbinding ADR and therefore is not an optimal litigation reform measure. *See* S. 667, 104th

Securities Litigation Reform Act of 1995 is the only Congressional proposal that would maximize protections against "crib death" while not compromising the effective private enforcement of the federal securities laws.

Like the House Bill, the Senate Bill would eliminate a host of abusive practices in private securities fraud litigation. The Senate Bill forbids the receipt of referral fees paid for assisting an attorney in recruiting investors who have the specific intention of bringing a securities fraud action,[144] and prevents an attorney with a beneficial interest in the securities at issue from participating in the fraud action.[145] Moreover, the Senate Bill places a cap on the award of attorneys' fees by disallowing any amount in excess of a reasonable amount recovered by the class plus reasonable expenses.[146] The Senate Bill would also prohibit the payment of private plaintiffs' legal fees from SEC disgorgement pools.[147]

Similar to the House Bill, the Senate Bill's proposal for plaintiff steering committees is also intended to ensure client control over the litigation process. Upon its own motion or a motion by a member of the shareholder class, the court may appoint a committee of class members to direct counsel for the class.[148] For the committee to be certified, its combined membership must cumulatively hold the lesser of five percent of the securities in dispute with a market value of $10 million or if necessary a smaller amount as the court deems appropriate under the circumstances.[149] In cases where there is no motion to this effect, the court reserves the right to appoint a guardian *ad litem* who is responsible for directing counsel on behalf of the entire class.[150]

The Senate Bill would also heighten the pleading standard in securities fraud suits by requiring that plaintiffs allege specific facts relating to the state of mind of each defendant when the

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Cong., 1st Sess. (1995). For this reason, S. 240, which contains provisions for both nonbinding ADR and safe harbor for predictive statements, is the sole focus of this section.

[144] *See* S. 240, 104th Cong., 1st Sess. § 101 (1995).

[145] *See id.*

[146] *See id.* Regarding the payment of attorneys' fees from settlement funds, this section stipulates, in part, that "attorneys' fees awarded by the court to counsel for the class shall be determined as a percentage of the amount of damages and prejudgment interest actually paid to the class as a result of the attorneys' efforts." *Id.*

[147] *See id.*

[148] *See id.* § 103.

[149] *See id.*

[150] *See id.*

alleged violation occurred, in addition to specifying each misleading statement made by the defendant.[151] Essentially, this pleading provision requires the plaintiff to plead with particularity that the defendants had an intent to defraud or scienter.[152] Furthermore, the Senate Bill includes a named plaintiff threshold provision that requires that lead plaintiffs in class action suits own in the aggregate a certain value or percentage of the securities at issue. Under this provision, a plaintiff must establish ownership of either one percent or $10,000 in market value of the securities in dispute in order to obtain certification as a class representative.[153] This named plaintiff threshold requirement, like the House Bill's provision, may be similarly viewed as a deliberate attempt to suspend the use of "professional plaintiffs"[154] in securities fraud litigation.

Although the Senate Bill retains the existing joint and several liability scheme for defendants who are primary wrongdoers,[155] it establishes a new scheme of proportionate liability for those defendants found less culpable.[156]

The most significant feature of the Senate Bill is its provision affording either party the opportunity to request nonbinding alternative dispute resolution (ADR) at the outset of the securities suit.[157] The ADR provision stipulates that if either party refuses

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[151] *See id.* § 104. The bill provides that a plaintiff may recover damages for securities fraud "only on proof that the defendant acted with some level of intent," and if the plaintiff's complaint alleges "specific facts demonstrating the state of mind of each defendant at the time the alleged violation occurred." *Id.*

[152] *See id.* A prerequisite to a court's finding of scienter is the intent to defraud, or the mental state embracing an intent to deceive, manipulate, or defraud. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976).

[153] S. 240, 104th Cong., 1st Sess. § 101 (1995).

[154] "Professional plaintiffs" are essentially repeat lead plaintiffs in securities class action suits. Typically, "professional plaintiffs" receive incentive payments from attorneys for acting as class representatives and assuming various responsibilities on behalf of the class. *See generally* Andrew Leigh, *Being a Plaintiff Sometimes Amounts to a Profession*, INVESTOR'S BUS. DAILY, Nov. 1, 1991; Coffee, *Understanding the Plaintiff's Attorney*, *supra* note 4.

[155] *See* S. 240, 104th Cong., 1st Sess. § 203 (1995). The Senate bill also retains joint and several liability for defendants who substantially assisted primary wrongdoers or who knowingly engaged in fraudulent activities. *See id.*

[156] *See id.* Proportionate liability under the Senate bill is to be determined by the defendant's degree of responsibility. The damage amount is "[m]easured as a percentage of the total fault of all persons involved in the violation, of each person found to have caused or contributed to the damages incurred." *Id.* In determining the degree of responsibility, the trier of fact shall consider two factors: the nature of the conduct of each person and the nature and extent of the causal relationship between that conduct and the damage claimed. *See id.*

[157] *See id.* § 102. This section permits parties to nonbinding ADR to agree on the type of ADR to be applied. If the parties cannot reach agreement within 20 days after consenting to ADR, the court shall specify the type of ADR to be used. *See id.*

to proceed under ADR or refuses unreasonably to accept the results of ADR and that party eventually loses the securities suit in court, the court shall award costs including legal fees to the prevailing party, provided that the legal position of the losing party or the losing party's attorney was not "substantially justified."[158]

On the issue of damages, the Senate Bill's nonbinding ADR provisions makes concerted effort in protecting small investors who are named plaintiffs alleging securities fraud. In an effort to avoid "chilling" the private enforcement of the federal securities laws, the Senate Bill exempts any named plaintiff owning less than $1 million in securities from the assessment of court costs including legal fees, notwithstanding a court's finding that the securities fraud claim was not "substantially justified."[159] Primarily intended to protect the interests of small investors, this provision would effectively relieve small investors from the assessment of penalties for a failure to reasonably assert a substantial justification for fraud claims. At the same time, the provision limits opportunistic shareholders and lawyers, who already possess the sophistication and resources necessary to investigate thoroughly and justify a fraud claim, from bringing such claims absent substantial justification.[160]

The Senate Bill's safe harbor provision modifies current securities law governing predictive statements by allowing the defendant to move for summary judgment on whether Rule 175, the safe harbor exception, applies.[161] Notwithstanding current law, this safe harbor expands the rights of courts in assessing whether statements regarding the future economic performance of a par-

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[158] *See id.* Section 102 provides, in part, that upon the motion of the prevailing party made prior to the final judgment, the court shall award costs, including reasonable attorneys' fees against the losing litigant, if

> (a) the party unreasonably refuses to proceed pursuant to an alternative dispute resolution procedure, or refuses to accept the result of an alternative dispute resolution procedure;
>
> (b) final judgment is entered against the party; and
>
> (c) the party asserted a claim or defense in the action which was not substantially justified.

Id.

[159] *See id.*

[160] *See generally* Jeff Nesbit, *Lawyers Waging War on High-Tech Industry*, WASH. TIMES, Mar. 10, 1995, at B7.

[161] *See* S. 240, 104th Cong., 1st Sess. § 201 (1995). Rule 175, the current safe harbor regulation for predictive statements, provides that a forward-looking statement shall not be deemed a fraudulent statement unless it was made without a reasonable basis or was disclosed other than in good faith. *See* 17 C.F.R. §§ 230.175, 240.3b-6 (1994).

ticular company may justifiably form the basis for a securities fraud suit.[162] Moreover, the safe harbor provision would permit the SEC to develop rules and offer recommendations regarding the standards courts should apply when determining the merits of a defendant's summary judgment motion for a safe harbor exemption.[163]

VII. CONCLUSION

The 104th Congress has justifiably pursued inquiry into the detrimental effects of 10b-5 nuisance suits and their predominant role in the "crib death" of emerging companies. Due to the role of venture capitalists in spurring economic development, venture-backed emerging growth companies have recently become the source of new jobs, markets, and advanced technology.[164] Yet, because of the unique cost imbalance between plaintiff shareholders and emerging growth companies, the ubiquity of nuisance suits and meritless settlements render these companies ill-equipped to both manage business operations and wage frequent defenses to 10b-5 shareholder class action suits.

Congress must respond to the unique dilemma posed by the "crib death" of emerging growth companies by enacting private securities litigation measures that would inhibit the filing of nuisance suits. At the same time, these measures must also ensure investor confidence in the securities markets by affording adequate remedies for securities fraud. Since investors end up on both sides of the equation, Congress must bear in mind that

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[162] *See* S. 240, 104th Cong., 1st Sess. § 201 (1995). The bill grants courts the authority to rule whether a forward-looking statement was within the coverage of any SEC rules governing such statements. *See id.* The bill also grants courts the authority to restrict or extend discovery, in light of whether or not dilatory conduct or duplicative discovery has occurred. *See id.*

[163] *See id.* Considerations that the SEC may take into account include

(1) appropriate limits to liability for forward-looking statements;
(2) procedures for making a summary judgment determination of the applicability of any Commission rule for forward-looking statements early in a judicial proceeding to limit protracted litigation and expansive discovery;
(3) incorporating and reflecting the scienter requirements applicable to implied private actions under section 10(b); and
(4) providing clear guidance to issuers of securities and the judiciary.

Id.

[164] *See generally* NATIONAL VENTURE CAPITAL ASSOCIATION ET AL., FIFTH ANNUAL ECONOMIC IMPACT OF VENTURE CAPITAL STUDY (1995) (summarizing the monumental economic impact of venture capital-backed companies between 1989 and 1993, during which time each of the companies surveyed, on average, created 152 new jobs, invested $8.7 million in R & D, and generated $4 million in exports per company).

the long-term financial interests of both emerging companies and shareholders are inextricably linked to the resolution of the "crib death" phenomenon.

In the interests of both emerging growth companies and investors, provisions for nonbinding ADR and safe harbor for predictive statements must be incorporated into any Congressional enactment affecting private securities litigation. The Senate Bill, which contains provisions for both nonbinding ADR and safe harbor for predictive statements, squarely accounts for the magnitude of the "crib death" problem without sacrificing the private causes of action necessary to deter securities fraud. In full view, both emerging companies and shareholders would reap the benefits, both legal and economic, from reform measures that include provisions for nonbinding ADR and the safe harbor of predictive statements.

Emerging companies and venture capitalists are an integral part of continued economic stability. It is appropriate for Congress to act responsibly and enact private securities litigation reforms that would effectively cure "crib death," thereby protecting new jobs, new markets, and technological advancement.

RECENT DEVELOPMENTS

CAN THE IRS MAINTAIN THE DEBT-EQUITY DISTINCTION IN THE FACE OF STRUCTURED NOTES?

> "There's glory for you!"
> "I don't know what you mean by 'glory'," Alice said.
> "I meant 'there's a nice knock-down argument for you!'"
> "But 'glory' doesn't mean 'a nice knock-down argument'," Alice objected.
> "When *I* use a word," Humpty Dumpty said in a rather scornful tone, "it means just what I choose it to mean—neither more nor less."[1]

For many years, tax policymakers and academics have contemplated the proper tax treatment of convertible debt and bond-warrant packages, two of the simplest and earliest forms of what are now called "structured notes."[2] However, structured notes today are far more complicated than "plain vanilla" convertibles or investment units. These financial instruments involve often complex packages of financial flows and risks that can be viewed as either "debt" or "equity" and that may change over the life of the instrument. Because the tax treatment of debt and equity differs, the characterization of these hybrid instruments can have significant tax effects.

Congress, through the Internal Revenue Code (Code) and the Internal Revenue Service (Service) faces three basic policy choices in the taxation of structured notes. First, under a "wait and see" approach, the Service would assess tax only on noncontingent elements of the financial instrument until the contingency embedded in the instrument occurs. Second, under a "bifurcation" approach, the Service would attempt to bifurcate the instrument into its noncontingent and contingent debt and equity components. Finally, under an "integration" approach, the Service might treat a number of financial instruments with offsetting risk and

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[1] LEWIS CARROLL, THROUGH THE LOOKING-GLASS (1872), quoted in THE OXFORD DICTIONARY OF QUOTATIONS (Angela Patterson ed.) (4th ed. 1992) at 183.

[2] The current federal corporate income tax presents three sets of categorical issues. First, character issues arise because the taxpayer or tax policymaker must determine whether a particular item of income or expense is ordinary or capital and whether it is attributable to debt or equity. Second, timing issues, determining in which taxable year the income or deduction arises, affect the amount of taxes owed. Finally, source issues, questioning which nation's taxing authority should have the ability to tax a given item of income or must allow a particular deduction, arise in firms that earn income in more than one country. *See* Edward Kleinbard, *Beyond Good and Evil Debt (and Debt Hedges): A Cost of Capital Allowance System*, 1989 TAXES 943, 946.

yield effects (often referred to as "hedges") as one hybrid instrument.

Until recently, the Service has opted for either the "wait and see" or "bifurcation" approaches, trying to analogize new financial instruments to packages of traditional financial instruments for which tax rules are well defined. However, structured notes expose both the inability of the Service to keep apace of financial innovation and the inherent weaknesses of the Service's current policy of reasoning by analogy to traditional hybrid forms. Structured notes further blur the distinction between debt and equity, and the Service has provided no guidance on whether new forms of structured finance are debt or equity. Investors and issuers alike appear to be exploiting an opportunity to employ Humpty Dumpty as their tax advisor, making the words "debt" and "equity" mean whatever they choose while the Service scrambles to decipher the true character of their transactions. At bottom, the explosive growth of the structured note market may highlight the need to do away with the differences in the tax treatment of debt and equity.

I. THE DEVELOPMENT OF STRUCTURED NOTES

Corporations have issued debt-equity hybrids similar to what are now called structured notes for years. For example, in 1968, Loew's Theaters acquired Lorillard Corporation, offering each stockholder a package of bonds and options on Loew's common stock.[3] However, in recent years, the volume and variety of debt-equity hybrids have proliferated,[4] and an increasing number of issuers have pegged returns on the equity-flavored portion of such hybrids to indices or securities other than the issuer's.[5]

Although structured notes raise both timing issues and, in the case of structured notes linked to foreign currency, source issues, this Recent Development focuses on the character issues common to all forms of structured notes.

[3] This example was drawn from RICHARD BREALEY & STEWART MYERS, PRINCIPLES OF CORPORATE FINANCE, 524–25 (2d international student ed. 1984).

[4] According to one recent report, "Experts say close to $50 billion in structured notes was issued by companies in 1993 alone . . . ." Kelley Holland et al., *A Black Hole in the Balance Sheet*, BUS. WK., May 16, 1994, at 81.

[5] Even this development is not entirely novel. Debt convertible into stock of a company other than the issuer is known as "exchangeable debt" and, historically, has been governed by tax rules different from those for convertible debt. *See* Rev. Rul. 69-135, 1969-1 C.B. 198 (Unlike conversions of convertible debt, conversions of exchangeable debt are realization events under § 1001.).

A. *Two Building Blocks of Structured Finance*

Structured notes have their roots in convertible bonds and bond-warrant packages, often termed "investment units."[6] Convertible bonds allow holders an option to convert their security to a fixed number of shares at any time during the life of the bond. For example, XYZ Corporation may issue a fifteen-year bond for $1,000, convertible at the option of the bond holder into twenty shares of stock. The bond holder will find it worthwhile to convert her bond if the price of XYZ shares exceeds $50. In essence, what the bond holder has received is an XYZ bond *and* a call option on the XYZ stock.[7] Financial economists value a convertible bond by calculating the bond value and then adding the value of the conversion option.[8]

Unlike holders of convertible bonds, holders of investment units need not give up their rights as debt holders in order to exercise their warrants. Analysts typically value an investment unit by bifurcating the unit into its component bond and option, which is valued under the Black-Scholes formula.[9] For example, in 1972, Texas Instruments (TI) sold investment units consisting of one twenty-year, 7.75% subordinated debenture and fifteen warrants exerciseable before January, 1978, at $32.75, 13% above the market price of $29. The market price of the unit was $1,000.[10] Analysts would value the components by determining at what value the bond alone would trade in the market and then value the options based on their volatility and the expected value of interest rates.[11]

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[6] *See generally* BREALEY & MYERS, *supra* note 3, at 524–40 (referring to the use of both forms of securities in the 1970s and discussing the valuation of each).

[7] A call option is the right to purchase a financial interest at a specified price on or before a certain date. A put option is the right to sell a financial instrument at a specified price on or before a certain date.

[8] *See generally* BREALEY & MYERS, *supra* note 3, at 531.

[9] *Id.* at 524–25.

[10] *Id.* at 524.

[11] In the TI issue, the units were immediately separable and the bonds sold for $980 shortly after issue. Thus, the warrants must have been worth $1.33 each ($20 divided by 15 warrants) at issue. *Id.*

B. *Through the Looking-Glass: The Inverse Floater, Embedded Options, and Equity-Linked Notes*

The new breed of structured finance differs in several ways from the two building blocks described above. First, many newly issued structured notes contain embedded options on securities or indices other than those controlled by the issuer. Second, a number of new issues combine the legal structure of debt with contingent payments based on an option or a stock index that causes the instrument to mimic returns on a stock or portfolio of stocks. As Parts II and III will explain, these structures raise serious questions about the debt-equity distinction. Both of these features make the returns on the new structured notes more volatile than those on traditional convertible bonds or investment units.[12]

Finally, the explosive growth in the structured note market and the proliferation of highly tailored note structures may have impeded the development of an orderly, liquid secondary market in such securities.[13] In fact, the variety of structures makes it difficult even to describe the current activity in the structured notes market. However, three examples will serve to illustrate most of the major tax issues associated with structured notes.

1. The Inverse Floater

An inverse floater is a note on which the return is set at a fixed rate minus some variable rate. It is "inverse" in the sense of having returns that vary oppositely from the variable interest rate selected. For example, CIT Group (a joint venture of Chemical Bank and Dai-Ichi Kangyo Bank) recently borrowed $25 million at an interest rate set at 13.5% minus the three-month Italian interbank rate, which varies.[14] The CIT Group then hedged its position by entering into a swap, paying Chase Manhattan fixed

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[12] This increased volatility is probably best illustrated by Orange County, California's recent bankruptcy filing, discussed *infra*, note 18. It also has led one tax wag to define derivatives as "absolutely any financial contract on which your client has lost money." Briggs Adams, *Seminar Experts Define Derivatives in 25 Words—Or More*, CHI. LAW., Dec. 1994, at 66 (quoting Louis B. Freeman of Sonnenschien, Nash & Rosenthal).

[13] This concern recently led the SEC to deem five types of floating-rate securities, including inverse floaters (discussed *infra*, text accompanying notes 14–25), too risky to be held by money market funds. *See SEC Rule Could Put Securities Up for Grabs*, FORT LAUDERDALE SUN-SENTINEL, July 11, 1994, at D3. Money market funds currently hold some $4.5 billion in structured notes. *Id.*

[14] *See* Holland, *supra* note 4, at 82.

payments of twenty-two basis points[15] over Treasuries in exchange for payments mirroring those CIT owed its lender, saving eighteen basis points over the price of an ordinary Treasury-rate-based borrowing.[16]

However, it is worth considering the nature of the risk taken by CIT's investor, or counterparty. If the three-month Italian interbank rate rises above 13.5%, the investor receives no interest. Moreover, unlike the typical lender of floating-rate funds, CIT's investor loses when interest rates rise.[17] At first blush, the risk assumed by CIT's investor resembles that assumed by a fixed-rate bond holder; as interest rates rise, the market value of the instrument (as measured by its present value) declines. However, unlike the bond holder, CIT's investor also experiences a decline in annual yield, thus accelerating the decline in the market value of the investment.

In fact, CIT's investor faces the same risks with the inverse floater as if operating a business that generated a constant stream of operating revenues and financed operations with funds borrowed at the Italian interbank rate. This hypothetical business owner would have annual operating revenues of $3.38 million (13.5% return on $25 million in assets) and would pay interest equal to the three-month Italian interbank rate on $25 million in financing. Given this equivalence, it is difficult to say whether CIT has issued debt or equity.[18]

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[15] A "basis point" is one one-hundredth of a percentage point. For example, 22 basis points equals 0.22%.

[16] *See* Holland, *supra* note 4, at 82.

[17] Although fixed-rate bond holders face declines in the market price of their investments as interest rates rise, holders of floating-rate bonds earn additional income from the investments that offset the usual effect of interest rates on the market price. In contrast, as shown below, CIT's investor loses value on both principal and interest as interest rates fall.

Yield to CIT's Investor at Varying Interest Rates
(Dollars in millions)

Interbank Rate	Annual Yield	Present Value (PV) of Annuity	PV Principal	Total PV
1.0%	3.13	12.21	24.03	36.24
5.0%	2.13	7.55	21.60	29.15
10.0%	0.88	2.79	17.08	19.87
13.5%	0	0	15.05	15.05
15.0%	0	0	14.30	14.30

For purposes of illustration, the table makes two assumptions. First, that the term of CIT's inverse floater is five years. Second, the values shown reflect the investor's position at the end of the first year after it enters the inverse floater, assuming that expected interbank rates will remain constant for the remainder of the investment term.

[18] Recent reports that Orange County, California, has lost huge sums on structured

2. The Embedded Option

Unlike traditional investment units, new structured notes with embedded options frequently offer such options on stock, interest, or commodity indices rather than on the underlying stock of the issuer. For example, in May 1994, American General Finance (AGF) considered an issue of derivative-embedded structured notes, in which it would issue a package of debt plus index options.[19] AGF estimated that it could save twenty to twenty-five basis points over the cost of a traditional financing and planned to hedge any index risks.[20]

Professor Alvin C. Warren provides a more concrete example involving a "stock index growth note" (SIGN). The SIGN has a $1,000 stated indebtedness and at the end of five years will return to the investor her $1,000 plus $1,000 multiplied by the percentage increase in the Standard & Poor's Index of 500 stocks (S&P 500).[21]

As with the inverse floater, it is worth examining the character of the risk assumed by an investor in SIGNs. On its face, the SIGN resembles a package consisting of a $1,000 zero coupon bond and a call option on the growth in the S&P 500 index. However, one could recharacterize the SIGN as effectively amounting to a block of synthetic stock in an entity called the S&P 500 and the right to put that stock for a minimum of $1,000 at the end of the fifth year after issue. This dual character of the SIGN challenges a tax regime based on categorical distinctions and rules.

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notes provide another vivid example of the equity-like risks and volatility assumed by investors in structured notes. Orange County invested $8 billion in county funds and some $12 billion in borrowings in a portfolio heavily weighted towards inverse floaters. Leslie Wayne, *Big County is Facing Huge Loss: Orange, Calif., Hurt as Derivatives Drop*, N.Y. TIMES, Dec. 13, 1994, at A1. By August 1994, Orange County held $5.7 billion in structured notes that would lose value as interest rates rise. *Id.* at D16. Recent rises in interest rates caused Orange County's heavily leveraged portfolio to drop in value by an estimated $2 billion. Seth Mydans, *Orange County's Prosperity Seems Dented, Not Undone*, N.Y. TIMES, Dec. 13, 1994, at A1.

[19] *American General Mulls Structured Notes*, INSTITUTIONAL INVESTOR, May 23, 1994, at 6.

[20] *Id.*

[21] Alvin C. Warren, Jr., *Financial Contract Innovation and Income Tax Policy*, 107 HARV. L. REV. 460, 483–86 (1993). Warren's example is based on a 1991 offering by the Republic of Austria. *Id.* at 483, n.91.

3. Equity-Linked Notes

Like SIGNs, equity-linked notes offer investors an opportunity to earn income based on the performance of an underlying equity security. However, unlike SIGNs, most such issues pay a fixed, periodic return analogous to dividends during the life of the instruments, and the repayment of principal is linked to the performance of a stock or index.

For example, a "preferred equity redemption cumulative stock" (PERC) issue on Sears common stock promised the holder annual dividends of $3.75 between 1992 and the termination of the issue on April 1, 1995.[22] At the end of the PERC's life, the principal will be converted into common stock, with the conversion ratio determined by the trading price of Sears common stock on April 1, 1995.[23] The Sears PERC holders will receive a maximum of 1.3525 common shares for each PERC if the price of Sears common stock is trading at $43.63 or less, and a minimum of one common share for each PERC if the Sears common stock is trading at $59 or more.[24] In one sense, the PERC holder has a bond plus a call option on Sears stock with its value determined on a sliding scale. As with the SIGN, however, one could recharacterize the instrument as an effective investment in Sears common stock over the life of the PERC with a right to put the shares for a minimum dollar value of Sears shares at the PERC's end.

Although PERCs and SIGNs characterize interest and principal differently, investors face similar risks in either instrument. The characterization of those risks as "debt" or "equity" lies in the eyes of the (be)holder (and perhaps the issuer or the Service).

C. *Why Issue Structured Notes?*

Issuers of structured notes expect savings of about twenty basis points when compared with traditional financing.[25] Most appear to hedge any position risk associated with the equity-fla-

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[22] Robert H. Stovall, *Hedged Trading Strategies Via Percs*, FIN. WORLD, Dec. 6, 1994, at 124.

[23] *Id.*

[24] *Id.*

[25] *See* Holland, *supra* note 4, at 82

vored elements of the notes. Moreover, some closely held corporations may view structured note issues as a way to attract investors seeking equity-like returns without diluting control of the business.[26] The deductibility of the "interest" component of structured note packages creates a tax benefit on what the market might view as essentially an equity security, and this benefit drives a significant portion of the issuers' expected savings.

Investors appear to be attracted to the potential for customizing their risk exposure, the ability of structured notes to mimic returns from equity instruments that the investor may be restricted from holding, and, arguably, to the tax-driven premium paid by the issuer. In addition, under the 1986 regulations for contingent debt, structured notes offered an opportunity for investors to defer tax on their returns until the end of the instrument's life.[27]

Finally, it is worth noting that many structured notes transactions take advantage of asymmetries in tax status. Current tax rules, while often somewhat arbitrary, at least provide symmetry between issuer and investor treatment. If the investor gets to defer its gain, then the issuer must defer taking its interest deduction. If gain is capital to the investor, then the issuer may not deduct the payments made to the investor. But this symmetry does not include entities such as tax-exempt organizations and foreigners or broker-dealers covered by Section 475, under which all of their transactions in certain classes of financial instruments give rise to ordinary income or loss. Asymmetries such as these open the potential for tax-motivated structures in financing. For example, since a U.S. tax-exempt entity such as a foreign government does not need interest expense deductions and, thus, is indifferent to when they arise, it might willingly aid investors in developing a financing structure taking maximum advantage of deferral opportunities. In fact, the opportunity presented by the 1986 regulations for the investor to defer gain on an instrument issued by a tax-neutral issuer may have motivated Austria's SIGN issue.

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[26] Kevin Muehking, *The Discreet Charms of Private Placements*, INSTITUTIONAL INVESTOR, Nov. 1991, at 123.

[27] For a complete discussion, see *infra* part II.B.1.

II. Tax Treatment of Structured Notes Under Current Law

To understand or predict the Service's treatment of structured notes, it is useful to return to the two building block instruments discussed earlier, convertible debt and investment units.

Traditionally, the Service treats convertible debt as pure debt until conversion, at which time the investment becomes one in pure equity.[28] As one leading treatise states, "In effect, until conversion, debt genes are treated as dominant and equity genes are treated as recessive."[29] Conversion into the stock of the *issuing* corporation is not taxed,[30] because there is no true realization event on the investment package, or because the "open" nature of the transaction precludes current recognition. Of course, the issuing corporation receives the bonds and any additional payment for the stock tax-free.[31] In contrast, conversion into the stock of a corporation other than the issuer (an "exchangeable bond") is taxable to the investor.[32]

The tax treatment of investment units can be considerably more complicated.[33] Unlike convertible debt, investment units are bifurcated into their debt and equity components prior to any exercise of the equity option. The original issue discount (OID) rules require that the issue price of the investment unit be allocated between the debt and the option in accordance with their relative values.[34] Original issue discount income can arise if the issue price attributable to the debt portion is less than its face value. Moreover, OID income attributable to a taxable year is taxed in that year (and may be deducted as interest expense by the issuer) regardless of whether it is actually paid or received.

As the volume and variety of structured notes has ballooned, the Service has responded with two basic approaches based on

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[28] *See* Treas. Reg. § 1.1244(c)-1(b) (convertible debt cannot count as § 1244 stock); Rev. Rul. 69-91, 1969-1 C.B. 106 (convertible debt is not stock before conversion); *see generally* Boris I. Bittker & James S. Eustice, Federal Income Tax of Corporations and Shareholders ¶¶ 4.60–.62 (6th ed. 1994).

[29] Bittker & Eustice, *supra* note 28, at ¶ 4.60[1], 4-100.

[30] *See* Rev. Rul. 72-265, 1972-1 C.B. 222.

[31] *See* I.R.C. § 1032. (Subsequent references omit "I.R.C.")

[32] *See* Rev. Rul. 69-135, 1969-1 C.B. 198 (holding such an exchange taxable under the general principles of § 1001).

[33] *See generally* Emile Pesiri, *Untangling the Warrant Web*, 23 Tax Notes 525 (1984).

[34] § 1273(c).

the historical building blocks. Each is described in more detail below.

A. *Variable Rate Debt Instruments: Ignoring Debt-Equity Problems in the Name of Simplicity*

Recently adopted final regulations for "variable rate debt instruments" (VRDI)[35] take the approach of establishing a set of tax pigeonholes for several types of floating rate debt, which then are treated essentially as pure debt instruments and not subject to bifurcation.[36] These regulations apply to debt on which the stated interest varies in accordance with a series of one or more "qualified floating rates" or with a "single objective rate."[37] In fact, even an inverse floater qualifies as a VRDI so long as its returns vary as the inverse of a qualified floating or objective rate.[38]

Once an instrument is classified as a VRDI, the instrument is subject to the OID rules. The investor accrues interest income on the note each year at the most recent value of the qualified floating rate and the investor can take a corresponding interest expense deduction.[39] When such instruments have a secondary market, capital gain or loss on resale of the instruments is measured against a basis that includes the amount of OID income previously recognized by the investor.[40]

In essence, this approach treats debt with returns that vary only in accordance with a qualified floating rate as not having a contingent component. Moreover, the VRDI regulations may be overinclusive, because they appear to grant debt treatment to instruments such as the inverse floater with arguably equity-like returns.[41]

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[35] Treas. Reg. § 1.1275-5 (adopted Jan. 27, 1994).

[36] For a detailed discussion of the VRDI regulations as they stood in proposed form, see DAVID HARITON, FEDERAL INCOME TAXATION OF DEBT INSTRUMENTS 111-26.1 (Supp. 1993). Since the final regulations made relatively few changes to the 1992 proposal, Hariton's discussion remains an invaluable guide.

[37] Treas. Reg. § 1.1275-5(a)(3), (4).

[38] Treas. Reg. §§ 1.1275-5(c)(3), -5(d) (example 9).

[39] §§ 1275(a), 1272(a).

[40] § 1272(d)(2).

[41] Although Hariton calls the expansion of the initial VRDI proposed regulations to embrace inverse floaters "sound tax policy," he does not address the debt-equity classification issues raised by such treatment. HARITON, *supra* note 36, at 116.

B. *Contingent Debt Instruments: The Search for "Better" Bifurcation*

The search for rules governing so-called "contingent debt instruments" has been tortuous. Although Section 1275 permits the Service to prescribe regulations for contingent debt to ensure that the tax treatment of such instruments conforms with the OID approach,[42] the Service has failed in its first three attempts to issue final regulations with respect to contingent payments.[43] In December 1994, the Service issued its most recent proposed regulations on contingent debt instruments.[44] However, given the dismal history of the Service's previous attempts to regulate contingent debt, investors and issuers are unlikely to rely on these rules until they are made final.[45]

1. The 1986 Proposed Regulations: "Wait and See"

In its 1986 proposed regulations, the Service announced an approach that would treat all contingent payments in excess of the issue price as interest but would not tax any such payments until the year in which the payment amount becomes fixed.[46] Non-contingent portions would be segregated and treated according to ordinary interest and OID rules.[47] The proposed regulations took no position on when a contingent payment instrument would be classified as debt or equity.[48] Moreover, the proposed regulations did not define "contingent payment" but rather merely excluded contingencies based on insolvency or default and apparent contingencies that fit the definitions of the VRDI regulations.[49]

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[42] § 1275(d).

[43] For a tracing of this dismal history and a description of all three approaches, see HARITON, *supra* note 36, at 127-82.14.

[44] Prop. Treas. Reg. § 1.1275-4, 59 Fed. Reg. 64,884 (Dec. 16, 1994) *reprinted in IRS Issues Proposed Regs on Contingent Payment Debt Instruments*, 94 TAX NOTES TODAY 246-9 (Dec. 15, 1994) (available in LEXIS; TNT file) [hereinafter 1994 Proposed Regs].

[45] Edward D. Kleinbard, S. Douglas Borisky, & Rekha Vemireddy, *Proposed Regulations Affecting Contingent Payment Debt Obligations*, 66 TAX NOTES 723, 724–25 (Jan. 30, 1995).

[46] Prop. Treas. Reg. § 1.1275-4(e)(2), 51 Fed. Reg. 12022 (1986) [hereinafter 1986 Proposed Regs].

[47] 1986 Proposed Regs § 1.1275-4(f)(2).

[48] 1986 Proposed Regs § 1.1275-4(a).

[49] 1986 Proposed Regs § 1.1275-4(b); *see also* HARITON, *supra* note 36, at 129.

Because *all* tax on the contingent payments would be deferred until the payments became fixed, this regime would have offered substantial timing advantages to investors on the contingent portion of these instruments when compared with the OID rules governing the non-contingent payments. One would expect this timing advantage to be offset by the issuer's delayed ability to deduct the contingent interest paid. However, combinations of tax-neutral (e.g., foreign or domestic tax-exempt) issuers and tax-sensitive investors could capitalize on this deferral opportunity.

2. The 1991 Proposed Regulations: Steps Toward Bifurcation

In its 1991 proposed regulations, the Service modified its bifurcation approach to contingent debt. While the non-contingent portion of such instruments would still be subject to the ordinary interest and OID regime,[50] any part of the contingent portion determined by reference to "publicly traded property" would be treated as an option or other property right.[51] However, the 1991 proposal left a loophole for contingencies based on the value of property that is not publicly traded, granting such contingencies the deferral treatment of the 1986 proposed regulations.[52] One commentator argued that "if the bifurcation approach is to be retained, it should apply universally, and the regulations should simply state that any contingent obligation would be split into a noncontingent debt instrument and one or more property rights in accordance with the designation of the parties."[53]

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[50] Prop. Treas. Reg. § 1.1275-4(g)(3), 56 Fed. Reg. 8308 (1991) [hereinafter 1991 Proposed Regs].

[51] 1991 Proposed Regs § 1.1275-4(g)(2)–(4). However, the Service was careful to except, at least for the moment, traditional convertible bonds from such treatment, leaving untouched long-standing rules treating conversion of such instruments as a tax-free event. *See* 56 Fed. Reg. 8308 (1991) (preamble), *cited in* Edward D. Kleinbard, *Equity Derivative Products: Financial Innovation's Newest Challenge to the Tax System*, 69 TEX. L. REV. 1319, 1356 n.105 (1991).

[52] At least one corporation, Disney, attempted to take advantage of this loophole, issuing contingent payment obligations tied to the future performance of its television productions. *See* Tom Pratt, *Disney Plans Hybrid Zeros with Play on TV Business: Merrill to Sell the Deal on Best Efforts*, INVESTMENT DEALERS' DIG., Oct. 21, 1991, at 18.

[53] HARITON, *supra* note 36, at 182.2. Hariton's suggestion would lead to the accrual of OID at least on the noncontingent portion of an instrument with contingencies based on nonpublicly traded property, thus reducing one deferral opportunity inherent in the Disney proposed offering. *Compare id. with* 1994 Proposed Regs, discussed *infra* part II.B.4.

3. The Withdrawn 1992 Regulations: Bifurcation with Accrual

To prevent the deferral opportunity inherent in the 1986 proposal and harmonize the disparity between differing types of contingencies in the 1991 proposal, the Service revised its approach in late 1992. (This proposal was withdrawn by the Clinton Administration as part of a comprehensive review of regulations drafted by the Bush Administration.)[54] The 1992 proposal would have replaced both the 1986 and 1991 proposals with a system based on OID-like accruals for both contingent and noncontingent components of contingent debt without reference to whether the contingency is based on a publicly traded asset.[55] Taxpayers would have been able to choose from among seven different methods of accruing contingent and noncontingent income.[56]

4. The 1994 Proposed Regulations: Bifurcation, Accrual, *and* Integration

In December 1994, the Service formally proposed a simplified version of the withdrawn 1992 regulations. Although the current proposal still aims to tax accrued income on contingent debts and avoid the deferral opportunity of the "wait and see" approach, it reduces taxpayers' choices among accrual methods.

First, if the contingent debt instrument is issued for money or "publicly traded property," the issuer must prepare a projected payment schedule based on a forecast of likely contingent payments.[57] If the contingency is based on "quotable" property, then the contingency is valued at the forward price of a similar right or at the spot price of such a right plus interest at the applicable federal rate.[58] If the contingency is based on "nonquotable" property, then the issuer must project the yield of the contingent payment and select a projected payment schedule corresponding to that yield.[59] Once the payment schedule is projected, the

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[54] *See id.* at 128; *see also OMB Memo to Withhold Publication of Federal Regulations Affects Two IRS Proposed Regulations*, 93 TAX NOTES TODAY 19-13 (Jan. 27, 1993) *available in* LEXIS, Fedtax/TNT file.

[55] *See generally Proposed Regs Cover Treatment of Contingent Payment Debt Instruments*, 93 TAX NOTES TODAY 15-13 (Jan. 22, 1993) *available in* LEXIS, Fedtax/TNT file.

[56] *Id.*

[57] 1994 Proposed Regs § 1.1275-4(b).

[58] 1994 Proposed Regs § 1.1275-4(b)(4)(i)(A).

[59] 1994 Proposed Regs § 1.1275-4(b)(4)(ii).

issuer applies OID principles to accrue interest into each taxable year during the life of the instrument.

If actual payments differ from the projections, "positive adjustments" (when actual interest exceeds projections) are taxed as additional ordinary income when received[60] and "negative adjustments" (when projections exceed actual interest) either reduce the investor's interest income, create an ordinary loss, or reduce the amount realized on sale or retirement of the instrument.[61] To prevent holders of contingent debt instruments from converting OID interest income into capital gains by selling their instruments, the proposal would treat gains on sales of still-contingent instruments as ordinary income.[62]

Second, in contrast, if the contingent debt instrument is not issued for publicly traded property, the 1994 proposed regulations would first bifurcate the instrument into its contingent and noncontingent components.[63] The contingent instrument would be taxed separately as an OID debt instrument,[64] and the noncontingent component would be further bifurcated into principal and interest components and treated as a "plain vanilla" bond.[65]

Finally, the 1994 proposals include an opportunity for some issuers to elect integrated treatment of their transactions.[66] An issuer may integrate a "qualifying debt instrument" with another instrument or instruments used to hedge the risks of the qualifying debt instrument and treat the combination as a single "synthetic debt instrument."[67] For example, under the proposal, CIT would be able to integrate the inverse floater it issued with the interest rate swap it used to to hedge its exposure to the Italian interbank rate.[68] The resulting synthetic debt instrument would be treated as a VRDI yielding twenty-two basis points over the Treasury rate.

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[60] 1994 Proposed Regs § 1.1275-4(b)(6)(ii).
[61] 1994 Proposed Regs § 1.1275-4(b)(6)(iii).
[62] 1994 Proposed Regs § 1.1275-4(b)(8).
[63] 1994 Proposed Regs § 1.1275-4(c).
[64] 1994 Proposed Regs § 1.1275-4(c)(3).
[65] 1994 Proposed Regs § 1.1275-4(c)(4).
[66] 1994 Proposed Regs § 1.1275-6.
[67] 1994 Proposed Regs § 1.1275-6(a), (b)(4). To do so, the issuer must identify the instruments composing the synthetic security in advance. 1994 Proposed Regs § 1.1275-6(f). However, the proposal permits issuers to issue one security and later elect to hedge ("legging in") and to sell off one instrument in the package comprising the synthetic security without selling the others ("legging out"). 1994 Proposed Regs § 1.1275-6(d). Once an issuer legs out of a hedge, its remaining instruments are taxed separately. *Id.*
[68] *See* part I.B.1, *supra* text accompanying notes 14–18.

C. *Taxing the Inverse Floater, the SIGN, and the PERC Under Current Law*

As long as an inverse floater is based on a "qualified floating rate," its tax treatment will be determined by the VRDI rules. Investors will receive ordinary interest income, and payments made on the instruments will be deductible to the issuer, even if the returns on the instruments could be characterized as either equity or debt. Even if the instrument involved a series of rates, it could be treated as variable rate debt, provided that each rate would qualify individually.[69]

Current law treats both SIGNs and PERCs as contingent debt instruments. Unfortunately, the precise tax status of such instruments has been left unclear by the Service's multiple attempts at regulation.[70] Until recently, the 1991 proposed regulations provided the most persuasive authority for tax planners. Under those rules, the fixed repayment portion of the SIGN is treated as a zero coupon bond. The investor accrues OID income over the life of the SIGN, and the issuer may take a corresponding interest deduction, despite not having to pay out any cash until the SIGN matures.[71] The S&P 500-contingent portion of the SIGN is taxed as a cash-settled five-year option on the S&P 500 index, with a basis equal to the excess of the purchase price of the sign over the value of the zero coupon component.

The 1994 proposed regulations include as an example a version of the SIGN.[72] The example explains that the payment schedule would be the fixed payment at maturity ($1,000) plus the projected amount payable on the S&P 500 option. If there is a five-year forward price on the option, the issuer should use that price to construct the payment schedule. If there is no forward price, the issuer should take the current price compounded at the applicable federal rate of interest from the issue date until maturity. The entire payment schedule is then subject to the OID rules, requiring income to be accrued throughout the life of the SIGN.

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[69] Treas. Reg. § 1.1275-5(e)(3).

[70] Because there is substantial uncertainty about the persuasive authority of any of the Service's attempts to regulate contingent debt, *see supra* text accompanying note 43, this section will focus on tax treatment under both the 1991 and 1994 proposed regulations.

[71] 1991 Proposed Regs § 1.1275-4(g)(5) (giving an example mimicking the SIGN).

[72] 1994 Proposed Regs § 1.1275-4(b)(4)(vi) (Example 1).

In contrast, the 1986 proposed regulations would have allowed SIGN investors to avoid accruing *any* income until they received payments at maturity.[73] This potential tax planning feature of the Austrian SIGN issue and others like it may have prompted the Treasury to propose new rules in 1991.

Despite their facial resemblance to equity, PERCs are treated under the 1991 Proposed Regulations as contingent debt.[74] Under those regulations, the "dividend" payments received by PERC holders during the life of the security are treated as a nontaxable return of capital up to the principal amount for which the security was issued.[75] The contingent portion received at the termination of the PERC is treated as interest, after deducting any remaining return of capital.[76] This tax treatment has two curious effects. First, the periodic payments are treated as principal and the contingent final payment is treated as interest, exactly the opposite of the way the instrument is perceived by the market. Second, this treatment adopts a "wait and see" approach for PERCs similar to the treatment accorded all contingent debt under the 1986 Proposed Regulations. This latter feature allows investors an opportunity for deferral that they can no longer get with other similar forms of structured notes.

In contrast, the 1994 proposed regulations would require that the likely value of the contingent final payment be estimated and included in the payment schedule subject to the OID rules.

III. Financial Equivalencies and the Decreasing Tenability of the Debt-Equity Distinction

Structured notes and other debt-equity hybrids challenge the Service to characterize such instruments in a manner that reflects economic realities. Most commentary on these challenges has advocated approaches based on either bifurcation or integration.

The Service's 1991 proposals for contingent debt and its VRDI regulations,[77] like the new final rules for notional principal contracts,[78] can be viewed as part of a larger "switchboard" project, "[routing] the tax treatment of a variety of financial instruments

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[73] 1986 Proposed Regs § 1.1275-4(e)(2).
[74] 1991 Proposed Regs § 1.1275-4(f).
[75] 1991 Proposed Regs § 1.1275-4(f)(2).
[76] 1991 Proposed Regs § 1.1275-4(f)(2)–(3).
[77] 1991 Proposed Regs § 1.1275-4; Treas. Reg. § 1.1275-4, 5.
[78] Treas. Reg. § 1.446-3.

to the rules generally applicable to debt, options, or swaps, for example, depending on certain characteristics of the financial instruments."[79] If pursued, the switchboard project would be bifurcation on a grand scale. Although bifurcation holds the advantage of allowing the Service to employ existing tax pigeonholes, grand-scale bifurcation is likely to perpetuate and even exacerbate current anomalies in the tax treatment of economically equivalent financial instruments.

The 1994 proposed regulations for contingent debt largely extend the switchboard approach but rely more heavily on the OID rules as a source of analogy. The potential for integrated treatment of issuers in proposed Section 1.1275-6 recognizes that bifurcation can lead to anomalous results but fails to correct such anomalies for investors, who may hold complex portfolios of partially or completely offsetting contingent instruments. However, the 1994 proposed regulations raise both incremental and broader conceptual concerns.

Among the incremental concerns raised by the 1994 proposed regulations is that issuers may design a payment schedule that purposely defers or accelerates interest income and deductions. Because this proposal requires adjustments to the schedule only as actual payments are received, artful schedules might govern tax liabilities for years before they are corrected. Although the Service included an "anti-abuse" provision in the proposed regulations,[80] these provisions will be difficult to enforce, particularly for nonpublicly traded property.[81] To address this concern, the Service might instead require any instrument with a comparison market to be "marked-to-market," adjusting both current tax consequences and the projected payment schedule to reflect changes in market value at the end of each taxable year.[82]

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[79] Steven D. Conlon & Suzanne M. Russell, *Final Swap Regulations Leave Embedded Loan Concerns Unanswered*, 80 J. TAX'N 202, 206 (1994) (citing *Financial Products: The Switchboard Approach*, 60 TAX NOTES 942 (1993)).

[80] 1994 Proposed Regs § 1.1275-4(b)(4)(v).

[81] *See Law Student Suggests Refining Contingent Payment Debt Regs*, 95 TAX NOTES TODAY 42-35 (Mar. 2, 1995) (comments of Scott Marc Kolbrenner).

[82] *See* § 1256. To ameliorate the tax burden of a pure mark-to-market regime, the Service might consider a "retrospective mark-to-market approach" (RMTM) approach. *See generally* Reade Griffith, A Retrospective Mark-to-Market Approach to the Taxation of Financial Instruments (Dec. 1, 1994) (unpublished manuscript on file with the *Harvard Journal on Legislation*). Investors could elect either § 1256 or RMTM, which would collect the year-by-year tax owed under a mark-to-market regime on disposition of the asset. The RMTM owed for any given year would be treated as though paid with a loan from the Service, with interest computed at some easily ascertainable rate such as the "applicable federal rate" of § 1274(d) or the average of the underpayment rate

More fundamentally, the 1994 proposed regulations offer no guidance as to when a hybrid financial instrument will be treated as debt or equity. Nor can the regulations do so. Financial analysts have long recognized the notion of financial equivalencies. Simply stated, the value of a share of stock of a given company plus a put option on that share is equivalent to the value of a risk-free zero coupon bond and a call option on the share.[83] Recognizing these equivalencies leads one to some surprising insights. For example, "[w]henever a firm borrows, the lender effectively acquires the company and the shareholders obtain the option to buy it back by paying off the debt."[84]

Similarly, returning to the example of a convertible bond, one commentator notes, "many market participants view the decision to invest in a convertible bond not as the acquisition of a debt obligation with a stapled opportunity to roll the dice on equity prices, but as the de facto purchase of the underlying equity at an above-market price in return for an above-market current yield."[85] This contrasts sharply with the traditional tax treatment of a convertible bond, which waits until conversion to recognize the equity "genes" of the instrument.[86] Even an extension of proposed Section 1.1275-4 to cover these instruments still would characterize a significant portion of the convertible bond as debt, despite the way it is treated by market participants. This problem is only compounded when one recognizes that each of the three examples of structured notes considered in Part I can be characterized as either debt plus some form of option or as equity plus some form of option.

At bottom, neither bifurcation nor integration are wholly satisfactory answers to the character questions posed by structured

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defined by § 6601 and the overpayment rate defined by § 6611 (i.e., the federal short-term rate under § 1274(d) plus 2.5 percentage points, *see* § 6621). For instruments without a readily ascertainable comparison market, the RMTM approach could assume a constant growth (or loss) rate for each year between the acquisition and disposition of the asset to compute the tax owed for each year. *See* Mary Louise Fellows, *A Comprehensive Attack on Tax Deferral*, 88 MICH. L. REV. 722, 737 (1990). Although the Service would face some credit risk by allowing taxes to be paid retrospectively, this risk would be tempered by the tax lien value of the growth in the underlying asset and by the shortening of holding periods one might expect once the benefits of tax deferral are dampened or eliminated. *See id.* at 737 n.38.

[83] *See generally* Warren, *supra* note 21, at 465–70. For a good treatment of this proposition in the financial economics literature, see BREALEY & MYERS, *supra* note 3, at 435–38.

[84] BREALEY & MYERS, *supra* note 3, at 436.

[85] Kleinbard, *supra* note 51, at 1323.

[86] *Id.* at 1323 n.10 (citing BITTIKER & EUSTICE, *supra* note 28, at ¶ 4.60, p. 4-73).

notes. Even a relatively strong supporter of bifurcation supports it only "as necessary to preserve an income tax system which is riddled with senseless distinctions among categories of income and expense and which has very imprecise means of measuring and taxing income."[87] Although integration may seem more attractive in theory, it relies on the ability of the Service to recognize often complex financial equivalencies in taxpayers' portfolios—including "negative" financial equivalencies that could create complex straddles—and to decide which near-equivalencies are near enough to trigger integrating rules.[88] And the Service appears unwilling to go that far in applying an integration approach.

This confusing welter of existing rules and imperfect approaches for extending them leaves one longing for Ockham's razor.[89] Both Edward Kleinbard and Professor William Andrews may have suggested the appropriate tool: eliminating the debt-equity distinction for purposes of characterizing taxable income (or deductible expense).

A complex structured note may represent an exotic equity-linked market play to the investor while, merely being a cheaper source of plain vanilla financing to the issuer.[90] Given this quality, Kleinbard argues that it makes little sense to maintain the distinctions between debt and equity. Instead, he would allow issuing corporations a "cost of capital allowance" equal to a set rate multiplied by its total invested capital. The total invested capital would consist of any form of financing from some approved list designated by the taxpayer as part of its invested capital base.[91] Kleinbard argues that his proposal would greatly simplify the Code and obviate the need for the Service to keep apace of individual financial innovations.[92]

Professor Andrews, as Reporter for the American Law Institute's (ALI's) Federal Income Tax Project, also has recommended abolishing the debt-equity distinction.[93] Like Kleinbard, An-

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[87] Frank V. Battle, Jr., *Bifurcation of Financial Instruments*, 69 TAXES 821, 832 (1991).

[88] *See* Warren, *supra* note 21, at 474–76.

[89] Ockham's razor is "a rule in science and philosophy stating that entities should not be multiplied needlessly, which is interpreted to mean that the simplest of two or more competing theories is preferable . . . ." THE AMERICAN HERITAGE DICTIONARY 860 (2d collegiate ed. 1991).

[90] Kleinbard, *supra* note 2, at 954. Kleinbard summarizes this point memorably as "Your Tutti Frutti is My Plain Vanilla." *Id.*

[91] *Id.* at 959–61.

[92] *Id.*

[93] William D. Andrews, *Reporter's Study of the Taxation of Corporate Distributions*,

drews would allow issuing corporations a statutory allowance on qualified capital contributions.[94] However, Andrews would restrict the deduction to newly contributed equity capital to avoid a tax windfall to current equity holders, who did not expect a tax benefit when they purchased their stakes.[95]

Under either proposal, investors would still receive dividends and interest as ordinary income, and, because issuers would no longer have tax incentives to characterize instruments as debt rather than equity, investors could not demand additional, tax-influenced returns on newly issued debt.[96]

Although many supporters of bifurcation or integration have eschewed the Kleinbard or Andrews approaches as too radical to pass Congress,[97] the recent election returns indicate that substantial tax legislation may arise in this Congress. As Congress examines proposals to integrate, simplify, or otherwise alter the corporate income tax, perhaps it will eliminate the need to distinguish between "debt" and "equity" and put Humpty Dumpty out of the tax advising business.

—Matthew P. Haskins*

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in FEDERAL INCOME TAX PROJECT, SUBCHAPTER C: PROPOSALS ON CORPORATE ACQUISITIONS AND DISPOSITIONS AND REPORTER'S STUDY ON CORPORATE DISTRIBUTIONS 327, 367–70 (A.L.I. 1982) [hereinafter 1982 STUDY]; WILLIAM D. ANDREWS, REPORTER'S STUDY DRAFT 88–89 (1989) (prepared as part of the ALI's Federal Income Tax Project).

[94] WILLIAM D. ANDREWS, REPORTER'S STUDY DRAFT 88–89 (1989) (prepared as part of the ALI's Federal Income Tax Project).

[95] *See generally* 1982 STUDY, *supra* note 93, at 362–66.

[96] One remaining tax consideration for investors based on the debt-equity distinction might be the opportunity to defer taxation by investing in companies that pay low or no "dividends," effectively reinvesting the proceeds of their investment without paying an investor-level tax. This timing effect could be addressed through broader application of the mark-to-market rules of § 1256 or through the RMTM approach described *supra* note 82.

[97] *See, e.g.*, Randall K.C. Kau, *Carving Up Assets and Liabilities—Integration or Bifurcation of Financial Products*, 68 TAXES 1003, 1005 (1990).

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MANAGING MEDICAID WAIVERS: SECTION 1115 AND STATE HEALTH CARE REFORM

With the failure of federal health care reform in 1994, innovation on the state level has moved to center stage. Many states' health care reform plans include reform of the federal Medicaid programs that these states administer. Such efforts at reform, however, often run afoul of the complex requirements of the federal Medicaid statute, dealing with the methods by which health care may be delivered to the poor. Accordingly, states may apply for Section 1115 waivers, granted by the U.S. Department of Health and Human Services (HHS), which allow them to institute "demonstration projects" that are exempt from otherwise problematic federal Medicaid strictures. This Recent Development examines states' resort to Section 1115 waivers by tracing their rise to the forefront of health care reform and then considering some of their strengths and weaknesses as vehicles for government involvement in medicine.

Medicaid represents a major attempt by the federal government to improve access to medical care for the poor. Its enactment in 1965 (as an amendment to the Social Security Act of 1935) arguably represented the high-water mark of then-President Lyndon Johnson's "War on Poverty."[1] The Medicaid statute requires that a state, "as far as practicable under the conditions in such state," provide medical services to families with dependent children, and to blind, aged, or disabled individuals "whose income and resources are insufficient to meet the costs of necessary medical services . . . ."[2] The program is funded by both the states and the federal government[3] and is administered by the states.[4]

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[1] During U.S. Senate debate on the Medicaid bill, Senator Russell B. Long (D-La.) claimed that Medicaid would be "the largest and most significant piece of social legislation ever to pass the Congress in the history of our country." 111 CONG. REC. 15,037 (daily ed. July 6, 1965) (statement of Sen. Long).

[2] Health Insurance for the Aged Act, Pub. L. No. 89-97, tit. I, sec. 121(a), tit. XIX, § 1901, 79 Stat. 286, 343 (1965) (codified as amended at 42 U.S.C. § 1396 (1988)).

[3] The federal government provides between 50% and 83% of the funding for a state's Medicaid program, the exact amount depending upon the wealth of the state's population. *See* Health Insurance for the Aged Act tit. XIX, § 1905(b), 79 Stat. at 350 (codified as amended at 42 U.S.C. § 1396d(b) (1988)). *See generally* Stephen F. Loebs, *Medicaid—A Survey of Indicators and Issues*, *in* THE MEDICAID EXPERIENCE 5 (Allen D. Spiegal ed., 1979).

[4] *See* Health Insurance for the Aged Act tit. XIX, § 1901, 79 Stat. at 343 (codified as amended at 42 U.S.C. § 1396). *See also Medicaid: Title XIX of the Social Security Act—A Review and Analysis—Part I*, 4 CLEARINGHOUSE REV. 239 (1971).

States may thus determine how their Medicaid programs will operate and what services such programs will provide.[5] The federal government, however, has promulgated guidelines that limit the states' flexibililty in determining eligibility criteria and payment structures.[6] Two of the most significant of these guidelines require "comparability" (medical services provided to an eligible individual shall not be less in amount, duration, or scope from those provided to any other individual)[7] and "freedom of choice" (most eligible individuals may obtain medical services from any institution, agency, community, pharmacy, or person qualified to perform the services provided).[8]

This regulatory scheme has proved to be an expensive one—Medicaid spending has more than doubled from 1988 to 1992,[9] while 1995 estimates place the federal government's share of the program's bill at ninety billion dollars.[10] The increasing cost of Medicaid has long troubled Congress.[11]

Indeed, states' similar concern with the growth of Medicaid costs has caused them to search for new mechanisms for providing health care to the poor. Part of this search has involved obtaining exemptions from the complex requirements of the Social Security titles, a path available since 1962. Emphasizing the need for "imaginative" public assistance solutions and for welfare programs "more flexible and adaptable to local needs," Presi-

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[5] *Id.*

[6] *See* Health Insurance for the Aged Act tit. XIX, § 1902(a), 79 Stat. at 344–48 (codified as amended at 42 U.S.C. § 1396(a)). *See also Medicaid: Title XIX of the Social Security Act—A Review and Analysis—Part III*, 4 CLEARINGHOUSE REV. 348 (1971).

[7] *See* Health Insurance for the Aged Act tit. XIX, § 1902(a)(1)(B)(i)–(ii), 79 Stat. at 345 (codified as amended at 42 U.S.C. § 1396(a)(10)(B)(i)–(ii)).

[8] Social Security Amendments of 1967, Pub. L. No. 90-248, tit. II, sec. 227(a), tit. XIX, § 1902(a)(23), 81 Stat. 821, 903 (codified as amended at 42 U.S.C. § 1396a(23) (1988)).

[9] *See* John Holahan et al., *Explaining the Recent Growth in Medicaid Spending*, HEALTH AFF., Fall 1993, at 177. This rise in Medicaid costs can partially be attributed to the fact that between 1984 and 1990, Congress widened Medicaid eligibility to include low-income children, pregnant women, the elderly, disabled persons, the homeless, and recently legalized aliens. *See id.* at 184.

[10] *See Budget Blaster*, U.S. NEWS & WORLD REP., Feb. 20, 1995, at 33, 38–39.

[11] *See* ROBERT STEVENS & ROSEMARY STEVENS, WELFARE MEDICINE IN AMERICA 108–09 (1974); Kenneth R. Wing, *The Impact of Reagan Era Politics on the Federal Medicaid Program*, 33 CATH. U. L. REV. 1, 15 (1983). In October, 1994, U.S. Senator Robert Graham (D-Fla.) noted on the Senate floor that "[s]ince 1982, Florida has had its Medicaid program increase from $1 to $7 billion. In the years from 1990 through 1993, Florida saw its Medicaid budget expand by 30 percent, 26 percent, and 19 percent respectively." 140 CONG. REC. S15,053 (daily ed. Oct. 8, 1994) (statement of Sen. Graham). Senator Graham urged HHS to grant his state a demonstration project waiver, under which "costs would be controlled and managed . . . ." *Id.*

dent John F. Kennedy urged Congress in 1962 to amend the Social Security Act of 1935 to include a waiver provision permitting experimentation with methods of delivering benefits to beneficiaries of then-existing and future programs provided under the Act.[12] Congress accordingly provided in Section 1115 of the Act that:

> (a) In the case of any experimental, pilot, or demonstration project which, in the judgment of the Secretary, is likely to assist in promoting the objectives of [the Act] . . . .
> (1) the Secretary may waive compliance with any of the requirements of [various sections of the Act] . . . to the extent and for the period he finds necessary to enable such State or States to carry out such project . . . .[13]

The very brief Senate report on the section noted that federal guidelines imposed on the states by Congress "often stand in the way of experimental projects designed to test out new ideas and ways of dealing with the problems of public welfare recipients."[14] The projects to be approved were "those which are designed to improve the techniques of administering assistance and the related rehabilitative services under the assistance titles."[15] Upon passing the Medicaid statute in 1965, Congress amended Section 1115 to denote specifically its applicability to state Medicaid programs.[16]

The procedure for applying for Section 1115 waivers is complex. The Secretary of HHS may grant a waiver for a demonstration program that "furthers the general objectives of [Medicaid]."[17] To obtain a waiver, a state must thus submit a detailed project proposal to HHS, specifying the statutory and regulatory mandates to be waived and discussing the likely impact of the waiver on program expenditures, relevant laws, and beneficiaries enrolled in the project.[18] HHS's Health Care Financing Agency

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[12] *See* 108 CONG. REC. 1,487–89 (daily ed. Feb. 2, 1962) (message from Pres. Kennedy).

[13] Public Welfare Amendments of 1962, Pub. L. No. 87-43, tit. I, sec. 122, tit. XI, § 1115, 76 Stat. 173, 192 (1962) (codified as amended at 42 U.S.C. § 1315 (1988)).

[14] S. Rep. No. 1589, 87th Cong., 2d Sess. 19 (1962), *reprinted in* 1962 U.S.C.C.A.N. 1943, 1961.

[15] *Id.* at 20, *reprinted in* 1962 U.S.C.C.A.N. at 1962.

[16] *See* Health Insurance for the Aged Act tit. XI, § 1115, 79 Stat. at 352 (codified as amended at 42 U.S.C. § 1315).

[17] *See* S. Rep. No. 1589, *supra* note 14, at 20, *reprinted in* 1962 U.S.C.C.A.N. at 1962.

[18] *See* CONGRESSIONAL RESEARCH SERVICE, MEDICAID SOURCE BOOK: BACKGROUND DATA AND ANALYSIS (A 1993 UPDATE) 418 (1993) [hereinafter MEDICAID SOURCE BOOK]. *See, e.g.*, 59 Fed. Reg. 1951, 1966–67 (1994) (discussing Health Care Financ-

(HCFA) processes the waiver by first convening a technical review panel to compare and evaluate the demonstration proposal.[19] The panel scores the proposal's methodology and design, its objectives, its expected costs and returns and the applicant's knowledge and experience in the relevant policy area.[20] It also considers potential risks to the health and safety of participants in research activity.[21] Ultimately, the review panel recommends either approval, conditioned approval, or rejection of the proposal.[22] HCFA's Office of Research and Demonstration (ORD) then incorporates the review panel's recommendation into a decision memorandum to the agency's Administrator, who subsequently decides whether to grant a waiver for the demonstration proposal.[23]

HHS's discretion to grant Section 1115 waivers is not without its limits. Projects whose net annual federal costs exceed one million dollars and which affect more than 300 Medicaid recipients require the approval of both the HHS Assistant Secretary for Management and Budget and the White House Office of Management and Budget (OMB).[24] Until recently, OMB had insisted that these projects adhere to strict "budget neutrality," under which a state had to establish that its Medicaid program's service costs would be no greater with the project than without it.[25] OMB's insistence on "budget neutrality" contributed to the sharp decline in the number of waivers granted by HHS during the 1980s.[26]

Judicial scrutiny also limits HHS's discretion to grant Section 1115 waivers, but to a much lesser extent than does OMB oversight. Reviewing judges have suggested that they would overturn only a waiver decision that was "arbitrary and capricious and

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ing Agency research and development agreements and grants for fiscal years 1994–1996).

[19] *See* Allen Dobson et al., *The Role of Federal Waivers in the Health Policy Process*, HEALTH AFF., Winter 1992, at 72.

[20] *See, e.g.*, 56 Fed. Reg. 26,120, 26,131–32 (1991) (discussing Health Care Financing Agency research and demonstration cooperative agreements and grants for fiscal year 1991).

[21] *See* 48 Fed. Reg. 9266, 9269 (1983) (discussing exemption of certain research and development projects from regulation for protection of human research subjects).

[22] *See* Dobson, *supra* note 19, at 77.

[23] *See id.*

[24] *See* Elizabeth Andersen, *Administering Health Care: Lessons from the Health Care Financing Administration's Waiver Policy-Making*, 10 J.L. & POL. 215, 227–28 (1994).

[25] *See* Dobson, *supra* note 19, at 85.

[26] *See id.* HHS has recently announced that it will assess budget neutrality more flexibly than it had in the past. *See infra* note 35 and accompanying text.

lacking in rational basis," in light of the objectives of Medicaid.[27] Under this approach, a federal district court has held that the Secretary of HHS was authorized to approve a state Section 1115 experiment requiring Medicaid recipients to pay a portion of the cost of their benefits.[28] In 1994, however, the U.S. Court of Appeals for the Ninth Circuit vacated a Section 1115 waiver for a California AFDC demonstration project because it lacked a goal beyond that of saving money.[29] Furthermore, the court held that the requirement that demonstration projects promote the objectives of the relevant Social Security title obligated HHS to consider the impact of such projects on affected beneficiaries and to address their concerns in a full administrative record.[30] Nevertheless, the Ninth Circuit's recent efforts represent a departure from the norm. States have typically used Section 1115 waivers to implement long-term and extensive Medicaid reform without much judicial intrusion.[31]

Going beyond the deference shown by the judiciary, the Clinton Administration has actively facilitated the approval of Section 1115 waivers. Claiming that "for years and years and years, governors have been screaming for relief from a cumbersome process by which the Federal Government has micromanaged the health-care system affecting poor Americans," President Clinton has directed HHS to streamline the Medicaid waiver process.[32] Moreover, HHS outlined in 1994 a flexible approach to waiver approval that it claims will facilitate the testing of new pro-

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[27] *See* Crane v. Mathews, 417 F. Supp. 532, 539 (N.D. Ga. 1976). *See also* Aguayo v. Richardson, 473 F.2d 1090, 1103 (2d Cir. 1973). This interpretation of Section 1115 is based on Section 706(2)(A) of the Administrative Procedure Act. *See* 5 U.S.C. § 706(2)(A) (1988) ("The reviewing court shall . . . hold unlawful and set aside agency action, findings, and conclusion found to be arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.").

[28] *See* California Welfare Rights Org. v. Richardson, 348 F. Supp. 491 (N.D. Cal. 1972). The court also commented that had the Secretary approved a demonstration project that affected an "unreasonably large population" or lasted for an "unreasonably long period," she would perhaps have abused her discretion. *See id.* at 498. Moreover, the U.S. Supreme Court has suggested that, at a minimum, "serious statutory questions might be presented if a state Medicaid plan excluded necessary medical treatment from its coverage." Beal v. Doe, 432 U.S. 438, 444 (1977).

[29] *See* Beno v. Shalala, 30 F.3d 1057, 1069 (9th Cir. 1994).

[30] *See id.* at 1069–70, 1074.

[31] *See* Andersen, *supra* note 24, at 229.

[32] *See* Thomas L. Friedman, *President Allows States Flexibility on Medicaid Funds*, N.Y. TIMES, Feb. 2, 1993, at A1, A13. *See also* Larry Stevens, *States Test Medicaid Reforms*, BUS. & HEALTH, Aug. 1994, at 51. Indeed, upon taking office in 1993, President Clinton instructed HHS to approve waiver requests "whenever possible." *See* Robert Pear, *G.A.O. Says White House Is Expanding Medicaid Coverage*, N.Y. TIMES, Apr. 5, 1995, at A22.

jects.[33] Under this approach, the agency will permit the testing of the same or related policy innovations in multiple states, on the grounds that "replication is a valid mechanism by which the effectiveness of policy changes can be assessed."[34] Furthermore, HHS has committed itself to approving waivers for longer periods and to assessing budget neutrality more flexibly than it had in the past.[35] It has also vowed to limit the administrative constraints on the states and to reduce the processing time for waiver requests.[36] By the end of 1994, six states had received waivers from the Clinton Administration, seven applications were pending, and other proposals were being drafted.[37]

The new flexibility in Section 1115 waiver administration has ushered in an era in which waivers are granted not so much to improve the delivery of program benefits but rather to reduce program costs. The most recent demonstration projects initiated under Section 1115 often expand Medicaid eligibility but lock participants into a managed care entity (an HMO), whose primary-care physicians act as "gatekeepers" for all specialty or hospital services. Managed care achieves cost savings through a prospective payment system, as health care providers contract with a managed care plan and receive a fixed payment per patient *before* care is delivered.[38] Thus, it differs from the traditional fee-for-service system, which pays health care providers for costs incurred *after* care has been delivered.[39] According to HCFA's Office of Managed Care, enrollment in Medicaid managed care programs has increased sixty-three percent since 1993, and enrollees now represent one-quarter of all Medicaid beneficiaries.[40] Other waivers have allowed states to reimburse at a below-cost basis

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[33] *See* 59 Fed. Reg. 49,249 (1994) (discussing policies and procedures for reviewing demonstration proposals pursuant to Section 1115).

[34] *See id. See also HHS Announces Streamlined Policies for Evaluating State Waiver Requests*, B.N.A. HEALTH CARE POL'Y REP., Oct. 3, 1994, at D8.

[35] HHS will now approve demonstration projects lasting up to five years (as opposed to a previous average of three years) and assess budget neutrality over the projects' entire lives, rather than over each year of their existences. *See* 59 Fed. Reg. at 49,250.

[36] *See id.* Along these lines, HHS has hired the Research Triangle Institute to produce a "how-to" guide for states applying for waivers. *See HHS Encouraging Waiver Requests with Policy Principles*, B.N.A. HEALTH CARE POL'Y REP., Oct. 25, 1993, at D31.

[37] *See PPRC Commissioners Express Concern with Section 1115 Medicaid Waivers*, B.N.A. HEALTH CARE POL'Y REP., Dec. 19, 1994, at D16 [hereinafter *Commissioners Express Concern*].

[38] *See* John K. Iglehart, *The American Health Care System—Managed Care*, 327 NEW ENG. J. MED. 742 (1992).

[39] *See* ALAIN C. ENTHOVEN, HEALTH PLAN 9–10 (1980).

[40] *Commissioners Express Concern*, *supra* note 37, at D15.

services provided by federally funded health centers, a grant now being contested in court by community health centers.[41]

These significant changes have been achieved despite the Senate's suggestion in 1962 that "a demonstration project usually cannot be statewide in operation" and that HHS was to "selectively" approve state proposals.[42] Now that HHS has indicated its willingness to grant more waivers to more states with less delay, that selectivity has disappeared.[43] Section 1115 waivers are being granted for increasingly long-term and large-scale programs that can hardly be deemed "experimental."[44] The widespread health reform instituted under Section 1115's auspices thus represents a broad extension of the statute's reach—"[t]he spirit, if not the letter of the [Medicaid] law is being winked at," according to Joseph P. Newhouse, a professor of health policy and research at Harvard University and a member of the Physician Payment Review Commission, which advises Congress on Medicaid and Medicare policies.[45]

Although states may be using Section 1115 waivers in a manner that goes beyond what is legally permissible, many argue that there are strong policy reasons for their doing so. States often defend their use of Section 1115 waivers by arguing that the waivers allow them to serve as "laboratories of democracy,"[46] experimenting with health care reform options that other states and the federal government may then examine and perhaps duplicate. Specifically, as more states experiment with Medicaid delivery systems, the country will develop a complete record of health care reform alternatives. Both other states and the federal government will refer to this record during their own efforts to design Medicaid reform plans that are cost-effective, result in a high degree of patient satisfaction, provide high quality health

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[41] *See, e.g.*, National Association of Community Health Centers v. Shalala, No. 1:94CV01238 (D.D.C. filed June 7, 1994).

[42] S. Rep. No. 1589, *supra* note 14, at 20, *reprinted in* 1962 U.S.C.C.A.N. at 1961–62.

[43] *See* Pear, *supra* note 32 and accompanying text.

[44] "We're deluding ourselves to call them experiments," said Physician Payment Review Commissioner William Curreri. *Medicaid Managed Care Demonstrations Spreading Rapidly, Despite Resistance*, B.N.A. HEALTH CARE POL'Y REP., Oct. 12, 1994, at D4. Arizona's "experimental" Medicaid system has operated under a waiver for thirteen years and affects every beneficiary in the state. *See* Andersen, *supra* note 24, at 229 n.67; MEDICAID SOURCE BOOK, *supra* note 18, at 418–19.

[45] *Commissioners Express Concern*, *supra* note 37, at D15.

[46] *See* Fernando R. Laguarda, *Federalism Myth: States as Laboratories for Health Care Reform*, 82 GEO. L.J. 159 (1993) (quoting New State Ice Co. v. Liebmann, 285 U.S. 262, 311 (1932) (J. Brandeis dissenting)).

care, and expand access.[47] Indeed, the fact that any given reform plan will likely unfold in unpredictable and complex fashions makes it especially incumbent on reformers to scrutinize the results of prior experimentation.[48]

States also argue that in the absence of national health care reform, they must take the lead in providing coverage for the uninsured.[49] Section 1115 waivers accordingly allow them to bypass the rigorous requirements of the federal Medicaid law[50] to expand access to Medicaid benefits. Indeed, many states have used Section 1115 waivers to widen Medicaid coverage—Oregon, for example, has extended Medicaid to over 100,000 previously uninsured individuals by instituting a "rationing" plan for all Medicaid recipients.[51] Other states that have enlarged or plan to enlarge their Medicaid rolls by means of Section 1115 waivers include Tennessee,[52] South Carolina,[53] and Hawaii.[54]

Most significantly, the astronomical rise in Medicaid costs[55] has caused states to seek out Section 1115 waivers to enable them to make the most efficient use of their health care dollars. States that have implemented Medicaid managed care plans under Section 1115 waivers report cost-savings.[56] Arizona's managed care program, for example, saved the state an estimated $100 million between 1983 and 1991[57] and has been praised for

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[47] *See supra* notes 14–15 and accompanying text.

[48] *See* Howard Dean, *New Rules and Roles for States*, HEALTH AFF., Spring 1993, at 184 (arguing that a managed competition model of health care reform should be tested in the states before being implemented through a national health plan).

[49] *See* Dobson, *supra* note 19, at 89 ("Federal gridlock on health care reform is widely assumed to be the impetus for the growing state activity.").

[50] *See supra* notes 6–8 and accompanying text.

[51] *See* Laguarda, *supra* note 46, at 185 n.169.

[52] *See* John K. Iglehart, *Health Care Reform—The States*, 330 NEW ENG. J. MED. 75 (1994).

[53] South Carolina received a Section 1115 waiver in November 1994 to implement the "Palmetto Health Initiative." The initiative will cover 149,000 uninsured individuals and place Medicaid recipients in managed care plans. *See South Carolina Awarded Conditional HCFA Approval for Managed Care Plan*, B.N.A. HEALTH CARE POL'Y REP., Nov. 28, 1994, at D22.

[54] *See HCFA Begins Publishing Notices of Section 1115 Waiver Requests*, B.N.A. HEALTH CARE POL'Y REP., Jan. 30, 1995, at D25 (noting that Hawaii's QUEST program, a managed care delivery system, would expand Medicaid income eligibility to 300% of the federal poverty level).

[55] *See supra* notes 9–11 and accompanying text.

[56] *See Medicaid Managed Care: Hearings Before the Subcomm. on Oversight and Investigations of the House Comm. on Energy and Commerce*, 103d Cong., 1st Sess. 26 (1993) (statement of Janet L. Shikles, Director of Health Financing and Policy Issues Human Resources Division).

[57] Nelda McCall et al., *Managed Medicaid Cost Savings: The Arizona Experience*, HEALTH AFF., Spring (II) 1994, at 241.

its quality by both hospitals and physicians.[58] These efforts may inspire other states to embrace managed care as a solution to escalating Medicaid costs.

While states are undoubtedly facing massive increases in Medicaid costs, their use to date of Section 1115 waivers as a way of alleviating these costs may, in the long run, cause more harm than good. First, the managed care plans often embraced by states arguably provide low quality health care to Medicaid recipients. Second, states using Section 1115 waivers to expand access to Medicaid benefits have done so at the expense of current Medicaid recipients. Third, inadequate health care reform through Section 1115 waivers will diminish opportunities for more effective reform in the forseeable future.

Most of the Section 1115 waivers awarded during 1994 went to states with Medicaid managed care plans.[59] Yet managed care may provide lower quality care than does the traditional fee-for-service model. Opponents of managed care argue that its design creates financial incentives for physicians to provide less care.[60] According to health policy research, this reduction in care will come, in part, at the expense of the elimination of clearly necessary treatment.[61] Thus, when a managed care plan devotes a lower amount of expenditures to an enrollee, both unnecessary and *necessary* care may be eliminated.

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[58] *See, e.g.*, Lisa Schroepfer, *Designing a System Better Than Medicaid*, ARIZ. TREND, May 1988, at 60.

[59] *See supra* notes 38–40 and accompanying text.

[60] *See* Rand E. Rosenblatt, *The Legal Implications of Health Care Cost Containment: A Symposium: Medicaid Primary Care Case Management, the Doctor-Patient Relationship, and the Politics of Privatization*, 36 CASE W. RES. L. REV. 915, 920 (1986). Proponents of managed care systems, however, counter that the traditional fee-for-service model results in an oversupply of medical care. *See generally* Kenneth Arrow, *Uncertainty and the Welfare Economics of Medical Care*, 53 AM. ECON. REV. 941 (1963); ALAIN C. ENTHOVEN, THEORY AND PRACTICE OF MANAGED COMPETITION IN HEALTH CARE FINANCE 41 (1988).

[61] *See* JOSEPH NEWHOUSE, FREE FOR ALL?: LESSONS FROM THE RAND HEALTH INSURANCE EXPERIMENT 173–74 (1993). A comparison of a cost-sharing plan and a free plan found that while the *number* of medical-surgical hospitalizations in the cost-sharing plan was lower, the *proportion* of inappropriate to appropriate admissions was the same: "Cost sharing has a nonspecific effect on the use of medical services. In particular, it reduces appropriate and inappropriate services . . . by the same proportion." *Id.* at 180. *See also*, Lucian L. Leape, *Does Inappropriate Use Explain Small-Area Variations in the Use of Health Care Services?*, 263 JAMA 669 (1990) (study of three procedures (coronary angiography, carotid endarterectomy, and upper gastrointestinal tract [UGI] endoscopy) found that while usage rates in different areas were highly variable, the inappropriateness rates across both high- and low-use areas varied only a little, if at all).

The elimination of necessary care seems extremely likely to occur under Medicaid managed care programs, if only because Medicaid recipients are more likely than the general population to be handicapped, disabled, or beset by chronic illness.[62] Indeed, diagnosis and treatment of the severely or chronically ill may depend upon the type of cost-intensive technology that is anathema to managed care plans.[63] Furthermore, many ill people require a variety of prescription drugs or undergo a number of procedures and are thus in greater need of the continuous care that is traditionally associated with a fee-for-service system—only those physicians intimately familiar with these patients' records will be able to provide them with a satisfactory level of care. It is therefore unsurprising that one study concluded that low-income, sick people fare poorly under managed care plans.[64]

If Medicaid managed care programs do not provide an adequate level of care for the poor, then they run afoul of Medicaid's original purposes. Medicaid was meant to overcome a "dual track" tradition in health care. It aimed to supply the poor with health care "'of high quality and in no way inferior to that enjoyed by the rest of the population.'"[65] Yet by placing Medicaid patients in managed care programs that affect the poor more severely than the general population,[66] Section 1115 waivers recreate exactly the dual track system that Medicaid attempted to eliminate.

Section 1115 plans designed to expand access to Medicaid benefits may also harm current Medicaid recipients. For example, Oregon implemented a waiver plan that raised eligibility cut-offs for Medicaid but rationed care to pay for the resulting expansion of Medicaid rolls.[67] The original Medicaid population,

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[62] *See* Robert J. Blendon et al., *Medicaid Beneficiaries and Health Reform*, HEALTH AFF., Spring 1993, at 132. Of those aged 18–64, 28.5% of Medicaid beneficiaries versus 11.4% of all Americans suffered from general health problems in 1992. *Id.* at 137. Of children, 21.6% of Medicaid beneficiaries reported health problems in 1992, compared with 13.0% of all children. *Id.* at 138.

[63] *See, e.g., Health Role of States in Health Care Reform Proposal: Hearings Before the Subcomm. on Health of the House Comm. on Ways and Means*, Federal Document Clearing House, Nov. 5, 1993, *available in* LEXIS, LEGIS Library, CNGTST File (statement of Ann Torregrossa, staff attorney, National Health Law Program) (Between mid-1960s and 1980, Pennsylvania's Medicaid managed care program refused to cover CT-scans, ultrasound, and radiation therapy and chemotherapy for cancer.).

[64] *See* NEWHOUSE, *supra* note 61, at 287.

[65] *See* Rosenblatt, *supra* note 60, at 930–31 (quoting DEPT. OF HEALTH, EDUC. & WELFARE (HEW), HANDBOOK OF PUBLIC ASSISTANCE ADM'N (Supp. D, § D-5140)).

[66] *See supra* notes 62–64 and accompanying text.

[67] *See* Laguarda, *supra* note 46, at 185.

and not the entire population of the state, therefore bore the burden of health care reform by giving up important medical services to enable the previously uninsured to receive basic health care.[68] Similarly, Tennessee paid for an expansion of Medicaid coverage to 1.5 million previously uninsured individuals by placing original Medicaid recipients in managed care programs.[69] Reports from February 1995, show Tennessee's hospitals as having received only forty-four cents for every dollar of care provided.[70] Such shortfalls create a danger that physicians and hospitals will ration care to offset such losses.[71]

Admittedly, expanding Medicaid coverage to the previously uninsured by rationing care may benefit the "poor" as a whole. States adopting such a system have nevertheless made a troubling choice. Rather than expanding coverage while preserving the quality of health care received by current Medicaid recipients, these states have pursued the former objective at the expense of the latter. Financing the expansion of coverage to the previously uninsured by progressively taxing a state's entire population, however, could achieve *both* objectives.[72] It thus deserves serious consideration as an alternative to the "zero-sum" approach embodied by rationing.

Despite their tendency to solidify class-based inequities in the provision of health care,[73] Section 1115 demonstration projects will likely satisfy an American public concerned primarily with restraining rising health care costs, secondarily with removing from its view the plight of the uninsured, and hardly at all with providing high quality health care coverage to all the poor. In

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[68] *See* Norman Daniels, *Is the Oregon Rationing Plan Fair?*, 265 JAMA 2232 (1991).

[69] *See* Reed Branson, *They Need to Fix It, Not Study It, THA Chairman Says of TennCare*, COMMERCIAL APPEAL (MEMPHIS), Feb. 3, 1995, at A10.

[70] *See id.*

[71] *See Reform Lessons. TennCare: Problems May Show Way to Go*, COMMERCIAL APPEAL (MEMPHIS), Jan. 23, 1995, at A4 ("Anecdotal testimony indicates there may be some rationing of care.").

[72] An example of this approach is Canada's universal system, where tax contributions finance a relatively uniform health system. *See generally* John K. Iglehart, *Health Policy Report—Canada's Health Care System*, 315 NEW ENG. J. MED. 206–08 (1986).

[73] Some commentators have suggested that Medicaid patients *already* receive a substantially lower standard of care than do persons with private insurance. *See, e.g.*, PAUL C. WEILER ET AL., A MEASURE OF MALPRACTICE 47 (1993) (discussing survey finding that Medicaid patients suffered from medical negligence more frequently than did privately insured patients). *See also* Lester Thurow, *Medicine Versus Economics*, 313 NEW ENG. J. MED. 611, 613 (1985) (stating that medical care is distributed along three tiers—a government financed-tier for the poor and elderly, an employer-financed middle tier, and a "free-market" tier for wealthy individuals, who can afford higher rates than can both the government and employers).

accepting these piecemeal solutions to health care problems, we thus risk locking the current Medicaid population in a dual track system. This is a high price to pay for containing costs and expanding access to the uninsured. Both Congress and the Clinton Administration should therefore reconsider their willingness to approve readily states' use of Section 1115 waivers.

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BOOK REVIEWS

A NATION UNDER LAWYERS: HOW THE CRISIS IN THE LEGAL PROFESSION IS TRANSFORMING AMERICAN SOCIETY. By *Mary Ann Glendon*. New York: Farrar, Straus and Giroux, 1994. Pp. 3, 294, notes, index. $24.00 cloth.

"What does it mean when prominent law professors deride the rule of law, when judicial moderates openly disdain popular government, and when practitioners adapt ethical rules to fit changing behavior rather than orienting their behavior toward standards deliberately set high?" (p. 6). In *A Nation Under Lawyers*, Mary Ann Glendon draws on her experiences as an attorney and an academic to confront these issues, producing a straightforward and entertaining exploration of the events and ideas that have led to the current atmosphere of discontent, if not crisis, in the legal community. Glendon finds that there has been a fundamental change, beginning in the 1960s, in the perception of the roles of lawyers, judges, academics and the entire legal system. Unlike much of the current criticism, Glendon moves beyond merely stringing together a series of anecdotes of abusive lawyers to examine with candor the larger trends that are facing the legal profession and explore both their roots and potential implications. Because these trends have been incremental, the legal community has been able to avoid confronting their consequences. Though Glendon refuses to commit to concrete proposals for reform, *A Nation Under Lawyers* serves as a fine wake-up call, highlighting the issues that the legal community as a whole should confront.

Glendon begins by exploring the current state of practicing lawyers. Drawing on the work of Jane Jacobs, Glendon finds that the lawyer plays dual, inherently conflicting roles as both "raider" and "trader" (pp. 63–64). While acting as the former, the lawyer is concerned with acquiring and guarding property or other intangible goods for clients and relies on loyalty among firm members for protection both from strangers and from lawyers outside the firm. Conversely, a lawyer acting as a "trader" seeks to engage in producing and trading the client's goods and, therefore, places great value on operating honestly in order to foster reliable understandings and relationships with other lawyers and strangers with whom deals may be made. This duality of roles confronts the lawyer with various dilemmas. For example, a

lawyer must attempt to balance the desire to be a client's loyal raider with the need to be a trader within the court system, obeying both the word and the spirit of its rules.

Glendon focuses mainly on how these dual roles have affected big-firm corporate practice. The "golden age" of law firms, the 1920s to the 1960s, saw the development of certain "understandings" concerning not only career paths, but also firm unity over economic considerations, independence of attorneys from their clients and the public role of the attorney. While raider traits had traditionally been appreciated in litigators, corporate lawyers were able to maintain more of a trader role, promoting honest and cooperative behavior, distilling conflict, and maintaining the ability to tell "would-be clients that they are damned fools and should stop" (p. 75). The end of the "golden age" of corporate law firms, according to Glendon, began in the early 1970s when economic pressures and increased competition led to the implementation of cost-cutting measures, including previously unheard of layoffs. Changing demands from clients and the increasingly technocratic role of attorneys in the modern world transformed the former "understandings" into a "friend-of-the-client" ideal. Thus, corporate attorneys have increasingly dropped their trader and peacemaker instincts and adopted raider characteristics, reflected in the takeover craze and savings and loan debacle. While blind loyalty to the client may appear to reflect a more pragmatic role for lawyers, easing any ethical conflict by abandoning pretensions of acting for any interest other than the client's, this "superficially appealing solution to the conflicts that attend a lawyer's role sweeps serious problems under the carpet" (p. 58). Ultimately, Glendon asserts, this mixture of trader and raider roles has destroyed the basis of both, leaving neither loyalty nor honesty.

The loss of traditional "understandings," Glendon argues, and the subsequent lack of "independence, public service and professionalism" have led to the current dissatisfaction among young attorneys. In addition to complaining of long hours and a lack of meaningful responsibility, young lawyers feel increasingly useless if not engaged in conflict. Glendon claims that conflict avoidance and peacemaking skills should also be appreciated. Certain qualities—the eye for the issue; the feel for common ground; the eye to the future; mastery of the apparatus; legal architecture and procedure; problem solving; and strong tolerance—accentuate a lawyer's ability to serve these roles (pp.

100–08). Unfortunately, litigators, like surgeons, receive the acclaim while the peacemaker merely dispenses preventative medicine. Having raised these issues, Glendon fails to assert any concrete proposals or convince the reader that change is possible. Instead, the reader is left to wonder how the profession will find creative solutions to reattain the ethical "understandings" of the past and value the productive peacemaker role of the attorney.

Glendon is even more critical of the judiciary. She does not make a political judgement of the "activist" Warren Court or the more recent decisions of the "moderate" and "conservative" justices, but rather critiques the changing way that "judges and the legal community in general think about judicial excellence and about the role of the judiciary in American society" (p. 117). Glendon extols what she terms the "classical" ideals of judicial behavior—"impartiality, prudence, practical reason, mastery of craft, persuasiveness, a sense of the legal system as a whole, the ability to preserve principled continuity while adapting the law to changed social and economic conditions—and above all, self-restraint" (p. 118). This restraint, according to Glendon, is manifested in Chief Justice John Marshall's "consistent acknowledgment of the Court's limited role within the constitutional regime" (p. 118) and Justice Holmes's insistence "that the Supreme Court must not sit as a super-legislature and the unelected justices must not substitute their views for the judgments of the people's elected representatives" (p. 120). Glendon dismisses the idea that an increasingly complex world forces an abandonment of these "classical" ideals. She points out that the decisions of Benjamin Cardozo manage to "maintain predictability, coherence, and continuity while making the law responsive to the needs of a changing society" (p. 133). These ideas in private law were capably carried forward into the new world of regulatory law by August and Learned Hand and Henry Friendly.

In contrast, Glendon is highly critical of the "romantic" ideal of the judiciary encompassed in the Warren Court. She portrays *Brown v. Board of Education* as an act of statesmanship not grounded in the constitutional text, a successful "wager" that not only precipitated the view that law could be used to promote constructive change, but also altered contemporary attitudes about race relations (pp. 154–56). Glendon's model of romantic adjudication, however, is Justice Brennan, who rejects Marshall's legacy by asserting that "[t]he course of vital social, economic,

and political currents may be directed" (p. 159). Glendon finds that this attitude has been extended far beyond its functional use, permeating federal and state courts as "[t]he flight from politics turned into a stampede, as courts became alternatives to legislatures, and judges began acting like executives and administrators" (p. 141). Nor has the recent shift in the Supreme Court reversed this process. While the Rehnquist Court may have called a halt to further expansion, it has also "sanctioned uses of judicial power as startling as any of those of their predecessors" (p. 142).

Why, though, is the classical judge superior to the romantic judge? According to Glendon, compassion, while initially appealing because it provides protection for the weak, is ultimately destructive because it leaves the liberties of citizens to the vagaries of the personal beliefs of the judge. While assertive judging leads to arbitrary judgments, independent and impartial judging ultimately protects all factions. Although complete impartiality may be unattainable, judges should provide the ideal for which to strive. The increasing complexity of society also requires judges to exercise self-restraint to maintain predictability and coherence in the law. Finally, because romantic judging dismisses actions of the political branches, it ultimately demoralizes the political process and endangers democracy.

Glendon finds that the expansive powers she criticizes have not led to more satisfied judges because increased caseloads have lowered both the quality of judgments and the satisfaction of judges. The problems stem from three categories: neglect, inappropriate delegation, and erosion of institutional checks on the arbitrary exercise of discretion (p. 144). Relatively low salaries and decreasing prestige accorded the position by the legal community make serving as a judge a less and less attractive option to the brightest minds. Like her findings concerning attorneys, Glendon concludes that the legal profession must alter its perception of excellence and learn to honor "ordinary judges" who approach their position with humility and self-restraint even if they do not "make lively copy" (p. 172).

Continuing her theme, Glendon is highly critical of the profound change that occurred in legal academia in the 1970s. She traces the development of common law in the United States, chronicling the rise of the moral logic espoused in Lord Coke's statement that "reason is the life of the law" and its subsequent rejection in Holmes's classic declaration that "[t]he life of the

law has not been logic: it has been experience" (p. 188). This period was followed by successful adaptations of the law to the demands of the complex modern world and the increased regulation stemming from the New Deal. "In the early 1960s, the American variant of the common law tradition seemed to be in reasonably healthy condition," (p. 197) Glendon writes, evidenced by the success of the Uniform Commercial Code, the systematizing into treatises of fields that had been born in legislation (such as securities, antitrust and tax), the contributions of legal history and the Law and Economics movement, and the demonstration of the potential of the legal profession evidenced by the *Brown v. Board of Education* decision (pp. 197–98). Interestingly, she finds the *Brown* decision inspiring to the legal profession, notwithstanding her earlier criticism that it was the "summit of romantic judging" (p. 156).

Glendon sees this system changing remarkably in the 1970s for a variety of reasons. "By the 1970s," Glendon writes, "law school had become the place for a bright, upper-middle-class liberal arts major to go when he still had no idea of what he wanted to do in life" (p. 201). Law professors were forced to adjust to this new student body by lightening their classes and becoming entertainers. Additionally, the LSAT was altered, dropping the quantitative sections and rewarding "verbal acrobats" (p. 203).

Law school faculties also changed, rejecting traditional legal scholarship epitomized by treatises and adopting more theoretical pursuits. The idea of a disinterested quest for knowledge was abandoned for politically loaded movements such as "advocacy" scholarship, Law and Economics and Critical Legal Studies. Nonetheless, the subsequent rivalries between law school faculty did not, in Glendon's mind, represent true diversity. Rather, faculties remained a rather homogeneous group. Politically, the "right" wing consists largely of "New Deal Democrats and libertarians, who are traditionalists with regard to scholarship and standards" (p. 216). True cultural conservatives and Republicans are rare. Faculty also increasingly share a general disdain for the corporate practice their students increasingly choose. According to Glendon, this point of view may stem from the fact that faculty predominantly come from elite law schools and increasingly consist of recent graduates who took few law courses after the obligatory first-year surveys and have little legal experience beyond judicial clerkships (pp. 217–18). Finally, she bemoans

an increasing tendency to view constitutional law as only rights-oriented, ignoring the issues of federalism and separation of powers.

Ultimately, Glendon wonders whether this system is adequately training new lawyers. Increasingly, law school classes are interdisciplinary pursuits taught by professors with little legal experience. This leads young lawyers to lack a true picture of how the legal system actually functions, what the settled law actually is, and what analysis goes into good legal advice. Why haven't students rebelled? Glendon claims that they have been pacified with less demanding classes, grade inflation, and the proliferation of law periodicals on which to participate.

Glendon is not, however, wholly critical of the new theoretical movement or wholly pessimistic about the future of legal education. She recognizes that traditional legal scholarship lacked any overriding theory and could only describe its mission with the cryptic refrain "[w]e're teaching them how to think like lawyers" (p. 233). Focusing on the work of Edgar Bodenheimer, Glendon finds that there is in fact a theoretical basis to thinking like a lawyer, namely the dialectical method through which available data and experience, forms and hypotheses, are tested against concrete particulars and weighed against competing hypotheses. Because the beginning premises are doubtful or in dispute, the goal is not certainty but the determination of which of the opposing positions is supported by stronger evidence (pp. 237–38). As law professors abandon teaching the dialectical method, law students are increasingly unable to "think like lawyers."

Glendon rejects this prognosis as too gloomy, however, citing the still significant numbers of professors who are content to train practicing lawyers and the increasingly productive cohabitation between theory and practice (pp. 244–46). Legal academia is also continuing to undergo transformation. This includes the rise of procedural teaching and scholarship, an area largely immune from theoretical strife, and a counter-reformation in constitutional law reuniting the subject with democratic theory. Students, in turn, are embodying what Glendon terms the "new postideological mood," pursuing more law classes and fewer liberal arts courses, and embracing demanding teachers with traditional teaching methods (pp. 249–50).

Glendon's final area of exploration concerns the role law now plays in our culture. Legalistic spirit, she asserts, permeates our society as its members increasingly adopt the vocabulary and

attitudes of hard-ball litigators. Once again, she perceives a breakdown of traditional "understandings," this time in the form of community and family structures that provided "nonlegal constraints on behavior and [ ] informal methods of handling disputes" (p. 264). This breakdown, in turn, puts increasing pressure on the courts to solve private disputes and to restore civility. This quick run to the courts to solve social ills, Glendon believes, has been largely ineffective and damaging to the political process. In addition, the middle class has been brought into a dispute resolution process that it cannot afford, further heightening aggravations with the system.

Thus, according to Glendon, the law has lost its proper place in our society. Whether a more productive balance can be reached will only be determined by the struggles among lawyers, judges and academics. Yet, despite the chaos Glendon finds to have ensued since the 1960s, "[t]hirty years is a short span in the life of traditions that have been evolving since the thirteenth century" (p. 288). Indeed, Glendon writes, young law students are increasingly realistic, Supreme Court decisions are less sensational, the boom years of practice are over, judges are recognizing limitations on their power, and academics are refraining from looking down their noses at constitutionalism and craft traditions, all "scattered signs that the extended orgy of legal hubris is winding down" (p. 288).

While Glendon's treatment of the fading traditional, ethical role of lawyers would seem to draw the most attention, it is the least satisfying section of the book. Glendon never addresses the legal profession as a whole, instead choosing to focus on corporate attorneys in large-firm practice. The "low-status" fields of personal injury, debt collection, domestic relations and criminal defense are largely dismissed (p. 67). Glendon never adequately explains why she views the loss of certain "understandings" among the relatively small minority of lawyers who practice in the "elite legal world" of large corporate firms as the key to the current ethical dilemmas and malaise within the entire legal profession. Did the majority of lawyers who practiced in the "low-status" fields not have these "understandings?" If they did not, has there been a fundamental change in the ethics of the profession? Or is this change merely the end of a fortunate time for elite lawyers who used to be able to avoid muddying their hands? If these "low-status" lawyers were able to maintain a higher ethical framework while practicing as raiders, they would

seem a better source for understanding how the dual roles can operate together more effectively.

Glendon is on firmer ground in her analysis of judicial decisions and the academic pursuits they inspire. Though hardly novel, her criticism of judicial activism is thoughtfully presented and adequately defended. The more interesting discussion, however, occurs when she raises the veil covering elite legal academia. Glendon provides a rare glimpse into the functioning of the Harvard Law School faculty and discusses the work and viewpoints of her colleagues with remarkable candor. Though generally appreciative of her colleagues' intellect, Glendon has a definite, arguably narrow, view of the role of legal education and defers little to fellow professors who disagree. Not surprisingly, older professors inspire her most pronounced praise.

Glendon's appreciation of the old guard and her view that things were better prior to the 1970s permeate the book. She regales the 1960s as the "golden age" when lawyers were ethical, judges were restrained, academics pursued the law, and families and communities were united. While Glendon refrains from wishing that modern American legal culture could somehow go back in time, her writing definitely gives one the sense that she believes that a legal and social nirvana has been lost in the last 30 years. One's initial reaction is to discard her view as naive, pessimistic, and reactionary. To do so, however, would miss the incredible utility of the book. Glendon has concisely and wittily expressed her opinion of where the legal community has come from, where it may be going, and why this may not be the best destination. This statement should not be taken as a rigid pronouncement of fact to be accepted or rejected summarily, but rather as a reasoned and multifaceted argument to which others may respond. If one agrees that the legal community should reflect upon its recent history and examine the consequences of recent trends, both positive and negative, Glendon's book provides an excellent basis for future discussion.

—Stephen Tackney

WELFARE REALITIES: FROM RHETORIC TO REFORM. By *Mary Jo Bane* and *David T. Ellwood.* Cambridge, Mass.: Harvard University Press, 1994. Pp. xvi, 220. $29.95 cloth.

The decades-long debate over welfare reform continues. As the first 100 days of the Republican Congress drift into the dog days of summer, the Contract with America's vision of welfare reform clashes with President Clinton's plan to "end welfare as we know it." Against such a backdrop, *Welfare Realities: From Rhetoric to Reform*, by prominent social scientists Mary Jo Bane[1] and David T. Ellwood,[2] performs two critical functions. The work offers an overview and synthesis of twenty-five years of social science research regarding Aid to Families with Dependent Children (AFDC).[3] Moreover, Bane and Ellwood offer concrete proposals to reform the current welfare system. Unfortunately, the authors ultimately fail to heed the implications of their own statistical analysis. Indeed, the book proposes a non-welfare system that contains many of the same weaknesses of the current AFDC system. The reader is left only with a sense of the limitations of the public assistance framework as a means of fostering self-sufficiency.

Welfare Realities is a compilation of five chapters written by different authors. "The Context for Welfare Reform," written by Bane and Thomas J. Kane,[4] presents a history of welfare reform since the 1960s and examines the current AFDC process. The chapter discusses the rise of what Bane and Kane call "the eligibility-compliance culture" within welfare administration, a culture that purportedly encourages recipients to focus on maintaining eligibility rather than on becoming self-sufficient (p. 7).

"Understanding Welfare Dynamics," the only chapter authored by Bane and Ellwood together, analyzes the quantitative research done on AFDC recipients since 1968.[5] The research reveals that

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[2] Assistant Secretary for Planning and Evaluation in the Department of Health and Human Services, on leave from the John F. Kennedy School of Government at Harvard University.

[3] Since the book concentrates on AFDC, the authors use "welfare" and "AFDC" interchangeably. I will do likewise.

[4] Assistant Professor of Public Policy, John F. Kennedy School of Government, Harvard University.

[5] The authors rely on the Panel Study of Income Dynamics (PSID), a survey that tracked the incomes of 5000 families and single adults from 1968 to 1988 (p. 31).

even though most persons starting a spell on AFDC will stay less than four years, half of those on welfare at any given time will have been recipients for eight or more years (pp. 30–31). The authors also note that teenagers, African Americans, high school dropouts, never-married mothers and women without recent work experience are the subgroups most likely to have long spells on AFDC (p. 48).

In "Understanding Dependency," Ellwood explores the usefulness of three models of welfare dependency. The rational choice model, employed by economists, explains long-term welfare use as a "series of reasoned choices in light of the available options" (p. 69). The expectancy model suggests that welfare dependency stems from a lack of control and confidence on the part of long-term recipients as to their ability to survive without welfare (p. 75). The cultural model proposes that a decline in the values of certain local communities, particularly those of the ghetto, has caused members thereof to view welfare as "a natural and legitimate alternative to either marriage or work" (p. 79). Ellwood concludes that some combination of the rational choice and expectancy models best explains welfare dynamics (p. 121). In doing so, he points out that the cultural model has not yet been sufficiently studied to be useful (p. 119).

In "Increasing Self-Sufficiency by Reforming Welfare," Bane explains her recommendations for reforming the current AFDC program, calling on her experience as Commissioner of the New York State Department of Social Services. Her proposals include streamlining eligibility rules and increasing benefits (pp. 136, 140). The author concentrates on the administration of job training programs, noting that whether mandatory or voluntary, a training program will be successful only if its administrators are dedicated to encouraging work—"What is necessary is a clear commitment and clear expectations that all clients can and are expected to participate in work or work preparation" (pp. 131–32).

The book climaxes with "Reducing Poverty by Replacing Welfare," where Ellwood presents his plan to replace welfare. This plan, which appeared in large part in one of his earlier books, *Poor Support*,[6] draws upon the historical interpretation and statistical analysis contained in the earlier chapters of *Welfare Realities*. Declaring that AFDC cannot be both a "program to en-

[6] DAVID T. ELLWOOD, POOR SUPPORT (1988.)

sure the long-term protection of children" and "a program to help people temporarily in times of trouble," Ellwood chooses the latter as his model for reform, a choice that he claims is consistent with the views of "all sides" involved in the most recent round of welfare reform (pp. 156–57). Accordingly, Ellwood seeks to present a temporary assistance program that encourages recipients to move off welfare and on to private-sector work and thus self-sufficiency.

As Ellwood's reform plan reflects the findings contained in the earlier chapters of *Welfare Realities*, it is an appropriate point of departure for critical analysis of the entire book. Ellwood prefaces his plan with the claim that "welfare does almost nothing to promote work or family or independence. Welfare almost never *solves* problems; it *salves* them with dollars" (p. 143) (emphasis in original). He then proceeds to set out three principles to guide his reform: (1) "people who work should not be poor"; (2) "children need support from both parents"; and (3) "[w]e ought to do more to help people help themselves, and we ought to expect more in return" (p. 143).

In order to help those who "play by the rules," Ellwood wants his proposed program to ensure that a full-time minimum wage worker will be able to support a family of four (p. 149). He accordingly proposes an Earned Income Tax Credit (EITC) triple the 1992 level,[7] noting that, in contrast to a minimum wage increase, an increased EITC imposes no costs on employers and thus does not result in fewer jobs (p. 149). Yet, a minimum wage hike is part of Ellwood's agenda as well. Conceding that even a tripled EITC would leave a family of four $2,500 below the poverty line, he proposes a $5.50 minimum wage which, when combined with the new EITC, would in fact allow a full-time worker to support his family (p. 150). According to Ellwood, the only alternative to raising the minimum wage is to provide food stamps, a move contrary to Ellwood's desire to keep working families out of the "welfare jumble" (p. 150).

Addressing his second principle, Ellwood proposes a universal and uniform system of mandatory child support. The plan has four elements: (1) both parents' Social Security numbers would be identified at birth; (2) child support payments would be set

[7] Ellwood notes that after the last chapter of the book was completed, President Clinton proposed, and Congress passed, a new EITC close to the level he had suggested (p. 150).

at a percentage of the income of the absent parent, usually the father; (3) all payments would be collected through automatic wage withholding by the employer; and 4) the government would assure that each child would receive $2,000 annually for support if a child support order were in place, even going so far as to make up the difference when collections fall short (p. 155). Ellwood recognizes that the fourth element will be the most controversial, but defends it by arguing that such a system will, at the very least, spur public debate about the parental responsibilities of fathers. He also notes that a universal system will serve mothers of all economic classes (pp. 155–56).

Ellwood recognizes that rapid adoption of the child support system that he proposes would leave those for whom a court order is not in place without child support payments in the short-run. In light of the fact that finding fathers can be a lengthy process, he advocates the provision of insured benefits to anyone making a good-faith effort to locate and identify the father (p. 161). Conceding that such a good-faith exception could be a large loophole, his only response to this possibility is that such a guarantee should "be written with considerable care" and that the good-faith provision should be phased out as the transition from welfare to the new system is completed (p. 161). In fact, he suggests that new enrollees should have to secure an award in order to be eligible for the insured child support (p. 161). Despite its shortcomings, his plan for insured child support features powerful incentives for self-sufficiency.

Ellwood's attempt to fulfill his third principle starts strong but ultimately fails to foster self-sufficiency. He proposes a transitional period between 18 and 36 months, depending on the age of the youngest child (p. 158). During that time, the recipient is eligible for job training and cash benefits. After that time, financial assistance would cease, although training would still be available (p. 157). Thus, "[a]fter benefits ran out, the only alternative for support would be to supplement child support with work" (p. 158). By focusing resources on "[a] rich set of training and support services" (p. 157) and using a strict deadline to provide incentive for participation in such services, Ellwood's welfare replacement plan provides powerful mechanisms for encouraging self-sufficiency.

These mechanisms are all but destroyed in the next paragraph. The startling shift justifies quotation at length:

> There are a number of concerns which must be addressed if we are to move to a truly transitional support system . . . . There will be people who cannot find work, and there will be regions where few jobs are available. If the government is not willing to provide cash support forever, *it must provide full- or part-time jobs for those who exhaust transitional support* . . . (p. 158) (emphasis added).

Here, the language of government guarantees enters Ellwood's plan. By providing what is essentially a good-faith exception for finding work, he risks eroding incentives for self-sufficiency.

Ellwood offers two replies to this problem. First, he argues that the guaranteed community service job program is not merely the "workfare" version of welfare under another name, for in workfare people "seem to be working for free," while in his program people would be paid for their work (pp. 159–60). This seems a rather semantic difference on which to distinguish a program and its radical replacement. One does not reform a program by changing the address on the government checks received thereby. Ellwood's mistake is looking at the problem from the wrong angle. Whether it is called "workfare" or Ellwood's "community service jobs," the positions are created for and provided to all applicants. These applicants need not compete in the job market nor hone their skills for the needs of today's business world. Indeed, Ellwood makes it clear that "if there are not enough jobs, one knows immediately and there is an impetus to find more" (p. 160). Both workfare and Ellwood's program thus give people work to do so that they can continue getting checks from the government.

This does not mean that Ellwood's program is entirely tantamount to workfare. Ellwood points out that with his program, "[w]hen people don't work, they don't get paid" (p. 160). If this means that clients can lose their jobs, then this plan is certainly a radical departure at least from workfare. Yet, that would also change the meaning of the government's obligation to "provide full- or part-time jobs, so that people can, in fact, support themselves" (p. 158). What would be the government's obligation to clients fired from its jobs program? Will they become part of the "system for exempting and protecting people who truly cannot work" (p. 160)? Will the government continue the cycle of training and jobs? The adoption of any of these options would render Ellwood's program hardly distinguishable from a mandatory workfare system.

Second, Ellwood suggests that whether guaranteed jobs are indeed workfare is largely irrelevant, for only a small proportion of transitional support-recipients would need the government-provided jobs (p. 158). He assumes that job training and EITC-based incentives to find private sector jobs will propel transitional support recipients to gainful private employment prior to their exhausting transitional benefits (pp. 158–59). The few recipients remaining would be given community service jobs. He thus concludes that his program will be considerably smaller than the current welfare system (p. 159).

This optimistic conclusion seems unwarranted. The rational choice model favored by the authors suggests that not only a reformed incentive structure but also job training is critical to encouraging welfare recipients to seek and accept private employment, for it supposedly raises the potential wages to be earned in the private sector (p. 74). Indeed, the fact that a disproportionate share of long-term welfare recipients lack high school diplomas and significant work experience highlights the importance of job training as a means of providing the employment skills that would enable one to escape welfare dependency (pp. 49–50). Thus, Ellwood would have his program offer "a rich set of training and support services" along with the cash benefits it provides (p. 159).

But will three years of job training be sufficient to deal with the complicated problems of those who have failed the traditional education system or the job market? The authors offer no assurance here. On the contrary, in "Increasing Self-Sufficiency," Bane admits that running a successful jobs program is "neither easy nor cheap, and will run afoul of both budget limitations and political commitments" (pp. 131–32). Moreover, if the cultural model of welfare dependency does in fact explain the welfare dynamics of certain communities, job training in such places would fail due to the presence of social norms that view welfare as a legitimate way to support oneself (p. 80).

Even if jobs programs were to instill benefit recipients with the skills necessary to compete in the private sector, the process of finding a job would not likely be easy. This may be problematic, in light of the expectancy model upon which the authors partly rely. The model suggests that if former benefit recipients encounter rejection during their job search, as is wont to happen, or lose their jobs when the economy falters, their sense of confidence and control might rapidly dissipate, causing them to retreat to

the security of benefit payments and guaranteed government jobs. More significantly, as previously mentioned, Ellwood concedes that "there will be regions where few jobs are available" (p. 158). His assertion that "a strong economy is good medicine" is surely accurate but hardly comforting to those who recognize, as does Ellwood, that the economy functions much like a "roller coaster" (p. 145). Ultimately, the reforms that Ellwood proposes fail to meet the stated goals of *Welfare Realities*. The book's plan salves without solving.

After examining the reasons why women go on AFDC, Bane and Ellwood declare, "These results lead to a critical conclusion: prevention is the best medicine" (p. 55). Although they were referring to single motherhood, the same conclusion could be applied to all the roots of welfare dependency. Ellwood's plan would fail to foster self-sufficiency because it starts with an intrinsic disadvantage—when the government steps in after people have dropped out of school and after jobs leave an area, it is very difficult to ensure that everyone is both provided for and self-sufficient. It seems that with *Welfare Realities*, Bane and Ellwood have pushed debate over welfare reform to its limit. The book provides a convincing analysis of both the history and the current dynamics of welfare. It also demonstrates the fundamental inability of welfare to overcome the larger problems of job disappearance and educational decline. Bane and Ellwood have thus set the agenda for a new round of social welfare debate.

—Peter Amuso

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