GENERAL LAW ISSUE

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DEDUCTION OF LITIGATION EXPENSES:
TRIAL LAWYERS V. I.R.S.

by Kelly Thrasher¹ and Joseph W. Blackburn²

I. OVERVIEW

Virtually every law firm in the nation has expended money on behalf of a client for litigation expenses without being paid a retainer first. Whether the money is spent under a contingency fee arrangement or for a long-time client that has a sudden emergency, lawyers are accustomed to writing checks out of their firms' accounts to cover everyday litigation costs such as filing fees, delivery expenses, and copying expenses. Sometimes the lawyer expects to be reimbursed; that reimbursement may be in as quick as a few days or it may be delayed until resolution of the claim, which could take years. Other times the lawyer expects to be reimbursed only if the action is successful. No matter what the circumstances, there are occasions where the lawyer spends money in furtherance of a client's case and is never repaid, or if repaid, the reimbursement is not until several years away.

As a cash basis taxpayer,³ the lawyer would prefer to deduct these litigation expenses as ordinary and necessary business expenses in the taxable year the amounts are expended against the income earned in that taxable year.⁴ If the lawyer is reimbursed in a subsequent year, then the lawyer would presumably be willing to include that reimbursement in that subsequent year's earned income.⁵

¹ Kelly A. Thrasher obtained a B.S. Degree in Accounting from Auburn University in 1998. Ms. Thrasher then obtained her J.D. Degree from the Cumberland School of Law, Samford University, in 2001. Ms. Thrasher would like to thank Dean Michael Floyd and Professor Joseph Snoe for their assistance in editing this article, as well as her family for their support.

² Joseph Blackburn graduated with honors in 1969 from the University of Kentucky, with a B.A. Degree. Mr. Blackburn obtained his J.D. Degree in 1974 from the University of Virginia. He is currently a Palmer Professor of Law at Samford University's Cumberland School of Law. Mr. Blackburn is also a Scholar in Residence at Sirote & Permutt, P.C., and he is a Member of the American College of Tax Counsel.

³ A cash basis taxpayer computes his taxable income by including all items which constitute gross income in the taxable year in which actually or constructively received while expenditures are deducted in the taxable year in which actually expended. See Treas. Reg. § 1.466-1(c)(1)(i) (2000).

⁴ See David A. Cooper, Litigation Costs Deductible Under 'Gross Fee' Setup, 24 TAX'N FOR LAW 279, 279-80 (1996). Ironically, the Service has not extended this same rationale to other businesses attempting to deduct ordinary and necessary business expenses when there was a possibility of reimbursement. See, e.g., Alleghany Corp. v. Commissioner, 28 T.C. 298, 305 (1957) (allowing an investment corporation taxpayer to deduct amounts as business expenses when the taxpayer had expended the amounts with a possibility of reimbursement); Electric Tachometer Corp. v. Commissioner, 37 T.C. 158, 162 (1961) (allowing a taxpayer to deduct moving expenses as ordinary and necessary business expenses when the taxpayer was forced to expend said expenses due to condemnation of its property and was later reimbursed by the State because although there was a contingent right of reimbursement, there was no fixed right of reimbursement).

⁵ See Cooper, supra note 4, at 280.
Although cash-method principles support the attorneys' position, the Internal Revenue Service would prefer to defer deductibility of the litigation expenses, especially if there is a possibility the lawyer will be reimbursed in a subsequent year, and then offset any non-reimbursed amounts against any amount recovered to calculate earned income for that subsequent year. If there never is any recovery, the Service would then allow the attorney to take a business bad debt deduction. For years, the Service and attorneys have disagreed over how to treat litigation expenses. Therefore, the courts have gotten involved.

Historically, the courts have taken the Service’s position in determining how litigation expenses should be treated. The courts have reasoned that in most cases the expenses were incurred under a contingency fee arrangement with a high probability of success, and thus there was a high expectation of recovery. The courts have also focused on the fact that ethical restrictions on attorneys have prohibited attorneys from becoming creditors of their clients, in order to avoid the possibility of the attorneys having a personal interest in the outcome of the litigation. In accordance with these ethical restrictions, the courts have treated any litigation costs expended in litigating a client’s claim as only an “advance” to the client. Thus, because ethically attorneys could only advance litigation expenses, the courts traditionally have refused to consider these expenses as the attorneys’ own expenses. Accordingly, attorneys have been denied immediate deductibility of litigation expenses.

Alabama lawyers recognized that if the advancement restriction was removed from Alabama’s ethical rule, then courts would no longer have any grounds on which to deny deduction of the litigation expenses. In 1994, the Alabama Bar Association proposed an amendment to Alabama’s Rule of Professional Conduct 1.8(e), which would allow Alabama lawyers to deduct

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6 Id.
7 Id.
9 Id.
10 Id.
11 See, e.g., Burnett, 356 F.2d at 760; Canelo, 53 T.C. at 224.
12 The Model Code of Professional Responsibility, replaced by the current Model Rules of Professional Conduct, contained restrictions prohibiting an attorney from advancing litigation expenses to his clients unless the client remained ultimately liable for the expenses. See MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 5-103(B) (1969).
15 Id.
16 Id.
17 See ALABAMA RULES OF PROFESSIONAL CONDUCT Rule 1.8(e) (2000).
these expenses as ordinary and necessary business expenses.\textsuperscript{18} The Alabama Supreme Court accepted this amendment,\textsuperscript{19} and to date, Alabama lawyers have been successful in paying these expenses on their own account and taking an immediate deduction in the year the amounts were expended.\textsuperscript{20}

A year after Alabama's change, the Court of Appeals for the Ninth Circuit allowed a California lawyer to take a current business expense deduction for litigation expenses expended under a gross fee contingency arrangement.\textsuperscript{21} Because the gross fee arrangement made no reference to the client reimbursing the attorney, the court recognized that the lawyer-client relationship under this type of payment schedule was no different from any other business that must make expenses in order to earn revenue.\textsuperscript{22} The court also refused to be bound by California's Rules of Professional Conduct, which only allowed advancements.\textsuperscript{23} The court reasoned that because there was another California law regulating contingency fee arrangements, the Rules of Professional Conduct were not exactly state laws, and further, the Rules of Professional Conduct were not generally enforced.\textsuperscript{24} Finally a court saw the inappropriateness of requiring litigation expenses to be deducted as a business bad debt deduction and allowed litigation expenses to be deducted as ordinary business expenses.\textsuperscript{25}

This Article will first focus in Parts II and III on the development in the courts of the deductibility of litigation expenses, as well as the history behind today's Model Rules of Professional Conduct. Next, Part IV examines the change in Alabama. Also, the treatment of litigation expenses in the surrounding southeastern states will be considered, including whether those Bar Associations have plans to move to a rule similar to Alabama's. Part V examines the courts' changing positions on gross contingency fee arrangements. The Article will conclude in Part VI with how law firms should petition for a change in their states' rules of professional conduct as well as how contingency fee arrangements should be worded in order to ensure deductibility of litigation expenses as ordinary and necessary business expenses.

II. HISTORY OF THE TAX TREATMENT OF LITIGATION EXPENSES

Historically, courts have treated costs expended by a lawyer in preparation of litigation under a contingency fee arrangement as a nondeductible loan, or "advance," to the client, rather than as a deductible business expense of the lawyer.\textsuperscript{26}

\begin{itemize}
\item \textsuperscript{18} See id.
\item \textsuperscript{19} See id.
\item \textsuperscript{20} See ALABAMA RULES OF PROFESSIONAL CONDUCT Rule 1.8(e) (2000).
\item \textsuperscript{21} See Boccardo v. Commissioner, 56 F.3d 1016, 1019-20 (9th Cir. 1995).
\item \textsuperscript{22} Id. at 1018.
\item \textsuperscript{23} Id. at 1019-20.
\item \textsuperscript{24} Id.
\item \textsuperscript{25} Id. at 1020.
\item \textsuperscript{26} See, e.g., Burnett v. Commissioner, 356 F.2d 755, 760 (5th Cir. 1966); Canelo v. Commissioner, 53 T.C. 217, 224 (1969); Silverton v. Commissioner, 36 T.C.M. (CCH) 817, 827 (1977); Watts v. Commissioner, 27 T.C.M. (CCH) 886, 887 (1968).\end{itemize}
A. Tax Code Distinctions

In order to understand the difference in treating litigation expenditures as unrecoverable loans rather than business expenses, the Tax Code must be examined.27 Attorneys prefer to deduct the litigation expenses under section 162, the ordinary and necessary business expense provision, because then the attorneys are allowed to take an immediate deduction of the expenses in the year the amounts were expended.28 The Service, however, requires attorneys to deduct only unrecoverable litigation expenses through section 166(a)(1), the bad debt provision, in the year that the amounts become uncollectible.29 The two treatments differ in how much of the litigation expenses may be deducted and in what taxable year.30

1. Section 162(a)

The business expenses provision, section 162(a), allows a deduction for “all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.”31 “Ordinary” has been defined as one that is normally to be expected based on the circumstances of the business activity, while “necessary” has been defined as one that is “appropriate and helpful to the business.”32 If the practice of law were viewed as a business, for income tax purposes, an attorney is in the business of prosecuting cases; thus, costs expended in pursuing these cases should be considered normally expected and also appropriate and helpful in order to litigate the claims.33 Accordingly, an attorney should be afforded the same treatment as other businesses that have expended amounts for normally expected, appropriate, and helpful reasons.34 Further, an attorney expends the costs in a certain year, yet the resolution of the case may not be for several years due to the lengthy nature of trials.35 The attorney, as a cash basis taxpayer, would prefer to accurately reflect his cash flows in the year the expense was paid and take advantage of this expenditure which has depleted his current cash flow, in accordance with the method utilized by other cash basis taxpayers, rather than waiting for possibly several years to offset the expenses against the recovery when, and if, it is finally recovered.36 Thus, the attorney would prefer to take advantage of the ordinary and necessary

28 See Eric S. Chofnas & Laine S. Walker, Deductibility of Litigation Costs May be Affected by Ethical as Well as Tax Factors, 18 TAX’N FOR LAW 82, 83 (1989).
29 Id.
32 Palo Alto Town & Country Village, Inc. v. Commissioner, 565 F.2d 1388, 1390 (9th Cir. 1977) (citing Commissioner v. Heininger, 320 U.S. 467, 471 (1943)).
33 See Chofnas & Walker, supra note 28, at 83.
34 Id.
36 Id.
business expense provision by deducting all of the litigation expenses, which are ordinary and necessary to the business of litigating, in the taxable year the expenses were expended.\textsuperscript{37}

2. Section 166(a)(1)

Instead of permitting a deduction, the Internal Revenue Service has traditionally treated these expenses as a loan to the client under section 166(a)(1), the business bad debt provision.\textsuperscript{38} Loans are not deductible in the year the money is loaned on the theory that the money will be repaid; thus the taxpayer has merely exchanged one asset for another, with no reduction in wealth.\textsuperscript{39} Once the loan is determined to be unrecoverable, the taxpayer is then allowed a bad debt deduction under section 166(a)(1).\textsuperscript{40} In other words, when the case has been unsuccessful, pursuant to the contingency fee arrangement and the Model Rules of Professional Conduct, the client is not obligated to repay the expenses.\textsuperscript{41} Thus the attorney essentially has a bad debt and is then entitled to a deduction in that subsequent year.\textsuperscript{42} But, in order to qualify for a bad debt deduction, there must first be a bona fide debt.\textsuperscript{43} The crux of the argument between the Service and attorneys is whether litigation expenses are bona fide debts.\textsuperscript{44}

Treasury Regulation 1.166-1(c) defines a debt, or loan, as a "valid and enforceable obligation to pay a fixed or determinable sum of money."\textsuperscript{45} A deduction cannot be taken if the repayment of the loan is contingent upon some event or the loan was made without a reasonable expectation of being repaid.\textsuperscript{46} Thus, attorneys argue that because the repayment of the expenses is always contingent on success at trial, there is never really a loan.\textsuperscript{47} To determine

\begin{itemize}
  \item \textsuperscript{37} See Palo Alto Town & Country Village, Inc. v. Commissioner, 565 F.2d 1388, 1390 (9th Cir. 1977) (citing Commissioner v. Heininger, 320 U.S. 467, 471 (1943)).
  \item \textsuperscript{38} See 26 U.S.C. § 166(a)(1) (1994). Section 166(a)(1) states, "There shall be allowed as a deduction any debt which becomes worthless within the taxable year." \textit{Id}.
  \item \textsuperscript{39} See Robert N. Amkraut, Note & Comment, \textit{Taxing Contingency Fee Attorneys as Investors: Recognizing the Modern Reality}, 71 WASH. L. REV. 745, 745 (1996); see also Herrick v. Commissioner, 63 T.C. 562, 568 (1975) (following precedent and holding that litigation expenses were actually loans because repayment was a contingent possibility, and thus not deductible as ordinary and necessary business expenses).
  \item \textsuperscript{40} See Canelo v. Commissioner, 53 T.C. 217, 226 (1969); see also Hearn v. Commissioner, 309 F.2d 431 (9th Cir. 1962), aff'd 36 T.C. 672 (1961) (holding that an attorney could not deduct litigation expenses until the "debts" were considered uncollectible).
  \item \textsuperscript{41} See Canelo, 53 T.C. at 226; see also Hearn v. Commissioner, 309 F.2d at 431, aff'd 36 T.C. 672 (1961).
  \item \textsuperscript{42} See Amkraut, supra note 39, at 745-46.
  \item \textsuperscript{43} See Goldstein v. Commissioner, 40 T.C.M. (CCH) 752, 754 (1980); see also Hodges v. Commissioner, 66 T.C.M. (CCH) 155, 156 (1993) (finding that no debtor-creditor relationship existed in order to take a bad debt deduction under section 166(a)(1)).
  \item \textsuperscript{44} See Goldstein, 40 T.C.M. (CCH) at 754; see also Hodges, 66 T.C.M. (CCH) at 156.
  \item \textsuperscript{45} Treas. Reg. § 1.166-1(c) (2000).
  \item \textsuperscript{46} See Goldstein, 40 T.C.M. (CCH) at 755.
  \item \textsuperscript{47} See, e.g., Burnett v. Commissioner, 356 F.2d 755, 759 (5th Cir. 1966).
\end{itemize}
whether a loan exists, however, the parties' actual intentions must be considered, not whether there was actually a loan and repayment. Accordingly, the Service has argued that under a contingency fee arrangement, the attorney has such high expectations of recovery that it can be construed that he was intending only to make a loan. Because the Service considered litigation expenses to be loans, litigation expenses, although often contingent, cannot be deducted until they have been determined uncollectible. The dispute over whether litigation expenses should be deducted immediately using the ordinary and necessary business expense provision or be required to take a deferred deduction using the bad debt provision eventually caused the courts to become involved to determine the true nature of litigation expenses.

B. Development of courts' rationales for treatment of litigation expenses as advances

The Service's and the attorneys' positions are both internally consistent. However, courts have relied on several different rationales for siding with the Internal Revenue Service and adhering to the legal fiction that an attorney is only making a loan to the client and is not entitled to deduction until the year the loan becomes worthless.

In the first case in which a court addressed this issue, the United States Board of Tax Appeals held that because the attorney had an unconditional right to recovery, the attorney was not entitled to a business expense deduction because the costs were only advanced to the client. Although this case did not involve a contingency fee situation as most of the later cases did, this case served as precedent for following cases that such costs should be treated as loans under section 166(a)(1) rather than as business expenses under section 162(a).

In the next few cases, the courts focused on the facts that the attorneys had carefully screened clients so that costs were expended only on those cases in which the attorneys had high expectations of recovery and the attorneys actually recovered a large percentage of the amounts expended. The high expectations of recovery and substantial actual recovery allowed the courts to conclude that

48 See Goldstein, 40 T.C.M. (CCH) at 756.
50 Id.
51 See Palo Alto Town & Country Village, Inc. v. Commissioner, 565 F.2d 1388, 1390 (9th Cir. 1977) (citing Commissioner v. Heininger, 320 U.S. 467, 471 (1943)).
54 Id.
55 See Cochrane, 23 B.TA. at 207.
56 See, e.g., Burnett, 356 F.2d at 759 (attempting to distinguish Cochrane).
the litigation expenses were loans even though reimbursements were contingent on success at trial. 58

In the late 1980s, the courts began to advance another reason as to why the expenditures should be treated as loans rather than business expenses: Ethical restrictions on lawyers permitted only the advancement of costs. 59 Perhaps the courts were realizing the fallacy of requiring contingent litigation expenses to be treated as loans and needed another rationale for denying immediate deductibility of litigation expenses. Regardless, using any of these rationales, attorneys have traditionally not been allowed to deduct litigation costs as business expenses. 60

1. Unconditional right to recovery theory

The first time a court considered litigation expenses incurred on behalf of a client, the court found that because the attorney possessed an unconditional right to recovery, the litigation expenses were not deductible. 61 In Cochrane v. Commissioner, 62 Mr. Cochrane, a New York attorney, had agreed to obtain a divorce for the daughter of a long-established client and personal friend. 63 The customary arrangement with this particular client was that Mr. Cochrane would perform any services and make any needed disbursements during the engagement, and when the services were rendered, the client would reimburse Mr. Cochrane for his disbursements as well as pay his fee. 64 This was also the arrangement used for the divorce proceedings. 65 In preparation of the divorce, Mr. Cochrane spent $5,000 by hiring an investigator, researching the laws of other states (as the daughter could not obtain a divorce in New York), traveling to Nevada (the eventual setting for the divorce), and other similar expenses. 66 After the divorce was granted, Mr. Cochrane informed the client that his expenses totaled $5,000 and his fee was $5,000. 67 The client immediately paid him $10,000, all of which Mr. Cochrane reported as income on his tax return. 68 Mr. Cochrane deducted the $5,000 of expenses incurred in preparation of the divorce. 69 The Internal Revenue Service assessed a deficiency in Mr. Cochrane's

58 See, e.g., Burnett, 356 F.2d at 760; Canelo, 53 T.C. at 224.
60 Id.
63 Id.
64 Id.
65 Id.
66 Id. at 203-04.
67 Id. at 204.
68 See Cochrane, 23 B.T.A. at 204.
69 Id.
income taxes on several grounds, including the tax treatment of the litigation expenses.70

In the United States Board of Tax Appeals, Mr. Cochrane argued that the $5,000 expenses should be deducted from income as “ordinary and necessary business expense[s] incurred and paid by him in obtaining a divorce for the daughter of one of his clients.”71 The court held that the expenses were not ordinary and necessary business expenses but rather advancements on behalf of his client for which the client unconditionally agreed to reimburse him, and thus could not be deducted.72 The court focused on the arrangement with the client and the fact that the client agreed from the outset to reimburse Mr. Cochrane for any expenses.73 Although the court did not allow the deduction of the expenses, the court held that because the amounts constituted advancements to the client, the amounts did not constitute income to Mr. Cochrane when he was reimbursed.74 Because Mr. Cochrane had an unconditional right to recovery, the court treated the litigation expenses as loans, which Mr. Cochrane could deduct only if the client never repaid him.75 Accordingly, the issue of litigation expenses with an unconditional right to reimbursement was staunchly resolved in favor of the Internal Revenue Service; however, attorneys still had an argument for litigation expenses with only a contingent right of reimbursement.76

2. High expectation of recovery theory

In the next line of cases, the courts were faced with the same issue but with a pure contingency fee arrangement.77 If the lawyers were not successful in resolving the claim, the client was not obligated to pay.78 The attorneys attempted to distinguish the contingent nature of the expenditures from the unconditional right of recovery that seemed to be the crucial factor in Mr. Cochrane’s case.79 The courts instead held that the attorneys had such a high expectation of recovery that, although contingent, the expenses should still be treated as advances.80

70 Id. at 202.
71 Id. at 207.
72 Id. at 207-08.
73 Id. at 207.
74 See Cochrane, 23 B.T.A. at 208.
75 Id. at 207.
76 See, e.g., Burnett v. Commissioner, 356 F.2d 755, 757 (5th Cir. 1966); Canelo v. Commissioner,
77 Id.
78 See, e.g., Burnett, 356 F.2d at 757; Canelo, 53 T.C. at 218.
79 See, e.g., Burnett, 356 F.2d at 759; Canelo, 53 T.C. at 223.
80 See, e.g., Burnett, 356 F.2d at 760; Silvertown v. Commissioner, 36 T.C.M. (CCH) 817, 827
(1977) (holding that the attorney presented no substantial evidence to show that litigation expenses
were actually not recovered, thus litigation expenses with a high probability of recovery were to be
treated as loans and not ordinary and necessary business expenses); Watts v. Commissioner, 27
T.C.M. (CCH) 886, 887 (1968) (holding that litigation expenses were not ordinary and necessary
business expenses even though the attorney only recovered 84% of the amounts expended because
In the first case, Mr. Burnett, a Texas lawyer, routinely provided living expenses to clients he represented in workers’ compensation and personal injury cases on a contingency fee basis. Mr. Burnett attempted to distinguish his expenditures as deductible ordinary and necessary business expenses because the clients were not unconditionally obligated to repay the amounts as the client was in Cochrane. Under the contingency fee arrangement, if Mr. Burnett was successful in litigating the client’s claim, the recovery would first be applied to repay those living expense expenditures and then any remainder would be divided between Mr. Burnett and the client according to previously agreed-upon percentages.

The United States Court of Appeal for the Fifth Circuit did not accept Mr. Burnett’s distinction and affirmed the United States Tax Court’s holding that the amounts were not deductible ordinary and necessary business expenses. The appellate court acknowledged that repayment was conditional upon the success of the case; however, the court focused on the fact that Mr. Burnett only paid living expenses for those clients for which he was “virtually certain” would be repaid. The court pointed out that section 162(a) requires determining whether an expenditure can be an expense based on the circumstances and conditions under which it was made. The court recognized that reimbursement was tied to the recovery of a client’s claim, thus indicating a contingent reimbursement; however, Mr. Burnett only advanced assistance to those clients whose claims had a high probability of success. The court further relied on the fact that Mr. Burnett actually experienced a high rate of return on the advances, with only $4,417 out of approximately $290,000 over a five-year period becoming worthless. Because of this evidence, the court held the amounts to be loans rather than business expenses.

The amounts in question, however, were for the clients’ living expenses; amounts expended for court costs and other litigation fees were remanded to the Tax Court to determine if they could qualify for section 162(a) deductibility. Accordingly, attorneys could still argue that pure litigation expenses with a

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81 356 F.2d 755 (5th Cir. 1966).
82 See Burnett, 356 F.2d at 757.
83 Id.
84 Id.
85 Id. at 759; see also Burnett v. Commissioner, 42 T.C. 9, 12 (1964).
86 Burnett, 356 F.2d at 759.
87 Id. at 759-60.
88 Id. at 760.
89 Id.
90 Id.
91 Id. at 761.
contingent right to reimbursement should be treated as ordinary and necessary business expenses.

b. Canelo v. Commissioner\textsuperscript{92} Three years later, the Tax Court extended the Burnett rationale to amounts expended on behalf of the client for typical litigation costs, such as travel expenses, cost of medical records, witness fees, deposition costs, filing fees, process fees, etc.\textsuperscript{93} Mr. Canelo and Mr. Kane, California attorneys in partnership together, specialized in tort liability and personal injury litigation and often operated under contingency fee arrangements.\textsuperscript{94} Like the arrangement in Burnett, the contingency fee contract provided that Mr. Canelo and Mr. Kane would advance the necessary court costs and expenses in prosecution of the claim, and then, if successful, the advanced costs would be repaid out of the recovery.\textsuperscript{95} Again, reimbursement was contingent on success.\textsuperscript{96} Mr. Canelo and Mr. Kane contended that because the repayment was contingent on success, the expenditures were “for the attorney’s own account,” and thus, should be deductible as ordinary and necessary business expenses.\textsuperscript{97} 

Mr. Canelo and Mr. Kane attempted to distinguish Burnett based on the different use of the amounts expended; the money advanced by Mr. Canelo and Mr. Kane was for litigation expenses, not living expenses.\textsuperscript{98} The court, however, held that this distinction was “without substance,” and instead emphasized that the “nature and the facts and circumstances under which the expenditures were made” was determinative of whether the expenses were deductible.\textsuperscript{99} The court held that “[i]f expenditures [were] made with the expectation of reimbursement, it follows that they [were] in the nature of loans.”\textsuperscript{100} Because Mr. Kane and Mr. Canelo screened clients and had “good hopes” of recovery, the court characterized the amounts as advances even though reimbursement was contingent.\textsuperscript{101} The court pointed out that these expenditures were made on “behalf of a particular client, under a reimbursement agreement signed by the client, to pursue a claim held by the client—a claim of no use to any person other than the client,” and thus, were different from the ordinary business expenses expended in anticipation of recovering them through success of the business.\textsuperscript{102} Because the expenses belonged to the client, litigation expenses were on the

\textsuperscript{92}53 T.C. 217 (1969).
\textsuperscript{93}See Canelo, 53 T.C. at 219, 225.
\textsuperscript{94}Id. at 218.
\textsuperscript{95}Id.
\textsuperscript{96}Id.
\textsuperscript{97}Id. at 223.
\textsuperscript{98}Id. at 225.
\textsuperscript{99}Canelo, 53 T.C. at 225.
\textsuperscript{100}Id.
\textsuperscript{101}Id. at 224.
\textsuperscript{102}Id. at 225.
client's account, not the attorneys', and thus, Mr. Canelo and Mr. Kane could not
deduct litigation expenses as ordinary and necessary business expenses.103

Mr. Canelo and Mr. Kane also argued that if the amounts had to be
considered loans, the loans should also be considered under section 166(a)104 and
therefore the attorneys should be able to establish a reserve for bad debts.105 The
attorneys argued that the expenditures were not based on an unconditional
obligation to be repaid until the case was closed.106 The court noted that with
still pending cases, there was not yet an unconditional obligation, so no
immediate deduction could be allowed for a bad debt.107 However, the court
conceded that if the case was closed, and the attorneys had not recovered the
advances, then they were allowed a bad debt deduction.108 Thus, the court
allowed the attorneys to deduct the contingent litigation expenses when an
unconditional obligation arose.109

When trying to reconcile the "unconditional obligation" language with the
contingency of the reimbursement of the litigation expenses, perhaps the court
realized that this argument did not have much vitality and other authority was
needed. In a footnote, the court referred to the American Bar Association's
Model Code of Professional Responsibility provision which allowed a lawyer to
advance the expenses of litigation as long as the client remained ultimately liable
for the expenses.110 This footnote hinted at another line of reasoning for denying
the current deductibility of litigation expenses which was to be developed
later.111

c. IRS Technical Advice Memorandum Decision

More than a decade after Canelo, a taxpayer petitioned the Internal Revenue
Service seeking advice as to whether the Service had changed its position on
litigation expenses.112 The taxpayer's situation was virtually identical to Canelo;
however, the taxpayer presented section 6(14) 4.5 from part IV of the Internal
Revenue Manual as authority that the Service had decided to allow litigation
expenses to be deducted as business expenses.113 The proffered section of the
Audit Technique Handbook stated:

103 Id. at 224.
104 "There shall be allowed as a deduction any debt which becomes worthless within the taxable
105 See Canelo, 53 T.C. at 225.
106 Id. at 225-26.
107 Id. at 226.
108 Id.
109 Id.
110 Id. at 225, n.3.
Commissioner, 65 T.C.M. (CCH) 2739, 2743 (1993).
113 Id. (referring to I.R.S. Manual 6(14)4.5 (1981)).
In addition to the ordinary expenses of the profession, an attorney has expenses on behalf of clients. Generally, advances in cash for expenses incurred by an attorney on behalf of a client are not deductible where the attorney is entitled to reimbursement and in fact is to be reimbursed. The usual practice in regard to a client's cost on a case is to charge for the costs and deduct them from the settlement received. In personal injury claim cases taken on a contingent fee basis, the attorney may not be entitled to reimbursement, therefore, the expense would be deductible in the year expended. If claimed as current expenses, the examiner should determine that the proper amount is included in income when a settlement is received.114

The Service rejected the taxpayer's argument, pointing out that the Internal Revenue Service Manual was not binding upon revenue agents conducting an audit, but only existed to provide assistance when reviewing complex issues that were particular to a specific industry.115 By doing so, the Service represented that the statement in the Internal Revenue Service Manual did not illustrate that the Service was changing its position on the tax treatment of litigation expenses.116 Instead the IRS preferred the treatment the courts had been applying to litigation expenses.117

3. Ethical restrictions theory

In the 1980s, the ethical restrictions placed on attorneys became another reason the courts denied current deductibility of litigation expenses.118 The ethical restrictions in effect at this time only allowed litigation costs to be advanced, with the client remaining ultimately liable for repayment.119 Because of the ethical requirement that the client retain ultimate liability, the courts continued to require that litigation expenses be deducted under the bad debt provision, if and when the expenses were determined uncollectible, rather than an immediate deduction under the business expense provision.120

a. Boccardo 121

The United States Claims Court was one of the first courts to apply the ethical restrictions as a way to prevent deductibility of litigation expenses.122 Mr.

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114 Id. (citing I.R.S. Manual 6(14)4.5 (1981)).
115 Id.; see also Sloane, supra note 49, at 472-73.
116 See Chofnas & Walker, supra note 28, at 84.
117 Id.
119 See Chofnas & Walker, supra note 28, at 85.
122 See Boccardo, 12 Cl. Ct. at 185-86.
Boccardo, a California lawyer specializing in contingency personal injury cases, was also attempting to deduct costs disbursed for preparation and trial costs. Like Mr. Canelo, Mr. Kane and Mr. Burnett, he “expected to win most of [his] cases and, thereby, receive reimbursement of [his] expenses.” The United States Claims Court followed precedent and determined that the amounts were loans, and thus, not deductible. The court relied on the fact that Mr. Boccardo expected to be reimbursed, screened clients carefully, and recovered 90% of his expenses when only 70% of his cases were successful, thus illustrating that he used discretion when deciding which clients would be advanced expenses. Because Mr. Boccardo was virtually certain to be repaid for the litigation expenses, the court allowed contingent litigation expenses to be treated as loans.

In this opinion, however, the Rules of Professional Conduct were not tucked away in a footnote, but rather used to begin the court’s discussion. The court referred to Rule 5-104 of the California Rules of Professional Conduct, which allowed California attorneys to “advanc[e] the costs of prosecuting or defending a claim or action or otherwise protecting or promoting the client’s interests.” The court did not make much use of rule 5-104 other than to reemphasize the traditional theory that the attorney was only “advancing” funds to the client rather than outright paying for the expenses on the attorney’s own account. Either way, it was evident that other support was needed to continue requiring litigation expenses to be treated as loans as the high expectation of recovery theory was weakening.

b. Boccardo II

Six years later, Mr. Boccardo was back in court again trying to deduct litigation expenses. After his loss in the United States Claims Court, Mr. Boccardo restructured his fee policy whereby he was utilizing two different fee arrangements, the gross fee arrangement and the net fee arrangement. The essential difference between the two was that the net fee arrangement specifically provided that litigation costs were to be repaid to the law firm as well as the law firm’s percentage of the recovery, whereas the gross fee arrangement only allowed the law firm to recover its percentage of the

123 Id. at 185.
124 Id.
125 Id. at 188.
126 Id. at 187-88.
127 Id. at 186.
128 See Boccardo, 12 Cl. Ct. at 185-86.
129 Id.
130 Id. at 186.
131 Id.
134 Id. at 2740.
recovery. Mr. Boccardo acknowledged that litigation costs advanced to clients represented under a net fee arrangement were not deductible. However, based on tax counsel’s suggestion, Mr. Boccardo contended that litigation costs expended for cases under a gross fee arrangement should be deductible because the arrangement indicated no right of reimbursement. The IRS disagreed, however, and disallowed the deduction because the IRS contended that Mr. Boccardo did have an expectation of reimbursement and the California Code of Professional Responsibility allowed attorneys only to advance, not pay, litigation costs. As usual, the court had to decide.

The United States Tax Court found no distinction between the two arrangements but did acknowledge that reimbursement might be more uncertain under the gross fee arrangement. Instead, the court relied on the actual reimbursement rate of the litigation costs and the careful screening of each client before paying for litigation expenses. The court held that “[t]he fact that the gross fee arrangements provide for reimbursement solely from recovery on the client’s claim operates only to affect the degree of contingency” and “the contingent nature of reimbursement was specifically rejected as a reason for concluding that the costs paid by a law firm were not advanced with the expectation of reimbursement.” Accordingly, Mr. Boccardo could not immediately deduct the litigation expenses under either arrangement, regardless of whether reimbursement was contingent on success at trial.

Mr. Boccardo also tried to argue that the advanced costs were reimbursed from the percentage paid to the lawyer as the legal fee, not the actual recovery, thus the expenses should be deductible. This court responded to this argument with California Rules of Professional Conduct rule 5-104, which allows an attorney to pay costs incurred by or for a client as long as the costs are “repaid

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135 Id. The net fee arrangement stated:

The Law Firm shall pay all costs. I understand that such payments are not a loan or an advance. All such costs shall be repaid to the Law Firm only out of any recovery. The attorneys’ fees will be based on the percentage of the recovery after deducting costs. The Law Firm’s fee for attorneys’ services is 33 1/3% of the net sum recovered in the event that said claim is settled before commencement of trial, otherwise 40% of said net sum. In the event there is no recovery on said claim, the Law Firm shall receive nothing for its services or for costs.

136 Id.

137 Boccardo, 65 T.C.M. (CCH) at 2740.

138 Id. at 2742-43.

139 See Boccardo, 65 T.C.M. (CCH) at 2741.

140 Id.

141 Id. at 2741-42.

142 Id. at 2743.

143 Id. at 2742.
from funds collected . . . for the client" or the costs were advanced in prosecuting the claim. The court stated, "The recovery belongs to the client, not the firm. Thus, the reimbursement of costs to the firm comes from the recovery of the client." The court applied the California Rules of Professional Conduct to the facts to find that the litigation expenses must have been advanced to the client or else the contingency fee contract would have violated California rule 5-104. Again, the court had to use the ethical restriction in order to support its finding that the litigation expenses with a contingent right of reimbursement were actually loans and not business expenses.

c. Milan v. United States

In 1988, the United States District Court for the Eastern District of Michigan applied the ethical argument rationale to similar facts. In Milan, a Michigan attorney was also representing personal injury clients on a contingent fee basis. The court followed the United States Claims Court in the Boccardo case, and its reasoning was based on the California Rules of Professional Conduct. The court focused on the Michigan Bar’s Code of Professional Responsibility, which stated that “[w]hile representing a client in connection with contemplated or pending litigation, a lawyer shall not advance or guarantee financial assistance to his client, except that a lawyer may advance or guarantee the expenses of litigation, . . . provided the client remains ultimately liable for such expenses.” The court held that because of the Michigan State Bar’s requirement, the court must find, as a matter of law, that litigation costs were only advances to clients and not deductible as ordinary and necessary business expenses. Thus, because of state ethical restrictions, attorneys still could not deduct litigation expenses as ordinary and necessary business expenses.

When the courts began relying on ethical restrictions rather than just the high probability of reimbursement as support for requiring litigation expenses to

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144 Id. at 2742-43.
145 See Boccardo, 65 T.C.M. (CCH) at 2743.
146 Id.
147 Id.
150 Id. at 693.
151 Id. at 694 (following Boccardo v. United States, 12 Cl. Ct. 184 (1987)).
152 Id. at 695.
153 Id. Other state courts have held similarly. See, e.g., In re Carroll, 602 P.2d 461, 466 (Ariz. 1979) (holding that attorney violated state ethical rule DR 5-103(B) by making advances to clients without keeping the client ultimately liable for the repayment of such expenses because such treatment resulted in the attorney buying an interest in the litigation); Brown & Huseby, Inc. v. Chrietberg, 248 S.E. 2d 631, 633 (Ga. 1978) (holding that state ethical rule DR 5-103(b) was constitutional); In re Berlant, 328 A.2d 471, 478 (Penn. 1974) (affirming the suspension of attorney’s license for making improper advances to clients, among other ethical violations).
154 See Milan, 679 F. Supp. at 695.
be treated as loans, attorneys began to have a better opportunity to change the tax treatment to allow immediate deductibility under the ordinary and necessary business expense provision, by changing the ethical rules. The American Bar Association has suggested rules of conduct for attorneys for almost a century. These model ethical restrictions have been changed several times over the years, and moreover, states have the privilege of modifying their ethical restrictions to implement changes from the model rules in response to their particular state bar's requests. This Article next focuses on the development of the model ethical restrictions as well as measures that states, specifically Alabama, are taking to allow immediate deductibility of litigation expenses.

III. HISTORY OF ETHICAL RESTRICTIONS

Ethical restrictions have long placed limits on what attorneys could do in advancing litigation costs for their clients, especially if operating under a contingency fee arrangement. In the United States, the ethical limitations have evolved from strictly prohibiting advances to clients, to allowing advances as long as the client remained ultimately liable, to finally allowing advances where repayment was contingent on the outcome. Today's ethical restrictions are different from the ethical restrictions of the early 1980s, and thus, a change may be possible in the tax treatment of litigation expenses. But, in order to understand the possibility of this change, the development of ethical restrictions placed on attorneys must first be considered.

A. Common law ethical restrictions

In England and the early United States, the client was regarded as being the owner of a legal claim. Because the client was the owner of the claim, it followed that the client should bear the litigation expenses expended for the claim. The early ethical rules were designed to ensure client ownership and prohibit attorney ownership through the practices of maintenance and champerty. Maintenance was the practice of "improperly stirring up litigation and strife by giving aid to one party to bring or defend a claim without just cause

155 See CANONS OF PROFESSIONAL ETHICS (1908); MODEL CODE OF PROFESSIONAL RESPONSIBILITY (1969); MODEL RULES OF PROFESSIONAL RESPONSIBILITY (1983).
156 Id.
157 See Amkraut, supra note 39, at 751-53.
158 See CANONS OF PROFESSIONAL ETHICS Canon 42 (1908).
159 See MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 5-103(B) (1969).
160 See MODEL RULES OF PROFESSIONAL RESPONSIBILITY Rule 1.8(e) (1983).
161 Id.
162 See Amkraut, supra note 39, at 751.
163 Id.
or excuse."165 Champerty was a specialized form of maintenance whereby the person “assisting another’s litigation [the lawyer] becomes an interested investor because of a promise by the assisted person [the client] to repay the investor [the lawyer] with a share of any recovery.”166 Thus, the early ethical rules were focused on “prevent[ing] meritless claims by prohibiting attorneys from ‘investing’ in their clients’ cases.”167 There was particular concern that a lawyer’s judgment might become corrupted if he had an investment in the client’s case.168 Specifically, the contingency fee arrangement was often perceived as allowing attorneys to acquire an investment in the clients’ cases because the attorneys were spending their own money on behalf of the clients in pursuit of the clients’ claims.169

**B. Ethical development of contingency fee arrangements**

Because contingency fee arrangements were perceived as allowing an attorney to acquire an investment in his client’s case, contingency fee arrangements were considered champertous until the end of the 19th Century.170 The 1908 Canons of Professional Responsibility accepted the use of contingency fee arrangements; however, some states continued to prohibit the use of such arrangements.171 In 1965, Maine finally repealed the last prohibition on contingency fee arrangements in the United States.172 Today, the use of contingency fee arrangements is still disallowed in England and parts of Canada.173 In the United States, however, contingency fee contracts are the most commonly used fee arrangement for personal injury plaintiffs’ attorneys.174 Throughout the development of ethical restrictions, special emphasis has been placed on the contingency fee arrangement to ensure the attorney’s independence.175

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165 CHARLES W. WOLFRAM, MODERN LEGAL ETHICS, § 8.13 (1986). See also Vaughan v. Marable, 64 Ala. 60, 66 (1879) (defining maintenance as the “officious intermeddling in a suit that no way belongs to one, by maintaining or assisting either party, with money or otherwise, to prosecute or defend it.”).

166 Id. See also Holloway v. Lowe, 7 Port. 488 (Ala. 1838) (defining champerty as “the unlawful maintenance of a suit, in consideration of some bargain, to have a part of the thing in dispute or some profit out of it”).

167 Amkraut, supra note 39, at 752.


169 See WOLFRAM, supra note 165, at § 9.4.1.

170 Id.

171 Id.

172 Id.

173 Id.

174 See Amkraut, supra note 39, at 747.

175 Id. at 751-53.
C. Code of Legal Ethics

In 1887, the United States' first rules regarding ethical restrictions placed upon attorneys, the Code of Legal Ethics, were adopted in Alabama.\textsuperscript{176} The Code of Legal Ethics contained regulations against "stir[ring] up litigation"\textsuperscript{177} and becoming creditors of clients,\textsuperscript{178} among others.\textsuperscript{179} By 1908, eleven other states had adopted similar ethical codes.\textsuperscript{180} In response, the American Bar Association finally considered drafting a model ethical code, using Alabama's Code of Legal Ethics as a model.\textsuperscript{181} Because the Code of Legal Ethics only regulated Alabama attorneys' behavior, a discussion on the specific provisions of the Code of Legal Ethics will be deferred until the discussion on the historical development of ethical restrictions in Alabama.

D. Canons of Professional Ethics

On August 27, 1908, the American Bar Association adopted the Canons of Professional Ethics, which was based largely on Alabama's Code of Legal Ethics with some changes incorporated from the other states' codes.\textsuperscript{182} Canon 28\textsuperscript{183}

\textsuperscript{176} See Judge Walter B. Jones, Canons of Professional Ethics, Their Genesis and History, 2 ALA. LAW. 247, 247 (1941). Colonel Thomas Goode Jones was the drafter of the Code. \textit{Id.} at 247. Jones went on to serve two terms as governor of Alabama and was appointed United States Judge for the Northern and Middle Districts of Alabama. \textit{Id.}

\textsuperscript{177} Rule 20 of the Alabama Code of Legal Ethics stated:

\begin{quote}
It is indecent to hunt up defects in titles and the like and inform thereof, in order to be employed or bring suit; or to seek out a person supposed to have a cause of action, and endeavor to get a fee to litigate about it except where ties of blood relationship or trust, make it an attorney's duty; it is unprofessional to volunteer advice to bring a law suit. Stirring up strife and litigation is forbidden by law, and disreputable in morals.
\end{quote}

\textit{Jones, supra note} 176, at 266.

\textsuperscript{178} Rule 38 of the Alabama Code of Legal Ethics stated: "Attorneys should, as far as possible, avoid becoming either borrowers or creditors of their client; and they ought scrupulously to refrain from bargaining about the subject matter of the litigation, so long as the relation of attorney and client continues." \textit{Jones, supra note} 176, at 271.

\textsuperscript{179} See Jones, supra note 176, at 266, 271.

\textsuperscript{180} \textit{Id.} at 256.

\textsuperscript{181} \textit{Id.}

\textsuperscript{182} \textit{Id.} Alabama's Code of Legal Ethics was cited as the "foundation" for the Canons of Professional Ethics. \textit{Id.}

\textsuperscript{183} Canon 28 of the American Bar Association's Canons of Professional Ethics stated:

\begin{quote}
It is unprofessional for a lawyer to volunteer advice to bring a lawsuit, except in rare cases where ties of blood, relationship or trust make it his duty to do so. Stirring up strife and litigation is not only unprofessional, but it is indictable at common law. It is disreputable to hunt up defects in titles or other causes of action and inform thereof in order to be employed to bring suit or collect judgment, or to breed litigation by seeking out those with claims for personal injuries or those having any other grounds of action in order to secure them as clients, or to employ agents or runners for like purposes, or to pay or reward, directly or indirectly, those who bring or influence the bringing of such cases to his office, or to remunerate policemen, court or prison officials, physicians, hospital attaches or others who may succeed, under the guise of giving disinterested friendly advice, in influencing the criminal, the sick and the injured, the ignorant or others, to seek his professional services. . . .
\end{quote}

\textbf{CANONS OF PROFESSIONAL ETHICS Canon 28 (1908).}
followed the Code of Legal Ethics rule regarding stirring up litigation. There was no rule in the Canons of Professional Ethics regarding lending money to clients until 1928 when Canon 42\textsuperscript{184} was adopted.\textsuperscript{185} The newly adopted Canons of Professional Ethics did contain a similar rule, Canon 10,\textsuperscript{186} which prohibited a lawyer from purchasing any interest in the litigation, although this prohibition had not been specifically restricted in the Code of Legal Ethics.\textsuperscript{187} These canons were designed to discourage lawyers from stirring up frivolous litigation in an attempt to only enrich the lawyer, as well as keeping the lawyer from having a personal interest in the litigation which might result if he had expended personal money that was at stake.\textsuperscript{188} These canons remained in effect for over sixty years until becoming outdated by changing societal perceptions.\textsuperscript{189} In particular, society no longer found it necessary for there to be an absolute prohibition against attorneys advancing litigation expenses to their clients, particularly when an attorney was representing a client in a contingency fee setting.\textsuperscript{190}

\textit{E. Model Code of Professional Responsibility}

The absolute ban on lawyers providing financial assistance for their clients was finally revoked with the adoption of the Model Code of Professional Responsibility, adopted by the American Bar Association in 1969 to replace the Canons of Professional Ethics.\textsuperscript{191} The Model Code of Professional Responsibility was organized into three parts: Canons, Ethical Considerations, and Disciplinary Rules.\textsuperscript{192} The Canons were statements in general terms of "the standard of professional conduct expected of lawyers in their relationships with the public, with the legal system, and with the legal profession." \textsuperscript{193} The Ethical Considerations were the "objectives toward which every member of the profession should strive."\textsuperscript{194} The Disciplinary Rules were required of every lawyer in the Bar; no lawyer could fall below this minimum level of conduct.

\textsuperscript{184} Canon 42 of the American Bar Association's Canons of Professional Ethics stated, "[a] lawyer may not properly agree with a client that the lawyer shall pay or bear the expenses of litigation; he may in good faith advance expenses as a matter of convenience, but subject to reimbursement." \textit{Canons of Professional Ethics} Canon 42 (1908).
\textsuperscript{185} See Jones, \textit{supra} note 176, at 266, 271.
\textsuperscript{186} Canon 10 of the American Bar Association's Canons of Professional Ethics stated that "[t]he lawyer should not purchase any interest in the subject matter of the litigation which he is conducting." \textit{Canons of Professional Ethics} Canon 10 (1908).
\textsuperscript{187} See Jones, \textit{supra} note 176, at 276.
\textsuperscript{188} See Mark Lynch, \textit{Ethical Rules in Flux: Advancing Costs of Litigation}, 7 Litig. 19, 19 (1980).
\textsuperscript{189} Compare \textit{Canons of Professional Ethics} (1908) with \textit{Model Code of Professional Responsibility} (1969).
\textsuperscript{190} See Lynch, \textit{supra} note 188, at 19.
\textsuperscript{191} \textit{Id}.
\textsuperscript{193} \textit{Id}.
\textsuperscript{194} \textit{Id}.
without being subject to disciplinary action. All three sections contained provisions regarding litigation expenses.

Canon 5 and the ethical considerations and disciplinary rules which accompanied Canon 5 replaced Canons 10, 28, and 42 of the Canons of Professional Ethics. Canon 5 required a lawyer to exercise independent professional judgment when acting on behalf of a client. Ethical Consideration 5-1 further suggested that the lawyer's personal interests should not "dilute his loyalty to his client." Ethical Consideration 5-8 stated:

A financial interest in the outcome of litigation also results if monetary advances are made by the lawyer to his client. Although this assistance generally is not encouraged, there are instances when it is not improper to make loans to a client. For example, the advancing or guaranteeing of payment of the costs and expenses of litigation by a lawyer may be the only way a client can enforce his cause of action, but the ultimate liability for such costs and expenses must be that of the client.

Disciplinary Rule 5-103(B) prohibited attorneys from "advanc[ing] or guarantee[ing] financial assistance to his client." Disciplinary Rule 5-103(B) differed from the traditional canons by allowing an exception for "the expenses of litigation, including court costs, the expenses of investigation, expenses of medical examination, and costs of obtaining and presenting evidence"; however, the client had to remain "ultimately liable for such expenses."

Disciplinary Rule 5-103(B) was met with widespread dissatisfaction from state bar associations and public interest groups that contended that this rule restricted lawyers from providing legal services to less-affluent individuals and

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195 Id.
196 See MODEL CODE OF PROFESSIONAL RESPONSIBILITY Canon 5 (1969); MODEL CODE OF PROFESSIONAL RESPONSIBILITY EC 5-1 (1969); MODEL CODE OF PROFESSIONAL RESPONSIBILITY EC 5-8 (1969); MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 5-103(B) (1969).
198 Id.
201 Disciplinary Rule 5-103 states:

(A) A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation he is conducting for a client, except that he may: (1) Acquire a lien granted by law to secure his fee or expenses. (2) Contract with a client for a reasonable contingent fee in a civil case.

(B) While representing a client in connection with contemplated or pending litigation, a lawyer shall not advance or guarantee financial assistance to his client, except that a lawyer may advance or guarantee the expenses of litigation, including court costs, expenses of investigation, expenses of medical examination, and costs of obtaining and presenting evidence, provided the client remains ultimately liable for such expenses.

MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 5-103(B) (1969).
202 MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 5-103(B) (1969).
203 Id.
public interest causes. Disciplinary Rule 5-103(B) provided exceptions regarding these concerns, thus allowing the attorney to bear litigation costs in cases where the client was indigent, cases where the attorney was to receive absolutely no fee, and cases where a public service organization was paying the costs. However, these exceptions did not provide adequate protection for public service litigation. Middle income persons represented on a contingency fee basis often could not reimburse the attorney for substantial amounts of litigation costs if the action failed. Further, in class action cases, the named plaintiff often recovered less than the litigation expenses that he would be required to repay. As one advocate for revising Disciplinary Rule 5-103(B) stated,

Since the code recognized that contingent fee arrangements may be the only way for many people to afford litigation, the code should also allow contingent cost arrangements. In reality, the practice flourishes—lawyers either do not require the client to assume liability for costs, or if the obligation is in the retainer agreement, they do not try to collect. But the code should be brought into line with reality, particularly when one of the most serious criticisms of the profession is its failure to provide affordable legal services.

In response, the American Bar Association Commission on Evaluation of Professional Standards (popularly known as the “Kutak Commission”) began in 1977 to revise the Model Code of Professional Responsibility and Disciplinary Rule 5-103(B).

F. Model Rules of Professional Conduct

The Kutak Commission quickly realized that a revision of the Model Code of Professional Responsibility would not be as effective as an entirely new code, thus the drafting of the Model Rules of Professional Conduct began. The Kutak Commission unofficially released a draft of the proposed Model Rules of Professional Conduct in August 1979; however the official draft released in January 1980 differed from the previous version. The unofficial draft retained the gist of Disciplinary Rule 5-103(B) but eliminated the requirement that the client remain ultimately liable for the expenses. This proposal was supported by the Board of Governors of the District of Columbia Bar Association who had petitioned the District of Columbia Court of Appeals to amend Disciplinary Rule

204 See Lynch, supra note 188, at 19.
205 See MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 5-103(B) (1969).
206 See Lynch, supra note 188, at 20.
207 Id.
208 Id.
209 Id.
210 Id. at 19.
212 See Lynch, supra note 188, at 19.
213 Id. at 21.
The District of Columbia Bar pointed out four reasons for eliminating the ultimate liability clause: (1) Disciplinary Rule 5-103(B) was "widely ignored"; (2) there were other disciplinary rules which adequately insured that a lawyer would not pursue malicious or harassing claims or claims in which the lawyer might have a financial interest at stake; (3) if contingent fee arrangements were permissible, then contingent cost agreements were not significantly different from contingent fee arrangements; and (4) public interest litigation was rapidly developing. The District of Columbia Bar wanted to go even further and allow the phrase "a lawyer may pay," making it absolutely clear that the expenses were on the lawyer's account and not the client's; however, not everyone agreed with the District of Columbia Bar.

The unofficial draft was replaced by the Kutak Commission's official draft which prohibited a lawyer from providing financial assistance for clients except that "(1) a lawyer may advance court costs and expenses of litigation, repayment of which is contingent on the outcome of the matter; (2) a lawyer or legal services organization representing a client without fee may pay court costs and expenses of litigation on behalf of a client." This wording only allowed the attorney to pay litigation expenses on his own account when he was representing without charging a fee.

The work of the Kutak Commission became the Model Rules of Professional Conduct in 1983. Still similar to the Canons of Legal Ethics and the 1969 Model Code of Professional Conduct, the new Model Rules of Professional Conduct were reorganized into categories based on functions, such as client-lawyer relationship, the lawyer as counselor and as advocate, etc.

Disciplinary Rule 5-103 became today's Rule 1.8(e) of the American Bar Association's Model Rules of Professional Conduct, which reads:

A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

(1) a lawyer may advance court costs and expenses of litigation, the payment of which may be contingent on the outcome of the matter; and

(2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.

Thus, under Rule 1.8(e) of the Model Rules of Professional Conduct, if the client is not indigent, the attorney must be reimbursed for any advanced costs from the recovery; however, if there is no recovery, the client is no longer personally

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214 Id.
216 See Lynch, supra note 188, at 21.
217 Id.
218 Id. at 59.
219 Id.
220 See A LEGISLATIVE HISTORY, supra note 211, at v.
222 MODEL RULES OF PROFESSIONAL RESPONSIBILITY Rule 1.8(e) (1983).
liable. In addition, Rule 1.8(j) echoes the early prohibitions against maintenance and champerty by prohibiting a lawyer from acquiring a proprietary interest in litigation the lawyer is conducting for a client, unless the lawyer has acquired a lien to secure the lawyer’s fee or expenses, or contracted with the client for a reasonable contingent fee.

In 1997, a new Commission on Evaluation of the Rules of Professional Conduct was created to evaluate and consider any concerns advanced regarding the current Model Rules of Professional Conduct. Popularly referred to as “Ethics 2000,” the Commission was scheduled to submit a report with recommendations to the American Bar Association House of Delegates in 2000. Although the current model rule allows only advancement of litigation expenses, with repayment contingent on the outcome, it is entirely possible that in the future a new model rule will reflect the change implemented by Alabama and suggested by recent court decisions. Until then, however, the Model Rules, and states which follow the Model Rules, do suggest that payment of litigation expenses can only be advancements, supporting the Service’s position that litigation expenses are only deductible through the bad debt provision when determined uncollectible. Thus, the obvious solution would be to change the rule. Accordingly, Alabama undertook to do so.

IV. DEVELOPMENT OF ETHICAL RESTRICTIONS IN ALABAMA

A. Historical Restrictions

Alabama has always been on the forefront when it comes to ethical restrictions for attorneys. As discussed above, Alabama was the first state in the union to establish ethical restrictions regarding attorneys’ behavior. The Code of Legal Ethics consisted of Alabama’s first ethical provisions governing lawyers’ conduct. Alabama considered it “disreputable in morals” to “stir up strife and litigation,” and therefore prohibited such conduct. Alabama also required that its attorneys refrain from lending money to their clients while the attorney-client relationship existed. These principles, among others, guided Alabama lawyers for eighty-seven years until the Alabama State Bar adopted its

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223 See Chofnas & Walker, supra note 28, at 85.
224 See MODEL RULES OF PROFESSIONAL RESPONSIBILITY Rule 1.8(j) (1983).
225 See A LEGISLATIVE HISTORY, supra note 211, at v.
226 Id.
227 See MODEL RULES OF PROFESSIONAL RESPONSIBILITY Rule 1.8(e) (1983).
229 See Jones, supra note 176, at 247.
230 Id.
231 Id.
232 Id. at 266.
233 Id. at 271.
own Code of Professional Responsibility in 1974, modeled largely after the American Bar Association's Code of Professional Responsibility of 1969.\textsuperscript{234}

Alabama's Code of Professional Responsibility Canon 5 and Ethical Consideration 5-1 mirrored the American Bar Association's version; however, a distinction was made in Alabama's Ethical Consideration 5-8 and Disciplinary Rule 5-103(B).\textsuperscript{235} Ethical Consideration 5-8 retained the essence of the American Bar Association's standard, though an extra requirement was added: Lawyers could not promise financial assistance prior to the lawyers' employment by the client.\textsuperscript{236} The same requirement appeared in Disciplinary Rule 5-103(B).\textsuperscript{237}

In an Opinion of the General Counsel, an Alabama attorney inquired whether costs of litigation could be advanced without holding the client liable.\textsuperscript{238} The General Counsel responded that such a contract would be unethical as it would be in violation of Ethical Consideration 5-8 and Disciplinary Rule 5-103(B).\textsuperscript{239} The General Counsel referred to both Alabama's version and the American Bar Association's version, pointing out that both versions require the client to remain ultimately liable, with the Alabama rule even stating "without regard to the outcome of the litigation."\textsuperscript{240}

Alabama's Code of Professional Responsibility remained in effect until 1990 when the Alabama Bar adopted the American Bar Association's Model Rules of

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\textsuperscript{235} Compare Model Code of Professional Responsibility Canon 5, EC 5-1, EC 5-8, DR 5-103(B) (1969), with Alabama Code of Professional Responsibility Canon 5, EC 5-1, EC 5-8, DR 5-103(B) (1974).
\textsuperscript{236} See Alabama Code of Professional Responsibility EC 5-8 (1974). Alabama's Ethical Consideration 5-8 stated:

A financial interest in the outcome of litigation also results if monetary advances are made by the lawyer to his client. Although this assistance generally is not encouraged, there are instances when it is not improper to make loans to a client, for example, the advancing or guaranteeing of payment of the costs and expenses of litigation by a lawyer when such is the only practicable way a client can enforce and protect his legal rights to a just conclusion. Under no circumstances, however, may a lawyer promise or permit another to promise such financial assistance prior to his employment by such client. Always the ultimate liability for such financial assistance must be that of the client, without regard to the outcome of the litigation.

Id.
\textsuperscript{237} See Alabama Code of Professional Responsibility DR 5-103(B) (1974). Alabama's Disciplinary Rule 5-103(B) stated:

While representing a client in connection with contemplated or pending litigation, a lawyer may advance or guarantee emergency financial assistance to his client, provided that the client remains ultimately liable for such assistance without regard to the outcome of the litigation, and further provided, that no promise of such financial assistance was made to the client by the lawyer, or by another in his behalf, prior to the employment of that lawyer by that client.

Id.
\textsuperscript{238} See William H. Morrow, Jr., Opinions of the General Counsel, 44 Ala. Law. 168 (1983).
\textsuperscript{239} Id.
\textsuperscript{240} Id.
Professional Conduct of 1983. Disciplinary Rule 5-103(B) was replaced with Rule 1.8(e):

A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

(1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter;

(2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client; and

(3) a lawyer may advance or guarantee emergency financial assistance to the client, the repayment of which may not be contingent on the outcome of the matter, provided that no promise or assurance of financial assistance was made to the client by the lawyer, or on the lawyer's behalf, prior to the employment of the lawyer.

Although Alabama's Rule 1.8(e) was different from Alabama's Disciplinary Rule 5-103(B) in that it allowed advancement of litigation expenses if repayment was contingent on the case's outcome or if the client was indigent, Rule 1.8(e) carried over the Alabama Disciplinary Rule 5-103(B) unique idea of prohibiting promises of financial assistance before the employment relationship commenced. For several years, Alabama was similar to the majority of other states that only allowed attorneys to advance litigation expenses with repayment being contingent on the success of the case. Accordingly, Alabama lawyers were required to defer deductibility of litigation expenses until determined uncollectible or collected.

B. Alabama's Change

In 1994, the Internal Revenue Service made a statement in a private letter ruling that opened the door to allowing litigation expenses as ordinary and necessary business expenses. The requesting taxpayer was a cash-basis lawyer attempting to deduct litigation expenses as ordinary and necessary business expenses. The taxpayer also had, in some instances, refrained from billing clients for out-of-pocket expenses, for various business reasons. The Service cited the precedent cases' general rule that "payment by one taxpayer of the obligation of another taxpayer is not considered an 'ordinary and necessary' expense for the paying taxpayer."
expense for purposes of section 162(a)." 249 The Service noted an exception, however, that the courts often overlooked: A taxpayer can make payments for the obligation of another taxpayer when the taxpayer is "expending such funds in order to protect or promote his own established business." 250 The Service held that if the taxpayer decided for valid business reasons to not seek reimbursement from the client, the taxpayer was entitled to a business expense deduction. 251

Alabama lawyers took this language and applied it to economic reality. First, courts were denying deductibility of litigation expenses if there was a high probability of repayment. 252 Alabama recognized that very few lawyers regularly advance money to a client unless there is a good chance of repayment; otherwise, a lawyer would not be in business very long. 253 Other businesses, however, could have an expense where ultimate recovery of expenses was equally as contingent as the repayment of litigation expenses, yet they were allowed to deduct their expenses as ordinary and necessary business expenses. 254 Alabama lawyers recognized that the tax treatment of litigation expenses as advances had begun as a legal fiction and was now being perpetuated by ethical considerations because the verb "advance" was used. 255 Relying on the language from the Private Letter Ruling where the Internal Revenue Service allowed a taxpayer to take a business expense deduction if he decided for valid business reasons not to seek reimbursement of litigation expenses, 256 the Alabama State Bar proposed an amendment to Alabama's ethical rule. 257

In 1995, the Alabama Supreme Court adopted a revised Professional Conduct Rule 1.8(e), which now reads:

A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:

249 Id. (relying on Boccardo v. United States, 12 Cl. Ct. 184 (1987); Herrick v. Commissioner, 63 T.C. 562 (1975); Canelo v. Commissioner, 53 T.C. 217 (1969), aff'd, 447 F.2d 484 (9th Cir. 1971); Silverton v. Commissioner, 36 T.C.M. (CCH) 817 (1977), aff'd, 647 F.2d 172 (9th Cir. 1981)).


251 See id.


253 See Amkraut, supra note 39, at 750.

254 See, e.g., Alleghany Corp. v. Commissioner, 28 T.C. 298, 305 (1957) (allowing an investment corporation taxpayer to deduct amounts as business expenses when the taxpayer had expended the amounts with a possibility of reimbursement); Electric Tachometer Corp. v. Commissioner, 37 T.C. 158, 162 (1961) (allowing a taxpayer to deduct moving expenses as ordinary and necessary business expenses when the taxpayer was forced to expend said expenses due to condemnation of its property and was later reimbursed by the State because although there was a contingent right of reimbursement, there was no fixed right of reimbursement).


257 Movants, Mr. David M. Wooldridge, Sirote & Permutt, P.C. and Joseph W. Blackburn, Palmer Professor of Law, Samford University's Cumberland School of Law and Scholar-In-Resident to Sirote & Permutt, P.C. wished to maintain appropriate ethical restrictions while permitting current deductibility of litigation expenses by Alabama lawyers.
(1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter;

(4) in an action in which an attorney’s fee is expressed and payable, in whole or in part, as a percentage of the recovery in the action, a lawyer may pay, for his own account, court costs and expenses of litigation. The fee paid to the attorney from the proceeds of the action may include an amount equal to such costs and expenses incurred. 258

Subsection 1 is essentially the same as the American Bar Association’s Model Professional Conduct Rule 1.8(e); however, the difference comes in the addition of subsection 4. 259 By adding subsection 4, the Alabama State Bar made it clear that attorneys operating under a contingency fee arrangement could pay litigation expenses on the attorneys’ own accounts even if the attorneys were eventually repaid the litigation expenses. 260 If the employment arrangement was worded consistently with this rule, emphasizing that the lawyer, rather than the client, was responsible for the litigation expenses, the lawyer could deduct the litigation expenses as ordinary and necessary business expenses. 261

For over a year, Alabama was on the forefront in achieving immediate deductibility of litigation expenses. It was unclear how the Internal Revenue Service and courts would evaluate Alabama’s change. To date, neither the Service nor the courts have specifically addressed Alabama’s unique position. In a 1995 landmark case, a federal circuit court finally supplied the language Alabama needed to rely on. 262

Next, this Article will discuss this landmark case and the change in judicial interpretation of litigation expenses, as well as current criticism of this new position.

V. COURTS CHANGE POSITION FOR GROSS CONTINGENCY FEE ARRANGEMENTS

A. Boccardo III

In 1995, the Ninth Circuit finally agreed with what attorneys had been arguing for decades. 264 The Ninth Circuit reversed the Boccardo Tax Court decision, and Mr. Boccardo was allowed to deduct the costs as ordinary and necessary business expenses. 265 On appeal, only Mr. Boccardo’s gross fee

258 ALABAMA RULES OF PROFESSIONAL CONDUCT Rule 1.8(e) (2000).
259 Compare ALABAMA RULES OF PROFESSIONAL CONDUCT Rule 1.8(e) (2000), with MODEL RULES OF PROFESSIONAL RESPONSIBILITY Rule 1.8(e) (1983).
260 See ALABAMA RULES OF PROFESSIONAL CONDUCT Rule 1.8(e) (2000).
261 Id.
262 See Boccardo v. Commissioner, 56 F.3d 1016, 1020 (9th Cir. 1995).
263 56 F.3d 1016 (9th Cir. 1995).
264 Id.
265 Id.
arrangement was considered. The court refused to apply the "advances" label as a matter of law when the client had absolutely no obligation to repay the expenditures. The court pointed out that the gross fee arrangement effectively made law firms no different from any other business whose revenue must exceed expenses incurred in order to make a profit. Because Mr. Boccardo was using a gross fee arrangement that made no reference to reimbursement of costs, he was allowed to deduct immediately litigation costs as business expenses.

Mr. Boccardo responded to the Tax Court's reference to California Rules of Professional Conduct rule 5-104 by arguing that his contingency fee arrangement did not violate a generally enforced state law that subjected the taxpayer to any penalty. Under section 162(c)(2), the Internal Revenue Service has the authority to deny deductibility of a business expense that violates a generally enforced state law. As for California rule 5-104 (since amended to 4-210(a) but effectively still the same), the court questioned whether it was even a state law. There was a specific California state statute, the California Business and Professional Code, which regulated contingency fee arrangements and did not prohibit lawyers from paying expenses. Even if it was a state law, the court found no evidence that it was generally enforced but rather found that in California "the line between 'costs' and attorney overhead included as part of the lawyer's fee [was] an undefined and changing one." Because the gross fee arrangements were not illegal, the court held that the payment of litigation costs were ordinary and necessary business expenses.

Attorneys' arguments fell on receptive ears—the repayment of litigation expenses are oftentimes contingent, and if contingent, they should not be required to be deducted through the bad debt provision which requires an

266 A "gross fee" arrangement is a contract whereby reimbursement of the client's costs comes solely from any recovery. See Boccardo v. Commissioner, 65 T.C.M. (CCH) 2739, 2741 (1993). For example, in Boccardo, if the firm pays $3,000 in costs on a case and recovers $5,000 after trial, under the gross fee agreement it recovers $2,000 of the costs, while under the net fee agreement it is reimbursed the entire $3,000. Id.
267 See Boccardo, 56 F.3d at 1020.
268 Id. at 1018.
269 Id.
270 Id. at 1020.
271 Id. at 1018 (referring to 26 U.S.C. § 162(c)(2) (1995)).
272 26 U.S.C. § 162(c)(2) (1994). Section 162(c)(2) states:
No deduction shall be allowed [as an ordinary and necessary business expense] for any payment . . . made directly or indirectly, to any person, if the payment constitutes an . . . illegal payment under any law of the United States, or under any law of a State (but only if such State law is generally enforced), which subjects the payor to a criminal penalty or the loss of license or privilege to engage in a trade or business.
273 See Boccardo, 56 F.3d at 1019.
274 Id.
275 Id. at 1020.
276 Id.
unconditional obligation of repayment. Further, ethical restrictions do not necessitate requiring the litigation expenses to be considered advancements. Whether anyone would agree with the Ninth Circuit was still to be determined.

B. Boccardo Applied

In 1999, another law firm was in court trying to deduct litigation costs as ordinary and necessary business expenses by relying on the Ninth Circuit’s holding in the 1995 Boccardo case. Pelton & Gunther, a California professional corporation specializing in personal injury automobile accident lawsuits, performed 90% of its services for the California State Automobile Association. Pelton & Gunther represented CSAA policyholders in their automobile accident claims with CSAA paying Pelton & Gunther a $400 retainer up front for each engagement. Pelton & Gunther would then pay all of the litigation costs in pursuit of the claim, often exceeding the retainer. Once the claims were closed, Pelton & Gunther would bill CSAA for its legal services, at an hourly rate, plus the litigation costs.

The United States Tax Court quickly dismissed the taxpayer’s attempt to distinguish Boccardo, pointing out that Pelton & Gunther was not using gross fee arrangements or even contingency fee arrangements, a crux of the Boccardo decision, but instead using hourly fee arrangements. The court held that Pelton & Gunther’s litigation costs were not deductible as ordinary and necessary business expenses because CSAA’s repayment of the advances was “in no way contingent upon the outcome of the underlying litigation.” The court relied on the fact that Pelton & Gunther fully expected to be repaid and actually was repaid for all litigation costs advanced to CSAA’s policyholders. The court pointed out that the litigation costs were not “a burden on [Pelton & Gunther] or a reduction of [Pelton & Gunther’s] fee income received from CSAA for legal services rendered.” Thus, Boccardo’s holding was limited to cases involving contingent gross fee arrangements only.

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277 Id.
278 Id.
280 Id. at *4.
281 Id. at *4-5.
282 Id. at *5.
283 Id.
284 Id. at *9-10.
286 See id.
287 Id. at *10.
288 Id.
C. Problems with Boccardo

Although the Ninth Circuit agreed with attorneys and allowed the deductibility of litigation expenses in gross fee arrangements,\(^{289}\) it is not yet clear if this theory will be adopted universally. Recent publications have failed even to recognize the change in tax treatment allowed in the 1995 *Boccardo* decision, citing the 1987 *Boccardo* decision as the current controlling authority.\(^{290}\) The United States Tax Court had the opportunity to analyze the Ninth Circuit's decision and offered no criticism, yet refused to apply it beyond the gross fee arrangement.\(^{291}\)

Further, the gross fee arrangement is a seldom used contingency arrangement.\(^{292}\) Generally, attorneys prefer and use the net fee arrangement because the litigation expenses are guaranteed to be reimbursed by any recovery.\(^{293}\) Reimbursement is always preferable to an income tax deduction of the same amount.\(^{294}\) As one commentator noted,

> The only difference between gross and net fee arrangements, as they relate to probability of recovering expenses, occurs in cases where expenses represent either a high percentage of recovery or exceed recovery . . . . Thus, it is possible that a gross fee attorney would not recover full expenses in a case where a net fee attorney would.\(^{295}\)

Thus, unless an attorney is willing to use the gross fee arrangement and risk not recovering full expenses, the *Boccardo* decision will be unpersuasive authority for deducting litigation expenses as ordinary and necessary expenses.

Further, in the *Boccardo* case, the parties stipulated that both the gross and net fee arrangements had the same percentage of expense reimbursement, yet the court went on to consider the difference between the two arrangements, paying no heed to the stipulation.\(^{296}\) Thus, it would appear to be easy for *Boccardo* to be reversed by a later case on this procedural ground. Accordingly, the more logical approach would be to try to deduct litigation expenses under the ethical restriction reasoning used by *Boccardo*.

Finally, this Article will provide recommendations for attorneys desiring to immediately deduct litigation expenses as ordinary and necessary business expenses.

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\(^{289}\) See *Boccardo v. Commissioner*, 56 F.3d 1016, 1020 (9th Cir. 1995).

\(^{290}\) See, e.g., 47A C.J.S. *Internal Revenue* § 133 (1999) (stating that litigation expenses were considered loans); 47A C.J.S. *Internal Revenue* § 155 (1999) (stating that litigation expenses were not deductible until determined unrecoverable from client); JACOB MERTENS, JR., THE LAW OF FEDERAL INCOME TAXATION 24A.31 (West 1997) (stating that litigation expenses were not currently deductible).


\(^{292}\) See Amkraut, *supra* note 39, at 746.

\(^{293}\) id. at 760.

\(^{294}\) id.

\(^{295}\) id.

\(^{296}\) id.
VI. RECOMMENDATION

The best scenario for deducting litigation expenses would be an attorney using a gross fee arrangement in a state that had an ethical restriction similar to Alabama’s allowing attorneys to pay litigation expenses on their own account. The gross fee arrangement must make no reference to the client being obligated for the expenses. One commentator points out, however, that the Tax Court looked unfavorably upon the Boccardo firm when the firm increased its percentage from one-third to 40% in order to make up for the difference when changing to a gross fee arrangement; therefore, attorneys must carefully review the economic effect when revising their fee arrangements. 297

Further, it appears that Alabama is the only southeastern state with an ethical provision allowing attorneys to bear the responsibility of paying for litigation expenses. 298 Of the southeastern states’ bar associations responding to the author’s inquiry, 299 six states have ethical rules regarding payment of litigation expenses modeled after the American Bar Association’s Rules of Professional Conduct Rule 1.8(e). 300 Two states are still using an ethical rule modeled after the Model Code of Professional Responsibility. 301 One state has a motion before its supreme court to replace the ethical rules with new ethical rules modeled after the Model Rules of Professional Conduct, 302 and the other state plans to make the same motion in the very near future. 303 Several states indicated that their bar associations have not considered changing the rule to allow deductibility of litigation expenses. 304 Accordingly, attorneys interested in changing their state’s...
ethical rule should petition their state bar association to amend their ethical rule
to allow the attorneys to pay litigation expenses on their own account. Commentators support Alabama’s position and also recommend that state bars amend their codes of professional responsibility to allow attorneys to release their clients from ultimate responsibility for these costs in order to have the greatest possibility of deducting litigation expenses as business expenses. 305

For those who do not want to use a gross fee arrangement, the fee arrangement still needs to make clear that the responsibility for paying litigation expenses belongs to the attorney. 306 When accounting for such expenses, the lawyer needs to make sure that the firm’s accounting ledger and financial statement describe these expenses as the firm’s. 307 These expenses should not be labeled as “loans” or “advances” to clients. 308 The firm or lawyer is free to keep up with expenses on a case-by-case basis, but should make sure that there are no internal references indicating that the litigation expenses were merely advanced to the client. 309 For law firms that do not use contingency fee arrangements, the firm may still be able to take advantage of the Boccardo holding by no longer billing for fees and expenses and just billing for fees alone. 310 This was precisely the scenario in Pelton & Gunther, in which the court refused to apply Boccardo. 311 Therefore, in order to insure deductibility of such a payment arrangement, the state’s ethical rule probably would also have to be amended. 312

VII. CONCLUSION

Although litigation expenses have historically been denied deductibility as ordinary and necessary business expenses, 313 the tide may be changing. The courts’ most sensible rationale for denying deductibility — that there was a high probability of recovery 314 — quickly lost its authority when a gross fee arrangement was used. 315 Further, when the state’s ethical restriction was not

the Ethics Committee, North Carolina Bar Association (Feb. 10, 2000) (on file with author); e-mail from Robert S. Wells, South Carolina Bar Association (Jan. 25, 2000) (on file with author).

305 See Greenberg & Janowski, supra note 35, at 72.
306 See Cooper, supra note 4, at 285.
308 Id. Goode warns about using labels such as “rebillable expenses,” “client costs,” or advances in the fee agreement, letters to clients, general ledger accounts, and charts of accounts. Id.
309 Id. at 11.
310 See Cooper, supra note 4, at 286.
312 Of course, the attorney or firm should petition the Internal Revenue Service for a change in its method of accounting if so required. See Cooper, supra note 4, at 285.
generally enforced, the courts overlooked the argument that states' ethical restrictions require litigation expenses to be considered advances. An attorney would have stronger grounds to argue for a deduction of litigation expenses if the state's ethical restriction did not even treat the litigation expenses as advances but rather on the attorney's own account. Thus, until the Internal Revenue Service formally changes its position and allows deductibility of litigation expenses as ordinary and necessary business expenses, attorneys in states that so permit should use an arrangement that makes clear the obligation is on the attorney to pay litigation expenses.

316 See Boccardo v. Commissioner, 56 F.3d 1016, 1020 (9th Cir. 1995).
317 See Goode, supra note 307, at 11.
LET'S PLAY JEOPARDY: WHERE THE QUESTION COMES AFTER THE ANSWER FOR STOPPING PROSECUTORIAL MISCONDUCT IN DEATH-PENALTY CASES

by Edward C. Brewer, III

"[W]hat's the use you learning to do right when it's troublesome to do right and ain't no trouble to do wrong, and the wages is just the same?" 2
"[Ethics] is [ethics] to the end of reckoning." 3

INTRODUCTORY STATEMENT

During oral argument in the Hamilton County death-penalty case of State v. Jones, 4 Chief Justice Thomas J. Moyer of the Ohio Supreme Court is quoted as having asked, "How do we stop prosecutors from engaging in conduct that we tell them time and time again is improper?" 5 This is not a new question. In State v. Lorraine, 6 Justice Wright observed in his concurrence that "[w]hy we see a continuing pattern of prosecutorial misconduct in capital cases is beyond me." 7 Earlier, in State v. DePew, 8 a majority of the Supreme Court commented on the need for prosecutors to obey the law of legal ethics in death-penalty cases. 9

Jones is the latest in a series of cases suggesting that prosecutorial misconduct in Hamilton County death-penalty cases is an issue that just will not go away. 10 The issue recently came to public attention in a news article in the

1 Associate Professor of Law, Salmon P. Chase College of Law, Northern Kentucky University; Vanderbilt University (J.D. 1979), The University of the South (Sewanee) (B.A. 1975). Professor Brewer teaches Professional Responsibility, Civil Procedure, Federal Jurisdiction, Remedies, and Trial Advocacy. He practiced in Atlanta, Georgia, from 1982 to 1996, in business litigation and pro bono representation, and prior to that was a law clerk to Honorable Virgil Pittman of the Southern District of Alabama, and Honorable Albert J. Henderson of the Fifth and Eleventh Circuits. Particular thanks are due to the editors and staff of the Northern Kentucky Law Review for their attention to the manuscript, and to Karen Pape for everything she does. The views expressed in this article are those of the author.

2 Mark Twain, The Adventures of Huckleberry Finn, Ch. 16 (1885).
3 See Hon. Mark P. Painter, Judge, Ohio First District Court of Appeals, in Cincinnati Shakespeare Festival, 2000-01 Season Brochure, at 3 ("Truth is truth to the end of reckoning").
6 613 N.E.2d 212 (Ohio 1993).
7 Id. at 224 (Wright, J., concurring).
9 See id. at 557; infra text accompanying notes 77-78 (quoting Supreme Court's comments). Justice Wright, "finding the majority's 'solution' to the problem of prejudicial prosecutorial misconduct particularly troublesome," would have reversed the penalty phase. Id. at 565-66.
10 See infra notes 27-47 and accompanying text.
Cincinnati Enquirer, which focused on the 14 death-penalty cases in Hamilton County in which such misconduct apparently has occurred. This article will respectfully offer a solution to the problem posed in DePew, Lorraine, and Jones, from the field of legal ethics.

THE ETHICS OF CRIMINAL CASES AND ENFORCEMENT, GENERALLY

All lawyers are required to observe the rules of legal ethics in effect in their jurisdiction of admission, in both civil and criminal cases. One such rule is Ohio Disciplinary Rule 7-106, which governs a lawyer’s trial conduct. DR 7-106(C) provides that:

[i]n appearing in his [or her] professional capacity before a tribunal, a lawyer shall not: (1) State or allude to any matter that he [or she] has no reasonable basis to believe is relevant to the case or that will not be supported by admissible evidence . . . . (3) Assert his [or her] personal knowledge of the facts in issue, except when testifying as a witness. (4) Assert his [or her] personal opinion as to the justness of a cause, as to the credibility of a witness . . . or as to the guilt or innocence of an accused; but he [or she] may argue, on his analysis of the evidence, for any position or conclusion with respect to the matters stated herein . . . . (6) Engage in undignified or discourteous conduct which is degrading to a tribunal.

Another such rule is DR 1-102(A)(5), which provides that “[a] lawyer shall not . . . (5) Engage in conduct that is prejudicial to the administration of justice.” As lawyers, we are charged with knowledge of these rules just as, in most cases, every citizen is charged with knowledge of the law’s requirements.

We cannot readily determine whether, or if so how many, prosecutors in Ohio or in Hamilton County have been disciplined for conduct in death penalty cases within DR 7-106(C) or DR 1-102, because the Ohio Board of Commissioners on Grievances and Discipline does not keep statistics by area of practice, and until recently the Ohio appellate courts did not name the prosecutors who had engaged in misconduct. We do know that an Ohio prosecutor was disciplined for lying to the trial court in Office of Disciplinary Counsel v. Greene, as were the defense lawyers in Office of Disciplinary Counsel v. Lynch, Office of Disciplinary Counsel v. Frenden, and Cincinnati

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11 See Hunt, supra note 5. Mr. Hunt observes that Hamilton County has the largest number of prisoners on death row in Ohio with 48. Id.
13 Id. DR 1-102 (A)(5).
14 See infra text accompanying note 54.
15 Telephone interview with Hon. Jonathan W. Marshall, Secretary to the Board, Sept. 11, 2000; see infra note 88 and accompanying text. Even assuming that the courts’ decisions had named the prosecutors, the ready availability of statistics would require both personnel rosters and a name-by-name records search.
16 655 N.E.2d 1299 (Ohio 1995).
17 643 N.E.2d 542 (Ohio 1994).
18 660 N.E.2d 1152 (Ohio 1996).
Prosecutors also have been disciplined for failures to turn over exculpatory evidence as required by *Brady v. Maryland*, in *Office of Disciplinary Counsel v. Jones* and *Cuyahoga County Bar Association v. Gertenslager*. Prosecutors’ misconduct was referred to disciplinary counsel by the Fifth District Court of Appeals in *State v. Miller-Cox* and by the Eighth District in *State v. Shelton*. A trial judge was publicly censured for discriminatory treatment of a litigant during a hearing in *Office of Disciplinary Counsel v. Mestemaker*.

What emerges from those cases is that both lawyers and judges, including prosecutors, have been disciplined for misconduct at trials and in hearings. However, the author was unable to find any published decisions of disciplinary action for prosecutorial misconduct in death-penalty cases as lamented by Chief Justice Moyer and Justice Wright.

**The Ethical Problems in the Death-Penalty Cases**

Some ethical issue involving the prosecutor has arisen in 14 of the 48 cases where the death penalty was successfully sought (although prosecutors have argued that this statistic is deceptive since it does not include those cases in which the jury rejected the death penalty or the case was plea-bargained). Whether those 14 cases constitute a representative set of examples or not, the conduct reported in them is independently significant for assessment under the rules of legal ethics. Those cases can be placed into one of three categories.

First, the Court stated in *State v. Combs* (1991) that a prosecutor may not make reference to the victim’s state of mind at the time of the crime because the

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19 687 N.E.2d 678 (Ohio 1997). Why the defense lawyers in these cases received six months and an indefinite suspension, respectively, for conduct that, at least in general terms, seems no more egregious than that in *Greene*, where the prosecutor netted a one-year suspension with ten months stayed, is beyond the scope of this article. See *Greene*, 655 N.E.2d at 1299.
21 613 N.E.2d 178 (Ohio 1993).
22 543 N.E.2d 491 (Ohio 1989). The prosecutor in this case was alleged to have negligently failed to hand over the *Brady* material. See *id*.
25 676 N.E.2d 870 (Ohio 1997).
26 See * supra* text accompanying notes 4-7.
27 See Hunt, * supra* note 5, at A16. It is unclear whether that argument purports to suggest that prosecutorial misconduct is significant only where it can be shown to have been material to securing a conviction and a sentence of death, that ethical misconduct in criminal cases does not matter unless its incidence is statistically significant over large samples, or that if one were to examine the records in the other thirty-four cases one would find even more ethical misconduct that happened to be unsuccessful in some regard.
28 See Hunt, * supra* note 5, passim.
argument calls for speculation. Yet appellate courts have criticized Hamilton County prosecutors for such speculation about the victim’s state of mind again and again, in *State v. Gumm* (1995), *State v. Wogenstahl* (1996), and *State v. Moore* (1998). The prosecutors in each of those cases appear to have violated DR 7-106(C)(1), plain and simple.

Second, in *State v. Hill* (1996), the prosecutor made reference to a personal belief about whether the defendant had lied on the stand. That prosecutor appears to have violated DR 7-106(C)(3) and (4).

Third, in four more recent cases, the prosecutors made derogatory comments in front of juries criticizing defendants for their exercise of fundamental constitutional rights. In *State v. Clemons* (1998), the prosecutor stated that the defendant’s lawyers were “just doing their job,” in derogation of the right to counsel provided for by the Sixth Amendment to the U.S. Constitution and Article I, Section 10 of the Ohio Constitution. In *State v. Sheppard* (1998), the prosecutor speculated about why the defendant did not offer a plea of insanity, in derogation of the Sixth Amendment right to a fair trial. In *State v. Fears* (1999), the prosecutor commented on the defendant’s decision not to testify, in derogation of the Fifth Amendment right not to be a witness against oneself. In *State v. Jones* (2000), the prosecutor repeatedly claimed that a person who did not testify at trial had lied (even after two objections had been

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30 See id. at 1077.
31 652 N.E.2d 253 (Ohio 1995).
32 662 N.E.2d 311 (Ohio 1996).
33 689 N.E.2d 1 (Ohio 1998).
34 See supra text accompanying note 12.
35 661 N.E.2d 1068 (Ohio 1996).
36 See id. Whether the prosecutor's derogatory remarks to the effect that the defense in *Hill* was “an effort really to defend the client but also to confuse the jury” were appropriate, excusable, or simply excused away by the majority need not be resolved given the even more egregious remarks in *State v. Clemons*, discussed infra in text accompanying note 38, and *State v. Jones*, discussed infra in text accompanying notes 44-47.
37 See supra text accompanying note 12. It does not stretch the point to suggest that a prosecutor’s references to evidence outside the record implicates the federal and state confrontation clauses. See U.S. CONST. amend. VI; OHIO CONST. art. I, § 10; see also *State v. Evans*, No. CR-191738, 1985 WL 8428, at *6 (Ohio Ct. App. 8th Dist. Nov.14, 1985).
38 696 N.E.2d 1009 (Ohio 1998).
39 Id. at 1022. See U.S. CONST. amend VI; OHIO CONST. art. I, § 10.
40 703 N.E.2d 286 (Ohio 1998).
41 See id. at 294. See also U.S. CONST. amend. VI; OHIO CONST. art. I, § 10.
42 715 N.E.2d 136 (Ohio 1999) Chief Justice Moyer delivered a compelling partial dissent in *Fears*, critical of prosecutors for continuing to ignore the warnings of *DePew* and critical of the Supreme Court for “continu[ing] to protest with no consequences.” *Fears*, 715 N.E.2d at 156-57.
43 See id. at 145. See also U.S. CONST. amend. V; DOYLE v. OHIO, 426 U.S. 610 (1976), GRIFFIN v. CALIFORNIA, 380 U.S. 609, 614 (1965). Perhaps this problem stems from taking the prosecutor’s right-to-comment provisions of the Ohio Constitution, article I, § 10 a little too seriously. Those provisions are, of course, preempted by federal law. See U.S. CONST. art VI, §1.
44 739 N.E.2d at 318-19.
sustained), characterized a defense expert as willing to say whatever the defense attorneys wanted him to say, and referred to the defense of the case as “a search for doubt, not a search for the truth,” in derogation of the Sixth Amendment and Article I, Section 10 rights to confrontation of witnesses and to defend oneself in a criminal case and of the constitutional requirement of proof beyond a reasonable doubt. The prosecutors in those cases appear to have violated DR 7-106(C)(1), DR 1-102(A)(5), and perhaps DR 7-106(C)(6) as well. Not incidentally, their comments treaded heavily upon the constitutional rights involved.

WHO CARES AND WHY?

Under one view, it may be argued that these problems are of diminished significance in a death-penalty case. A death-penalty case addresses some of the most horrific conduct that one person can commit against another, and therefore, a few ethical mistakes should not prevent a defendant guilty of such conduct from being convicted and punished. But, as the court noted in State v. Draughn, “[t]he incongruity of this rationale is that the better the state’s case, the more leeway is given to the prosecutor to overstep.” Thus under a contrary view, the requirement that the prosecutor comply with the United States and Ohio Constitutions assumes particular urgency and moral force where the penalty demanded is the defendant’s death. This latter proposition, as self-evident as it seems, is not without its problems under Ohio law: in State v. DePew, the Supreme Court went well beyond any necessity of the “harmless-error” rule and expressly balanced the public’s right to an effective criminal justice system against the defendant’s right to a fair trial.

This article rests on the premise that legal ethics are an important set of social values that have independent significance and that must be given force, more than anywhere else, in a trial where the death penalty is sought. The place of legal ethics in the constitutional and procedural validity of criminal convictions is a subject of considerable academic and judicial debate. But to separate the ethical issues from constitutional and procedural analysis is by no

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45 The Supreme Court criticized such comments in Fears, 715 N.E.2d 136 (albeit “with no consequences”), and such comments were one of the reasons for the reversal in State v. Miller, No. 18011, 2000 WL 1369918 (Ohio Ct. App. 2d Dist., Sept. 22, 2000).
46 See U.S. CONST. amend. VI. See also In re Winship, 397 U.S. 358 (1970).
47 See supra text accompanying notes 12-13.
49 Id. at 794.
50 See infra text accompanying note 68.
means to say that legal ethics has no significance in a death-penalty case. If anything, legal ethics ought to have more significance in death-penalty cases than in ordinary cases, and the demand for compliance with the rules ought to be the more exacting in such cases.

It also bears mention that, however infrequent and however quantitatively insignificant these ethical problems may be, they are not isolated instances among the Hamilton County death-penalty prosecutions. All attorneys, prosecutors included, are or should be well familiar with a criminal defendant's constitutional rights, and the principles of legal ethics that govern conduct in a courtroom. More importantly, all attorneys, prosecutors included, should respect and uphold, in word and deed, those rights and principles. Yet in nearly one out of three cases in which the death penalty was successfully sought in the last decade, the Ohio Supreme Court has had to address questions of misconduct by prosecutors in Hamilton County, often implicating important constitutional rights. Prosecutors may find it hard to know where some of the lines are drawn and may be subject to changes in rules of conduct, as present and former Hamilton County Prosecutors Mike Allen and Joe Deters have argued. But that argument has no persuasive force in the present context. The provisions cited above are plain and obvious in their meanings, have not been subject to changing or problematic interpretations by the Ohio appellate courts, and are clearly applicable to the cited cases. Moreover, it is reasonable to presume that death-penalty cases are prosecuted by seasoned veterans, not new lawyers who may make mistakes out of unfamiliarity or inexperience.

We can all agree that the prosecutors who made the offending arguments in Gumm, Wogenstahl, and Moore about the victim's state of mind knew or should have known about the decision in Combs. However heated a death-penalty prosecution may be, however complex the law affecting it, and however horrific the facts supporting it, are we asked to suppose that a prosecutor's decision to refer to the victim's state of mind at the time of death was anything other than a considered and calculated prosecutorial strategem? Would not any other such explanation strain credulity? How can such a strategem possibly be explained, much less legitimated, under those Supreme Court decisions? Like questions may be asked of the prosecutors' comments in Clemens, Sheppard, Fears, and Jones, criticizing defendants for exercising their constitutional rights. Any prosecutor knows or should know about the simple and basic constitutional protections that a criminal defendant enjoys when the

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53 See Hunt, supra note 5, at A16; supra notes 27-47 and accompanying text.
55 See Hunt, supra note 5, at A16.
56 Id. But see supra notes 27-47 and accompanying text; infra note 90.
57 See supra text accompanying notes 29-34.
58 Id.
59 Id.
60 See supra notes 38-47 and accompanying text.
State seeks to put him to death. Any prosecutor equally well knows or should know the uncontrovertible proposition that a prosecutor may not seek advantage before a jury from a defendant's exercise of those rights. Are we asked to believe that a prosecutor who makes reference to the defendant's decision to remain silent, to his decision not to plead insanity, and to his attorneys' defense of the case, has acted in any manner other than deliberately? What are we to think of that prosecutor's level of respect, or lack of respect, for those constitutional values and protections? There simply is no justification, and there can be no excuse, for the at-best verbal disregard of the Constitution that is reflected in the prosecutors' comments in Clemons, Sheppard, Fears, and Jones.

The prosecutor's reference to a personal belief in the defendant's guilt in Hill, although perhaps less constitutionally obnoxious than the misconduct in the other cases, fares no better from an ethical perspective. There is a simple rule concerning a lawyer's expressions of personal belief at trial: just don't do it. The prosecutor in State v. Young dealt with the problem by catching himself in mid-reference to a personal belief, thereby earning a reference to EC 7-24 rather than DR 7-106(C)(4) in the appellate court's expression of disapproval. There is no reason for a prosecutor's trial conduct in a death penalty case to be more ethically defective than that.

WHAT TO DO, WHAT TO DO? NO ANSWERS IN THE CRIMINAL LAW

What should the Ohio Supreme Court do about these problems? It is easier to see what the Court consistently does not do. The Court does not reverse the defendants' convictions. First, an appellate court will not reverse a conviction for "harmless error"; rather, the error must be "prejudicial." Second, an appellate court usually will not reverse where the defendant's attorney does not object to a prosecutor's misconduct, although Ohio law, in theory, calls for reversal for prosecutorial misconduct that is "so flagrantly improper as to prevent a fair trial . . . ." These two rules of law serve justice in most cases by

61 Id.; supra note 54.
62 See supra notes 38-47 and accompanying text.
63 Id.
64 Id.
65 Id.
67 See supra text accompanying note 12. Ethical Consideration 7-24 provides that "[t]he expression by a lawyer of his personal opinion as to the justness of a cause, as to the credibility of a witness, as to the culpability of a civil litigant, or as to the guilt or innocence of an accused is not a proper subject for argument to the trier of fact." OHIO CODE OF PROFESSIONAL RESPONSIBILITY EC 7-24 (1970).
ensuring that a conviction will be overturned only for substantial and significant reasons that go to the merits of the case.\textsuperscript{71}

These rules of the criminal law do not speak to questions of legal ethics, however, and it is important to keep the death penalty debate, including its emotionally and politically charged aspects, separate from the question at hand. We can argue about whether derogatory comments about the defendant’s exercise of a constitutional right should be subject to a per se rule of prejudice and reversible error.\textsuperscript{72} We can argue about the existence of an implied public right to the fruits of an “effective” criminal justice system, or whether such a right should be balanced against express constitutional protections for criminal defendants.\textsuperscript{73} We can argue about whether the rights of a victim should be given special consideration in a death penalty case.\textsuperscript{74} Whatever may be the solutions to any of these persistent questions, however, no rule of the criminal law and no result of the criminal justice system justifies or excuses conduct by prosecutors that violates the rules of legal ethics. And there lies the problem: there have been no consequences for the prosecutors’ violations of those rules in the cases in question.\textsuperscript{75}

\textbf{WHAT TO DO: A PLAN OF ACTION FROM THE LAW OF LEGAL ETHICS}

The law of legal ethics provides a ready answer to Chief Justice Moyer’s and Justice Wright’s questions, even if the criminal law is institutionally and doctrinally incapable of an answer.\textsuperscript{76} The truth is that the Supreme Court already knows what that answer is, and indeed, it has known for some time. In 1988, in \textit{State v. DePew}, the Court stated as follows:

There is one other alternative [to reversal of a death-penalty conviction] left to the courts in expressing our condemnation of intentional or unjustifiable misconduct by either prosecutors or defense counsel. Attorneys, trial courts, courts of appeals and this court should remain ever vigilant regarding the duties of counsel as exemplified in the following standards.

DR 1-102(A)(5) of the Ohio Code of Professional Responsibility provides that a lawyer shall not “[e]ngage in conduct that is prejudicial to the administration of justice.”

\textsuperscript{71} See Fears, 715 N.E.2d at 152; Gumm, 653 N.E.2d at 267.
\textsuperscript{72} See supra text accompanying notes 38-47.
\textsuperscript{73} See supra text accompanying notes 50-51. In fact, the Ohio Constitution says nothing whatsoever about an “effective criminal justice system.” The public’s right under the Constitution is to have an Executive who faithfully enforces the law. \textit{OHIO CONST. ART. III, § 8}. The law in question includes not only the criminal justice system but also the rules of legal ethics. Beyond that, the purported “balancing” of the public’s “right to justice” and the protections of accused persons under the federal and Ohio bills of rights seems to result in the latter’s going begging in all but the rarest of cases. See State v. Fears, 715 N.E.2d at 155-63 (Moyer, C.J., dissenting); see also infra note 117.
\textsuperscript{74} See Hunt, supra note 5, at A16 (quoting family member demanding justice for victim).
\textsuperscript{75} See Hunt, supra note 5. See also notes 15-26 and accompanying text.
\textsuperscript{76} See supra text accompanying notes 64-75.
DR 7-102(A)(5) states that a lawyer shall not "[k]nowingly make a false statement of law or fact." DR 7-106 provides that an attorney shall not "[s]tate or allude to any matter that he has no reasonable basis to believe is relevant to the case or that will not be supported by admissible evidence." The proposed standards of the American Bar Association for prosecutors provide in relevant part that "[j]t is unprofessional conduct to ask a question which implies the existence of a factual predicate which the examiner cannot support by evidence." ABA Standards Relating to the Prosecution Function and the Defense Function, The Prosecution Function (Tent. Draft 1970) 123, Section 5.7(d). These standards further provide that "[t]he prosecutor should not use arguments calculated to inflame the passions or prejudices of the jury."77

In order to preserve the fairness of trial proceedings and to deter further misconduct, it is henceforth the intention of this court to refer matters of misconduct to the Disciplinary Counsel in those cases where we find it necessary and proper to do so. We encourage all trial courts and appellate courts to take similar steps where appropriate.78

With due respect, thirteen years after State v. DePew, it is difficult to find evidence that any Ohio court, including the Supreme Court itself, has taken that statement of intention seriously.79 Indeed, and again with due respect, the fact that Chief Justice Moyer again must find himself asking "how do we stop prosecutors" from engaging in ethical misconduct at trial is evidence to the contrary.80

This writer’s respectful response to Chief Justice Moyer’s question, drawn from the law of legal ethics, therefore is as follows:

First, a violation of a rule of legal ethics should lead to disciplinary consequences for the prosecutor who engages in the misconduct at trial. Simply put, you can’t expect a problem to go away if you don’t create consequences for the person who creates the problem. The State of Ohio has a multi-layered lawyer disciplinary system that is nationally famous for its watchfulness, diligence, and vigor in pursuing attorneys who have violated the ethical rules. Its enforcement attorneys have been known to take cases to the United States Supreme Court to vindicate the principles that the system enforces.81 The bar

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78 Id. (emphasis added); accord State v. Fears, 715 N.E.2d at 155-63 (Moyer, C.J., dissenting); State v. Lorraine, 613 N.E.2d 212, 224 (Ohio 1993) (Wright, J., concurring).
79 See DePew, 528 N.E.2d at 542. The rare reversals include State v. Miller, No. 18011, 2000 WL 1369918 (Ohio Ct. App. 2d Dist., Sept. 22, 2000), but notwithstanding that the same prosecutor had earlier been involved in misconduct, that court did not name the prosecutor as suggested by Fears, see infra text accompanying note 88, nor does the opinion refer the case for discipline as called for in DePew, see supra text accompanying note 78. Two cases were referred to disciplinary counsel in State v. Miller-Cox, No. CA-8631, 1992 WL 127154 (Ohio Ct. App. 5th Dist. May 18, 1992), and State v. Shelton, No. 58737, 1991 WL 127154 (Ohio Ct. App. 8th Dist. June 27, 1991), but the prosecutor in State v. Hall, 665 N.E.2d 728 (Ohio Ct. App. 2d Dist. 1995), apparently escaped with an inconsequential chiding in the form of a reminder by a concurring judge that prosecutorial misconduct can be referred to disciplinary counsel.
80 See Hunt, supra note 5.
disciplinary authorities, including the Supreme Court's Board of Commissioners on Discipline and Enforcement and the Cincinnati Bar Association, need to turn their attention to prosecutorial misconduct in death-penalty cases in Hamilton County. When they do, prosecutorial misconduct may stop. If it does not, then the consequences can start.

Second, the Supreme Court, the First District Court of Appeals, and the Hamilton County Court of Common Pleas should take action against prosecutorial misconduct. Most obviously, as the Supreme Court observed in State v. DePew, they should refer cases of prosecutorial misconduct to the bar disciplinary authorities for review and prosecution. The Ohio Code of Judicial Conduct provides in Canon 3(D)(2) that "[a] judge who has knowledge that a lawyer has committed a violation of the Code of Professional Responsibility shall report the violation to a tribunal or other authority empowered to investigate or act upon the violation." This provision imposes a mandatory obligation upon a judge, and in not requiring that the violation raise a "substantial question" as to the lawyer's fitness to practice law, is stricter than the model provision in force in many other states. The question of the judges' knowledge is not in doubt, given the Supreme Court's holdings in the above cases and the content of the Ohio disciplinary rules. It is only a matter of marshalling the will to act, and reporting the ethics violations where they occur. It is a simple question of whether that provision of the Ohio Code of Judicial Conduct will or will not be obeyed.

Third, the Supreme Court and the First District Court of Appeals should be more active and more pointed in their reported decisions, in addressing prosecutorial misconduct. The Supreme Court's identifying prosecutors by name when it criticizes their trial misconduct is a welcome if too-recent development, but alone falls far short of an effective judicial response. That practice might well be applied in all cases and wedded to real criticism and judgment leveled against the prosecutorial misconduct. In apparent efforts to explain why such misconduct does not justify reversal under the harmless-error rule, the Court has often "criticized" misconduct in terms ranging from the

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82 The Cincinnati Bar Association is no stranger to ethics enforcement, but rather has an active disciplinary system. See, e.g., Cincinnati Bar Ass'n v. Fehler-Schultz, 597 N.E.2d 79 (Ohio 1992).
83 See DePew, 528 N.E.2d at 557.
89 Which of course should be coupled with action. Although one court of appeals described a prosecutor's statements of personal belief as "improper, and demonstrate an utter disregard for the Disciplinary Rules, the holdings of the Ohio Supreme Court, and our prior decisions," the court did not indicate that it would refer the case for disciplinary enforcement, and there is no reported decision involving discipline of the prosecutor in question. See State v. McComas, No. 93-CA-32, 1996 WL 71373 (Ohio App. 4th Dist. Feb. 15, 1996).
sternly avuncular to the tepid and luke-warm, perhaps even accounting for some of the professed confusion among prosecutors about “what the rules are.”

The State v. Sheppard case is a good example of this: in refusing to reverse based on the prosecutor’s comments about the victim’s state of mind, the Court lionized the prosecutor’s argument as mostly “restrained and straightforward and dealing reasonably with the facts of the crime,” but then trivialized the defendant’s objection by describing the offending reference as “two speculative comments” without even a passing reference to the applicable rules of legal ethics. The Court’s description of the same prosecutor’s constitutionally impermissible comments about the defendant’s failure to plead insanity as nothing worse than “[m]ore troublesome” sounds more in constitutional and ethical anomie than in judicial disapproval.

Unfortunately, the Jones case likewise has failed to vindicate the principles adverted to so long ago in DePew. The majority opinion mildly and inconsequentially chided the prosecutor for his “improper” remarks “allud[ing] to facts not in evidence.” Incredibly, the majority dismissed the defendant’s objection to the comment about the defense as a “search for doubt, not a search for the truth” without a word as to its ethical qualities. For its part, the concurring opinion said nothing whatsoever about the prosecutorial misconduct, still less about whether the case should be referred for disciplinary enforcement. There was no separate concurrence like Chief Justice Moyer’s in Fears, calling prosecutors and the Supreme Court yet again to task. The decision leaves one in mind of an old saying that might in the present context be recast as “this morale will continue until the beatings improve.”

Fourth, the Hamilton County Court of Common Pleas should independently enforce the rules of legal ethics in its courtrooms. A criminal defense lawyer cannot be expected to bell every ethical cat that strolls by where a defendant’s life is at stake, but a trial judge can: the defendant’s practical inability to object means that absent judicial action, prosecutorial misconduct too often will go without response. The usual approach of doing nothing unless and until the

90 See Hunt, supra note 5, at A16; text accompanying note 56. This author’s view is squarely to the contrary with regard to purported “confusion” among Hamilton County prosecutors. The explanations reported in the Cincinnati Enquirer that “the prosecutors don’t know what the rules are” or that “the Court is constantly changing the rules,” however appropriate for the consumption of a Hamilton County public that is not familiar with the rules in the first place, will not hold the first drop of water before a knowledgeable audience of lawyers or disciplinary authorities. See supra notes 27-47 and accompanying text.
92 Id.
93 739 N.E.2d at 318.
94 Id. at 318-19.
95 Id. at 321-23.
96 See id. passim.
PROSECUTORIAL MISCONDUCT IN DEATH-PENALTY CASES

defendant objects will not work if anything is to be done about the problem of prosecutorial misconduct at the trial level.97

The necessary approach is simple: the trial judges should "just say no" to prosecutorial misconduct in Hamilton County death penalty cases. Prosecutorial misconduct is not just a problem for the criminal defendant: it is a systemic problem for the fact and the appearance of justice in the Hamilton County Court of Common Pleas. It is a problem both for that Court as a judicial entity and for the judges trying the death-penalty cases. It is a problem that is exacerbated by its presence and persistence in high-profile, high-stakes cases that ought to involve none—or at least less, rather than more—of such conduct. Thus the trial judges should not wait for an objection but should take charge of the courtroom when prosecutorial misconduct occurs, particularly where the misconduct implicates the defendant's specific constitutional rights, and deliver a rebuke that will make clear both to the prosecutor and to the jury that the prosecutor has acted wrongly. The trial judges should take other and further action if the same or similar problems appear in the same case or with the same prosecutor.98

Fifth, the Supreme Court of Ohio and the Ohio State Bar Association should consider adopting a rule of legal ethics for both public and private lawyers, that places vicarious, supervisory, and institutional responsibility for attorneys' ethical misconduct on the office or firm, partners or managers, and supervising attorneys under whom that attorney practices law. A vicarious- and supervisory-responsibility provision is already contained in the American Bar Association's Model Rules of Professional Conduct, Rules 5.1 through 5.3, which are in force in the large majority of jurisdictions.99 An institutional-responsibility provision is contained in proposed Rule 5.1(a) of the American Bar Association's Ethics 2000 Commission, which would extend to the "firm" as an institution, including groups of governmental attorneys.100

Sixth, the Hamilton County prosecutors should not violate the rules of legal ethics in death-penalty cases. The prosecutor has a duty to seek justice, not merely to seek conviction—even in death-penalty cases.101 This article will not attempt to assess the reasons for such misconduct in individual circumstances, which is for those attorneys and their supervisors to address. As to institutional

97 If nothing else, as between defense attorneys in death-penalty cases on the one hand and trial judges on the other, the latter are eminently well suited and certainly better able than the former to do something about the problem.

98 See supra text accompanying notes 83-87.

99 MODEL RULES OF PROFESSIONAL CONDUCT Rules 5.1-5.3 (1998). The limits of vicarious or supervisory ethical responsibility for attorneys' misconduct on the office or firm, partners or managers, and supervising attorneys under whom that attorney practices law. A vicarious- and supervisory-responsibility provision is already contained in the American Bar Association's Model Rules of Professional Conduct, Rules 5.1 through 5.3, which are in force in the large majority of jurisdictions. An institutional-responsibility provision is contained in proposed Rule 5.1(a) of the American Bar Association's Ethics 2000 Commission, which would extend to the "firm" as an institution, including groups of governmental attorneys.


circumstances, one would assume that, like any good law firm, the Hamilton County Prosecutor’s office is concerned about complying with the rules of legal ethics, and that its attorneys work both individually and together towards that end. That is to their credit, even if it is as it should be. Model Rules 5.1 through 5.3 and proposed Rule 5.1(a) provide, however, systemic consequences where voluntary systems of ethical compliance break down.

It appears that, with due respect, the voluntary systems of ethical compliance in the Hamilton County Prosecutor’s office, if not broken down, may not be working effectively enough. The Hamilton County prosecutors’ “ethical error rate” is nearly 30 percent (14 of 48 cases) where the death penalty is successfully sought. That the 30 percent may be diluted by cases where the jury rejects the death penalty or a plea bargain is reached is simply beside the point. That rate is far too high where the moral legitimacy of imposing the law’s harshest consequences depends not only upon the courts’ and the prosecutors’ observance of the United States and Ohio Constitutions, and of criminal law and procedure, but also upon the observance of the rules of legal ethics.

LET US NOT JOUST WITH STRAW MEN

No proposal is likely to go unchallenged, particularly when it is joined with a plan of action for creating consequences and ultimately changing the conduct of lawyers. Prosecutorial misconduct in death-penalty cases is too important a subject to permit issue to be joined on anything other than the merits of the proposal: as Justice Wright noted in his concurrence in State v. Lorraine,

[i]t is crucial that attorneys demonstrate a proper regard for the constitutional requirement that trials be fair. The right to a fair trial is a hallmark of our democracy and something of which we are rightly proud. It is reprehensible for prosecutors, as agents of our government, to disregard this essential right for any reason.

A few words therefore are in order about what the above suggestions are not. First, these suggestions and their predicate contain no irretrievable element of censure upon the Hamilton County Prosecutor’s office. Whatever actions, attitudes or inadvertencies led to the prosecutorial misconduct in question seem well within the capacity and expressed willingness of that office to address. It must be said, however, that the decisions in the above cases speak for themselves, and that the occurrence of ethical misconduct is not open to any apparent question. The facts of the death-penalty cases make clear that the Hamilton County Prosecutor’s office’s expressed willingness should be joined

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102 See Hunt, supra note 5, at A16; text accompanying notes 53-67.
103 See MODEL RULES OF PROFESSIONAL CONDUCT Rules 5.1-5.3 (1998).
104 See Hunt, supra note 5, at A1; see supra note 27 and accompanying text.
106 See Hunt, supra note 5.
107 Id.
108 Id.
with state and local ethical enforcement (as is the case in all areas of the practice of law) to achieve better results.

Second, these suggestions will not result in an undue chilling of prosecutorial zeal or effectiveness, in death-penalty cases or in general. Canon 7 of the Ohio Code of Professional Responsibility provides that "[a] lawyer should represent a client zealously within the bounds of the law . . ." The law in question includes the rules of legal ethics that govern all lawyers, including prosecutors. Bar discipline is of varying severity and consequences. The consequences can be tailored to meet the nature and scope of the misconduct. Leaving that aside, even if there is some chilling effect, the improvement in the criminal justice system's ethics quotient in death-penalty cases will be well worth it.

Third, these suggestions will not impair the quality of justice in death-penalty cases, but rather will improve it. As matters now stand, death-penalty convictions that are tainted with prosecutorial misconduct do not result in reversals, even when the misconduct derogates from important constitutional rights. This is intolerable in a system that depends on the Constitution and the Bill of Rights: it undermines the moral integrity of the criminal justice system, it dishonors the rule of law, it degrades public respect for the legal system (both among criminal defendants and among citizens who come to think that prosecutors' ethical violations do not matter), and it damages the public reputation of the legal profession. If the criminal justice system cannot or will not respond with consequences, a response and consequences from the disciplinary system is all the more necessary.

Fourth, these suggestions do not propose that the problems identified in the article are the only problems that exist in the criminal justice system, or that Hamilton County is unique in having its problems. Clearly—and sadly, neither of those things is true, although both are beyond the scope of this article.

Finally, these suggestions will not impose upon any prosecutor rules that do not already apply to all lawyers, or rules that any prosecutor could or should object to. Rather, they call only for the enforcement of existing rules of legal ethics. We may assume that the Hamilton County Prosecutor's office would like nothing better than to eliminate prosecutorial misconduct and ethical violations

110 See id. EC 7.1.
111 See Ohio Supreme Court, Rules Governing the Bar, IV, § 1; V, § 6(B)(5). The rules presently provide only for public discipline, and some thought might be given to authorizing private admonitions and reprimands should that prove necessary to persuade trial and appellate judges to use the disciplinary system for its intended purpose. That suggestion, of course, preterms whether and why such an amendment should be necessary to achieve judicial compliance. See supra text accompanying notes 83-87.
112 A "zero-tolerance" program would not be entirely unwarranted. If Indiana University could put legendary coach Bobby Knight on a "zero-tolerance" leash and then fire him when he allegedly behaved inappropriately towards an allegedly disrespectful student, the Ohio courts can place prosecutors in death-penalty cases on a program of "zero-tolerance" for violations of the rules of legal ethics. See Knight firing causes chaos on IU campus, CINCINNATI ENQUIRER, Sept. 12, 2000, at B1.
in its death penalty cases. We may be confident that that office would agree that the prosecutor’s role is an important one that carries with it special responsibilities in the administration of criminal justice. All things being equal, a clean prosecution is easier to defend on direct appeal and in habeas corpus proceedings than a dirty prosecution. Made up as it is of members of the legal profession, the Hamilton County Prosecutor’s office can only be in favor of lawyer discipline where discipline is warranted, even if the lawyer proves to be one of its own. It seems clear, therefore, that there should be universal agreement among judges and attorneys that these suggestions should be implemented forthwith.

THE PRAYER FOR RELIEF

The above premises considered, this writer respectfully prays that the Supreme Court of Ohio take upon itself the forging of a full, complete and sufficient solution for the problem that it identified so clearly and accurately in 1988 in State v. DePew, that Justice Wright addressed in 1993 in his concurrence in State v. Lorraine, and that Chief Justice Moyer raised again in 2000 in his question at oral argument in State v. Jones. Now is the time.

At one level, the Supreme Court does not have the answers to Chief Justice Moyer’s question about “[h]ow do we stop” the problem of prosecutorial misconduct because it has been looking for answers in all the wrong places. These death-penalty cases come before the Court as criminal justice matters. An appeal in a criminal case can correct legal and constitutional error, but is not designed or (apparently) intended to reach ethical misconduct as such. It is fair to say, however, that the court may wish to reexamine its harmless-error rules, since the federal courts should not be required to step in and grant federal habeas relief because the Ohio state courts will not take action to prevent even prejudicial prosecutorial misconduct. A disciplinary enforcement proceeding is both designed and intended to reach ethical misconduct as such. A case of prosecutorial misconduct will not

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115 See supra text accompanying notes 4-7.

116 See supra text accompanying notes 50-67.

117 Despite the verbiage in DePew, the federal court in DePew v. Anderson, 104 F. Supp. 2d 879 (S.D. Ohio 2000), did what the Ohio courts failed or refused to do in six opportunities, and reversed the death-penalty conviction because of prosecutorial misconduct. The DePew case brings to mind a lawyer who was arguing a criminal case in the Supreme Court of Georgia some years ago, who was asked by one of the justices, “so do you expect us to reverse your client’s conviction because of that?” Not wishing to be untruthful with the court, although perhaps with more candor than may have been ideal, the lawyer is said to have replied, “no, your Honor. I expect the court to affirm the conviction, and that I will have to file a habeas petition and get the federal court to do it.” (The author was recently advised by an authoritative source that the lawyer’s response was that he would have to “get a real court” to reverse the conviction.)

118 Cf. DePew, 528 N.E.2d at 557 (“one other alternative”).
be redressed unless and until the Court turns to the only other tool that it has for
dealing with ethical misconduct. The Court will have to use the bar disciplinary
system for the purpose for which the Court itself designed and intended it.119

So where are the answers? As in the television game show of Jeopardy, the
answers came before the questions.120 The time to answer the questions is long
past, and the buzzer is going off. The answers are right in front of the Supreme
Court, in the Ohio Code of Professional Responsibility, in the rules and
procedures of the bar disciplinary system,121 and in the majority opinion in State
v. DePew.122 The Court will rediscover the answers to Chief Justice Moyer’s and
Justice Wright’s questions when these cases come before the Court as
disciplinary matters, not otherwise and not before.123 But if the Court does not
begin—however belatedly—to refer cases for disciplinary proceedings so that
prosecutorial misconduct can be met with a proper disciplinary response, then
the answer to the Justices’ questions will no longer be found in State v. DePew.
We will have a new question in Final Jeopardy: “Why do prosecutors violate the
rules of legal ethics in death-penalty cases?” And we will have a new answer on
the Final Jeopardy board that plainly reads: “Because the Supreme Court of
Ohio either can’t or won’t do anything about it.”

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119 The same principle applies, of course, to anyone else who wants to do anything about
prosecutorial misconduct in death penalty cases, including individual justices of the Supreme
Court. Id.

120 The analogy is not perfect, since the state of “double jeopardy” that is essential to the game
show is prohibited in the death-penalty context. See U.S. Const. amend. V; Ohio Const. art. I, §
10.

121 See Ohio Code of Professional Responsibility DR 7-106(C) & 1-102(A)(5) (1970); Ohio

122 See State v. DePew, 528 N.E.2d 542 (Ohio 1988). The answers are also in Chief Justice
Moyer’s dissent in State v. Fears, 715 N.E.2d at 155-63, and in Justice Wright’s concurrence in
State v. Miller, 613 N.E.2d at 224. The answers are ignored in State v. Jones, 739 N.E.2d 300
(Ohio 2000). See supra text accompanying notes 93-96.

123 Id. See also supra text accompanying notes 4-7.
PRIVATE LETTER AND REVENUE RULINGS:
REMEDY OR RUSE?

by Professor Dale F. Rubin

Private letter and revenue rulings pose many interesting questions in connection with the effect they can have on both the past and future actions of taxpayers and their lawyers. Unlike other agency nonlegislative interpretive rulings which, since the case of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, arguably have become subject to one standard of judicial review, private letter and revenue rulings remain the topic of a strenuous debate concerning the deference they should be accorded when a particular transaction becomes the subject of litigation between the Internal Revenue Service and the taxpayer. The effect of the issuance of private letter or revenue rulings on the taxpaying community can sometimes be so significant it cannot be doubted that, in such instances, such rulings have the same effect as a statute or a regulation.

Such rulings can send lawyers scurrying to revise their advice to their clients in order to avoid potential malpractice and a whopping tax bill to the persons they represent. In spite of Treasury Regulations and court rulings seeking to diminish the impact of such rulings, the continued reference to them by both the Service and the courts forces the taxpayer to pay close attention to such rulings when fashioning a transaction. The fundamental question this paper poses is whether the private letter and revenue rulings programs are the remedy to providing guidance to the taxpayer regarding the Service's position on a particular matter or a ruse given the uncertainty as to the deference such rulings will be given in the litigation context.

This paper will (1) examine the historical underpinnings of the private letter and revenue rulings program, (2) discuss the use of such rulings by both the Service and the courts, and (3) propose a remedy to help eliminate some of the

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1 Appalachian School of Law, Grundy, Virginia. Professor Rubin is a graduate of Stanford University and Boalt Hall. He teaches Business Associations, Torts, Administrative and Criminal Law. Professor Rubin has written many articles regarding the constitutionality of public subsidies to private corporations. Incidentally, Professor Rubin was a world record holder in the 440 yard relay at Stanford.

2 The theoretical difference between legislative and nonlegislative rules is clear. A legislative rule is essentially an administrative statute—an exercise of previously delegated power, new law that completes an incomplete legislative design. Legislative rules frequently prescribe, modify, or abolish duties, rights, or exemptions. In contrast, nonlegislative rules do not exercise delegated lawmaking power and thus are not administrative statutes. Instead, they provide guidance to the public.


4 467 U.S. 837 (1984). The applicability of the *Chevron* case to private letter and revenue rulings will be discussed later in this paper.

4 This raises an interesting question regarding what is law. Is it what the statute and regulations say it is or can the reaction of the public in certain instances to nonlegislative rulings imbue them with legal force and effect?
uncertainty in the taxpaying community regarding the propriety of their reliance on such rulings.

A. HISTORICAL UNDERPINNINGS OF THE PRIVATE LETTER AND REVENUE RULINGS PROGRAMS

1. Private Letter Rulings

Letter rulings are written statements issued by the Service which interpret and apply the tax laws to a set of stated facts.\(^5\) "...[L]etter rulings are issued only to taxpayers who specifically request them, and bind the agency only with respect to the particular taxpayer to whom they are issued."\(^6\) Taxpayers voluntarily seek letter rulings in advance of completing a transaction in order to obtain some measure of certainty or security with respect to the position of the Service.\(^7\) The history of private letter rulings commences with the beginning of the modern income tax in 1913 when the Bureau of Internal Revenue attempted to respond to any question it received, whether the transaction was completed, contemplated, or merely hypothetical.\(^8\) Even though the Bureau stated that it was not bound by the answers it gave, the number of requests for rulings was so large that in 1919, the Bureau decided to answer only those questions involving completed transactions of real, identified taxpayers.\(^9\) By the late thirties, taxpayers with prospective transactions needed some general procedure for ascertaining the tax consequences of those transactions.\(^10\) Thus, in 1938 Congress gave the Commissioner of Internal Revenue discretionary authority to enter into "closing agreements" which were legally binding on the Bureau with respect to prospective transactions.\(^11\) Since the closing agreements were consummated only after review and approval by high-level officials, the Bureau was untroubled by the binding effect of such agreements.\(^12\)

Due to the fact that such requests for closing agreements kept pouring into the Bureau even though the taxpayers needs could be met by a less formal procedure, which at the time did not exist, the Bureau developed a document called a "letter ruling," in which a lower level staff member indicated what action would probably be taken if the taxpayer were to request a formal closing

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\(^7\) See id. Although this statement is actually true, as I shall explain, the use of letter rulings have effects beyond the particular taxpayer who is the subject of the letter ruling.

\(^8\) See James P. Holden & Michael S. Novey, *Legitimate Uses of Letter Rulings Issued to Other Taxpayers-A Reply to Gerald Portney*, 37 TAX L. 337, 338 (1983-1984). This historical description of the development of private letter rulings relies heavily upon this article.

\(^9\) Id. (citing Mimeograph 2228, 1 C.B. 310 (1919)).

\(^10\) Id. at 339.


\(^12\) Id.
agreement. Even though the letter ruling was not binding, most taxpayers at the
time found the new procedure sufficient. In 1954, the renamed Internal
Revenue Service announced that taxpayers receiving favorable rulings would be
protected if the ruling was in error or the Service subsequently changed its
position. This position still holds true today.

2. Revenue Rulings

A revenue ruling is an interpretation or explanation of the tax laws by the
Service and is designated as a "revenue ruling." Revenue rulings generally
describe a set of hypothetical facts and state the Service's legal conclusions
based on those facts. The individuals who participate in the formulation of
Treasury regulations also draft and review revenue rulings. Rulings are
prepared by attorneys in the Office of the Chief Counsel and approved by
the Chief Counsel, Commissioner of Internal Revenue and Assistant Secretary (Tax
Policy). Revenue rulings are considered interpretive rules for purposes of the
Administrative Procedure Act (APA), and are exempt from notice and comment
issuance procedures and are published without a precedent announcement.
Revenue rulings are published in the Internal Revenue Bulletin. If a taxpayer
carries out a transaction in reliance on a revenue ruling, and the facts are
substantially the same as those contained in the ruling, the Service will be bound
to its determination in the ruling. Parenthetically, it is important to distinguish revenue rulings from Treasury
regulations, which have the force and effect of law. Treasury regulations are
binding upon both the taxpayer and the Service and are subject to the APA
requiring the Service to provide notice to the public of a proposed regulation,
thereby permitting the public the opportunity to comment on the intended
regulation. While revenue rulings may be revoked by the subsequent issuance
of a contrary ruling, the repeal of a Treasury regulation is a much more difficult

13 Id. at 340.
14 See Holden & Novey, supra note 8, at 340 (citing Caplin, Taxpayer Rulings Policy of the
  Internal Revenue Service: A Statement of Principles, 20 N.Y.U. INST. 1, 4-5 (1962)).
15 Id. (citing Rev. Rul. 54-172, § 12.05, 1954-1 C.B. 394, 401).
18 See Galler, supra note 6, at 1044.
19 Id.
20 See 5 U.S.C. §§ 551-559, 701-706 (1994); see also Wing v. Commissioner, 81 T.C. 17, 27
  (1983) (stating that revenue rulings have been called the "classic example" of interpretive rules).
21 See Galler, supra note 6, at 1044.
22 Id.
24 See Galler, supra note 6, at 1049.
25 See 5 U.S.C. §§ 553(b), (c) (1994); see also Treas. Reg. §§ 601.601(a)-(c) (as amended in 1983).
Thus, the level of confidence that a taxpayer has when acting pursuant to a Treasury regulation is significantly higher.

Historically, until about thirty-seven years ago, it had been the practice of the Service to publish rulings only when the issues involved were thought to be important enough to be of general interest. (Even today, revenue rulings may be published when there is a strong demand for private letter rulings on an issue and the Service recognizes that the need for general guidance may be satisfied with a revenue ruling.) In 1952, in order to assure the public of the impartiality of tax administration, the Subcommittee on Administration of the Internal Revenue Laws of the Committee on Ways and Means concluded that all rulings should be made public. In response, the Service committed itself to publish all communications to taxpayers and field offices involving substantive issues of tax law and all procedures affecting the rights and duties of taxpayers, which communications and procedures were intended by the Service to be used as precedents and guides. When the program commenced in 1953, the Service identified three principal purposes: (1) revenue rulings would be a vehicle through which the National Office could inform field personnel of precedents or guiding principles, (2) The Internal Revenue Bulletin would provide a permanent, indexed reference to Service positions, and (3) revenue rulings would enable the public to review interagency communications that the Service uses as precedents or guides.

This brief examination of the history and the current statutory framework of the ruling programs clearly indicates that the primary purpose of the programs is to provide taxpayers with guidance as to the Service’s position in relation to and the (possible) tax implications of the taxpayer’s future transactions. The issue of how much should the taxpayer and their lawyers rely on such guidance is the subject of the next section of this paper.

26 See Holden & Novey, supra note 8, at 347.
29 See Portney, supra note 27, at 752.
32 Id.
33 Id.
34 See Phillabaum, supra note 28, at 286-87.
B. HOW MUCH GUIDANCE, IF ANY, DO RULINGS PROVIDE?

1. Private Letter Rulings

The determination of how much guidance private letter rulings provide is ensconced in a quagmire of contradiction. Internal Revenue Code Section 6110(j)(3) states, in pertinent part, that letter rulings "may not be used or cited as precedent." Unfortunately, the clear wording of this statute does not end the controversy surrounding the guidance issue. In spite of the statute, both the Service and the courts refer the letter rulings for guidance in both the bureaucratic and the litigation context.

(a) Reliance on Letter Rulings by the Service

Holden and Novey posit the notion that "human institutions rarely behave randomly." Thus, in order to predict an institution's future conduct, one should examine its past and current behavior. With respect to letter rulings, the authors state the Service has never denied that its written determinations are accurate predictors both of its future written determinations and of its other conduct interpreting the Code. The authors also state that "notwithstanding the limited review to which letter rulings are subject, they generally are of high quality" and "likely to reflect the present position of the Service when one has been established." They further state that even when the Service has not taken an established position, letter rulings usually reflect the position the Service eventually will take.

The Service is unlikely to reverse itself once a position has been established, and therefore letter rulings (and technical advice memoranda) tend to be highly predictive of the conduct of both the National and the District Offices. In fact, although examining agents are instructed not to use such written determinations "as precedents," they are encouraged to use them "as a guide with other research material in formulating a district office position on an issue."

Furthermore, statements by Service personnel reveal their continued reliance on letter rulings. In a meeting of the Section of Taxation of the American Bar Association, the Assistant Commissioner (Employee Plans and Exempt Organizations) relied extensively on letter rulings to describe new developments.

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36 See Holden & Novey, supra note 8, at 344.
37 Id.
38 Holden & Novey, supra note 8, at 344.
39 See id.
40 Id.
41 Holden & Novey, supra note 8, at 344.
42 See id. at 344-45.
43 Id. at 345.
44 Id. (citing INTERNAL REVENUE MANUAL § 424(14).3(3)).
45 Id.
in the laws that he was responsible for administering. Finally, the authors cite a statement by a low-level employee of the Service that even though written determinations are not "precedent", they are persuasive to other staff members and him because "we know that the guys that wrote them were on our side." Thus, it appears that notwithstanding Internal Revenue Code Section 6110(j)(3), letter rulings are in fact deemed persuasive authority by the Service. Indeed, it would be foolish to believe that an organization would invest so much intellectual effort and time in such a program not to rely on and make reference to the product it yields.

(b) Reliance on Letter Rulings by the Courts

In a classic example of form over substance, the courts have given "lip-service" to the no precedent prohibition of the Code and have continued to refer to letter rulings in their decisions. While eschewing the precedential value of letter rulings, the courts nevertheless characterize letter rulings "as evidence of administrative interpretation." In a case in which taxpayers relied on actuarial tables prepared and distributed by the Service to determine the value of a remainder interest in real property, the court, in ruling for the taxpayers stated:

The IRS can hardly set forth actuarial valuation tables carrying the imprimatur of the government, issue revenue rulings on their proper use, and advise taxpayers through private letter rulings that the tables should be used in remainder interest sales and then protest when disinterested commercial parties... refused to bicker over the purchase price when the fair market value of the fee has been properly determined, [and] the measuring life meets the rules governing the tables' use....

The IRS had contended the absence of negotiations between the taxpayers was evidence that the remainder interest was not purchased at a fair market value. The aforementioned case is also significant in another respect. Not only does it refer to private letter rulings, it also implies that disinterested parties may rely on them both in preparing their transactions and in court.

In Hanover Bank v. Commissioner, the Commissioner reversed a position he had taken in a number of previous private letter rulings, to the detriment of the taxpayers. The Court found that although the taxpayers were not entitled to rely on letter rulings not specifically issued to them, the prior rulings were

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46 Id. (citing Winborne, Expanding the Scope of Taxation of Exempt Organizations: Trends in Unrelated Business Income, in Winborne, Hopkins, Hopkins, & Boisture, Expanding the Scope of Taxation of Exempt Organizations: Trends in Unrelated Business Income (unpublished outlines of remarks prepared for a panel discussion at meeting of ABA Section of Taxation, July 30, 1983, Atlanta, Ga.)).
47 See Holden & Novey, supra note 8, at 346.
48 Id. at 347.
49 ABC Rentals of San Antonio, Inc. v. Commissioner, 142 F.3d 1200, 1207 n.5 (10th Cir. 1998) (citing Commercial Bank N.A. v. United States, 93 F.3d 225, 230 (6th Cir. 1996)).
50 Wheeler v. United States, 116 F.3d 749, 769 (5th Cir. 1997).
51 See id.
52 369 U.S. 672 (1962).
significant since they disclosed the interpretation of the statute by the agency charged with administering the revenue laws. They provided further evidence that the language of the statute compelled the Court’s construction of the tax provision at issue.

Finally, in Wolpaw v. Commissioner of Internal Revenue which involved whether tuition waivers should be included in the taxpayers gross income, the court stated: “While this Private Letter Ruling [which was issued to other taxpayers excluding the tuition waivers] is not binding precedent upon the Internal Revenue Service as to other taxpayers, or upon this Court [citing I.R.C. § 6110(j)(3) (1988)], in the absence of any Treasury Regulations directly on point, we view it as evidence that the Internal Revenue Service treated tuition remissions like the one benefiting Mrs. Wolpaw as a “scholarship.” (emphasis added).

The aforementioned discussion clearly indicates, that in spite of section 6110(j)(3), it makes sense for a taxpayer not the subject of a private letter ruling, nevertheless to rely on or cite such rulings in court.

(c) Other Non-Party Taxpayer Incentives For Reliance On Letter Rulings

There are also other incentives a taxpayer who is not a party to a letter ruling may have for relying on such rulings:

As previously mentioned, the generally high quality of the National Office’s written determinations means that the interpretation embodied in any individual letter ruling is unlikely to be fundamentally changed. Thus, the expected cost of reliance (i.e. the cost of the Service changing its mind multiplied by the likelihood of that event occurring) is relatively low.

The cost in both time and money for a taxpayer to obtain an individual letter ruling is substantial. Thus, a taxpayer may deem it a better option to obtain a legal opinion from an attorney based on previous letter rulings.

A taxpayer’s confidence is enhanced by the fact that since letter rulings are open to public inspection, the taxpayer is able to examine and detect a trend, if any, in the Service’s mindset and act accordingly.

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53 Id. at 686 (footnote omitted).
55 47 F.3d 787 (6th Cir. 1995).
56 Id. at 792.
57 See Holden & Novey, supra note 8, at 349.
58 Id.
59 Id. The current filing fee is $3850 and the attorney’s preparation fee is in the range of $4000-$8000.
60 Id.
61 See I.R.C. § 6110(a) (1994); see also Treas. Reg. § 301.6110-1 (1977). Letter rulings are also available on-line and in print.
62 See Holden & Novey, supra note 8, at 349.
Finally, it should be mentioned the Service has the authority to revoke or modify a letter ruling that is found to be in error or not in accord with the Service’s current views. However, the regulations authorize the Service to apply its power to revoke only prospectively “except in rare or unusual circumstances.” In fact, the practice of the Service appears to be not to revoke letter rulings retroactively which are favorable to the taxpayer. This provides an additional reason why a taxpayer should deem it reasonable to rely on private letter rulings, especially if they are favorable to the taxpayer.

2. Revenue Rulings

While the issue regarding reliance of private letter rulings is characterized by a rampant disregard of the statute prohibiting such reliance, the ability of the taxpayer to rely on revenue rulings which by statute are binding on the Service, is substantially tempered by the plethora of standards the courts have devised regarding the weight or deference to be accorded such rulings. Since either the Courts of Appeals or the Tax Court decides most tax cases, I will discuss the standards of review applied by these courts separately.

(a) Courts of Appeals

Courts of Appeals appear to apply three different standards regarding the weight to be accorded revenue rulings. But making the issue even more complex is the fact that the courts that purport to apply the same standard do not, in fact, do so. Before discussing the standards, it is important to state that traditionally courts of appeals have agreed that revenue rulings do not have the same force and effect as Treasury Regulations and are not binding on the courts. One court explained the rationale for the court of appeals’ refusal to equate revenue rulings with Treasury Regulations is that revenue rulings are not issued in accordance with APA notice and comment procedures. In spite of this traditional posture, it appears the courts of appeals are leaning toward approaches, all of which mandate some deference to revenue rulings.

65 See James B. Lewis et al., Report on Exercise by the Treasury Department and the Internal Revenue Service of the Authority Granted by the Internal Revenue Code Section 7805(b) to Prescribe the Extent to which Tax Rulings or Regulations shall be Applied Without Retroactive Effect, 42 TAX.LAW. 621, 647 (1989).
66 See generally Brook, Inc. v. Commissioner, 799 F.2d 833, 836 n.4 (2d Cir. 1986) (stating a revenue ruling is not entitled to the deference accorded a Treasury Regulation or statute); Higginson v. United States, 238 F.2d 439, 446 (1st Cir. 1956) (determining that an administrative ruling does not rise to the stature of a regulation and does not have the force thereof).
(i) Reasonable and Consistent

The "reasonable and consistent" standard was first applied to a revenue ruling in 1979 in *Dunn v. United States* 68 which involved whether a deduction for a farming expense resulted in a material distortion of income. In this case, the court declared that revenue rulings "have the force of legal precedents unless unreasonable or inconsistent with the provisions of the Internal Revenue Code." 69 Prior to Dunn the "reasonable and consistent" standard had only been applied to regulations. 70 Even though no other court of appeals had ever followed such a radical approach as that used in Dunn with respect to revenue rulings, the courts now employ the "reasonable and consistent" phraseology set forth in the Dunn decision in a variety of circuits. Different circuits, however, accord differing levels of deference.

The Second Circuit, in *Amato v. Western Union International, Inc.*, 71 ignoring all precedents under which revenue rulings were deemed to have little or no weight, 72 stated: "Revenue rulings issued by the I.R.S. are entitled to great deference, and have been said to 'have the force of legal precedents unless unreasonable or inconsistent with the provisions of the Internal Revenue Code.'" 73 The Sixth Circuit has applied the reasonable and consistent standard in a number of cases but has no uniform rule with respect to the weight that revenue rulings are to be given. In some instances, "some deference" 74 has been accorded, while "great deference" or "force of legal precedents" is the standard used by other courts in the circuit. 75 In *Walt Disney Inc. v. Commissioner*, 76 the Ninth Circuit adopted a reasonable and consistent test while awarding "great deference" to the ruling that complied with the standard. 77

(ii) Deference to Administrators

Six courts of appeals, at one time or another, have given special treatment 78 to revenue rulings simply because they represent constructions of the Code by

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69 Id. at 993.
71 See Galler, supra note 6, at 1064.
72 773 F.2d 1402 (2d Cir. 1985).
73 See Galler, supra note 6, at 1064 (citations omitted).
75 Johnson City Medical Ctr. v. United States, 999 F.2d 973, 976 (6th Cir. 1993).
76 Progressive Corp. v. United States, 970 F.2d 188, 194 (6th Cir. 1992).
77 4 F.3d 735 (9th Cir. 1993).
78 See id. at 740.
79 See Galler, supra note 6, at 1068.
the agency charged with the Code’s administration. This standard, however, has been surrounded by controversy:

I believe that deference to the IRS is not appropriate if premised upon superior skills or knowledge possessed by agency staff members relative to private practitioners. Not only does the tax bar include many individuals with considerable ability and professional experience, but many of these lawyers have served as members of the Treasury Department and the IRS. Therefore, I cannot conclude that the IRS lawyers are better as a group than the private bar. [Although] the IRS is more expert in the tax law than are [most] judges, … the agency’s greater proficiency in tax law, however, should not automatically give rise to deference…

In examining some of the pitfalls to the “deference to administration” approach, Galler explains this approach gives the IRS a significant advantage. In fact, such deference actually encourages the agency to issue rulings since the mere existence of such a ruling improves the likelihood of the agency prevailing in cases in which a ruling is involved. However, when a ruling is involved, more, not less judicial scrutiny is required. Since a ruling is not subject to the notice and comment procedures mandated by the APA, a revenue ruling is not exposed to public examination. It is also important to remember the IRS is the agency charged with collecting tax revenues; thus, it cannot be doubted that some amount of bias is present in the process of issuing revenue rulings. Also, as IRS employees are no different from anyone else, they will exercise all power they perceive that they have. If revenue rulings are accorded almost the same deference as Treasury Regulations, it could encourage the Service to issue rulings that are decidedly contrary to the interest of the taxpayer.

(iii) Chevron Defe rence

There is a continuing controversy whether the standard set forth in the Supreme Court case of Chevron U.S.A. v. Natural Resources Defense Council, Inc. applies to revenue rulings. The Sixth Circuit is the only circuit to have applied Chevron in the context of IRS revenue rulings, but it has not embraced

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80 See generally Wood v. Commissioner, 955 F.2d 908, 913 (4th Cir. 1992) (stating that “[i]t is well-established that considerable weight is to be given to an agency’s construction of a statute that it is charged with administering”); Brook, Inc. v. Commissioner, 799 F.2d 833, 836 n.4 (2d Cir. 1986) (stating the Court gives some weight to the Commissioner’s reading of the statute, because it expresses the view of the agency whose duty it is enforce the statute); United States Trust Co. v. IRS, 803 F.2d 1363, 1370 n.9 (5th Cir. 1986) (stating that “[r]evenue rulings are entitled to deference insofar as they represent the ‘studied view of the agency whose duty it is to carry out the statute’”).

81 Galler, supra note 6, at 1069, 1070.

82 See id. at 1086.

83 Id.

84 Id.

85 Id. at 1088.

Chevron as controlling. 87 In Chevron, the Court had to decide the validity of an EPA regulation, which allowed states to treat all pollution-emitting devices within the same industrial plant as though they were encased within a single "bubble." 88 Prior to analyzing the "bubble" regulations, the Court established a two-step test with respect to the deference to be accorded administrative interpretations: (1) The first step is to determine whether Congress has directly spoken to the precise question at issue. 89 If so, both the agency and the court must give effect to the unambiguously expressed intent of Congress. 90 (2) If the court determines Congress has not directly spoken to the precise question at issue, the court then determines whether the agency's interpretation is based on a permissible construction of the statute. 91 The Court also stated that a "permissible construction" of a statute is one that is reasonable. 92 Thus, if the court determines that an agency's interpretation is reasonable, then it will be given controlling weight. 93 Although the Court does not specifically state that its decision in Chevron applies to revenue rulings, certainly the language is broad enough to encompass such rulings.

However, applying the Chevron analysis to revenue rulings has ominous effects. If, in the absence of a statute or a regulation, administrative interpretations or rulings are to be given controlling weight if reasonable and not subject to either public or judicial scrutiny, the protection of the taxpayer from draconian agency rulings would be all but lost. It is for these reasons some courts have refused to apply the Chevron analysis to interpretative rules issued without notice and comment. 94 In addition, one writer has stated that applying Chevron deference to non-notice and comment rules contravenes the traditional distinctions between legislative and interpretative rules, the latter category into which revenue rulings fit:

The legal effect of an administrative rule is largely a function of delegation. Legislative rules are entitled to legislative effect precisely because Congress has explicitly manifested its intention to delegate authority to the issuing agency to create rules that complete a statute or affect rights and obligations. Interpretive rules do not issue from specific statutory deputations, and so are subject to greater scrutiny by the courts. The APA mandates notice and comment

87 See Galler, supra note 6, at 1071.
89 Id. at 842.
90 Id. at 843 n.9.
91 Id. at 842-43 (footnotes omitted).
92 Id. at 843.
93 Id. at 840.
94 See Robert A. Anthony, Which Agency Interpretations Should Bind Citizens and the Courts?, 7 Yale J. On Reg. 1, 30, 36-40 (1990). Professor Anthony has opined that the process of inferring a delegation of policymaking authority in the absence of a statute should encompass two distinct stages: (1) the court must find that Congress has implicitly delegated policymaking authority with respect to the subject matter, and (2) that Congress has implicitly delegated authority to issue rules in the format in which the rules have been issued. Id.; see also Doe v. Reivitz, 830 F.2d 1441, 1446-1447 (7th Cir. 1987), Flagstaff Medical Ctr., Inc. v. Sullivan, 773 F. Supp. 1325, 1343-44 (D. Ariz. 1991).
procedures for the issuance of legislative rules, but not for interpretative rules. When Congress enacted the APA, it regarded public participation in the legislative rulemaking process as a counterbalance to the limited judicial review afforded legislative rules, and as a means of preventing agencies from exercising their rulemaking powers unilaterally and arbitrarily.\footnote{Linda Galler, Emerging Standards for Judicial Review of IRS Revenue Rulings, 72 B.U. L. Rev. 841, 863 (1992).} (footnotes omitted)

Finally, the case of Davis v. United States,\footnote{495 U.S. 472 (1990).} which was decided six years after Chevron, casts considerable doubt on the notion that the Chevron standard should apply to revenue rulings. In Davis, the Supreme Court was called upon to decide the weight of an IRS ruling without ever mentioning Chevron. The issue was whether parents of Mormon missionaries could deduct as charitable contributions funds transferred directly to their children when the children served as unpaid missionaries for the church.\footnote{See id. at 473-74.} The IRS had issued a ruling\footnote{See I.T. 1867, II-2 C.B. 155 (1923). The abbreviation "I.T." indicates a pre-1954 ruling issued by the Income Tax Unit or Division of the IRS, and is published in the Internal Revenue Bulletin.; see also Gail L. Richmond, Federal Tax Research, 59-60 (4th ed. 1990). "Because the Treasury Secretary did not formally approve I.T.'s, they neither committed the department or bound the courts." Id.} interpreting Section 170 of the Code, which stated that contributions made "for the use of" meant "in trust for."\footnote{Davis, 495 U.S. at 481-84.} The Court ruled that the payments were not deductible.\footnote{See id. at 488.} With respect to the deference accorded the ruling, the Court stated: "Although the Service's interpretative rulings do not have the force and effect of regulations, ...we give an agency's interpretations and practices considerable weight where they involve the contemporaneous construction of a statute and where they have been in long use."\footnote{Davis, 495 U.S. at 484 (citations omitted).} The Court also noted the revenue ruling has survived the reenactment of the statute that it construed.\footnote{See id. at 483-84.}

The fact that the Court, in Davis, does not refer to Chevron when deciding the weight to be given an administrative interpretation strongly suggests that the Chevron standard does not apply to revenue rulings: "Perhaps the omission of Chevron implies that courts are not bound by interpretive rules that are issued without notice and comment...Application of Chevron to non-notice and comment interpretive rules would require courts to accept these rules absent a showing of unreasonableness, and would effectively elevate these less formal rules to the status of notice and comment rules despite longstanding (pre-Chevron) precedent suggesting that interpretive rules are always nonbinding."\footnote{Galler, supra note 95, at 873-74.}

Since the issue of whether Davis sets a new standard for evaluating the weight of revenue rulings is not within the scope of this paper, it will not be addressed. Suffice it to say, however, that one writer has stated the three factors promulgated in Davis to be used when considering the weight to be given
revenue rulings “are intrinsically weak statutory aids and reliance on these factors is particularly inappropriate and unwarranted with respect to revenue rulings.”

(b) The Tax Court

The Tax Court is “unique in its absolute refusal to yield to IRS revenue ruling positions.” The court regards revenue rulings as nothing more than the IRS’s position with respect to the factual situations and the legal issues presented. It treats such rulings simply as the contention of a litigant. Of course, the court will consider a revenue ruling when arriving at a decision. For example, in Burton v. Commissioner the court stated that “[a]lthough revenue rulings are not binding on this Court, they may be useful in interpreting a statute based on their own intrinsic value.”

(c) The Retroactive Revocation of Revenue Rulings

Prior to concluding, mention should be made of the power of the Service to revoke revenue rulings retroactively. Pursuant to the case of Manhattan General Equipment Co. v. Commissioner and its progeny, the Supreme Court ruled the Commissioner may revoke retroactively or amend erroneous regulations or rulings. In this case the taxpayer relied on a regulation establishing the basis of stock in a reorganization. Subsequently, another regulation was issued which revoked the previous regulation resulting in a substantial reduction of the basis of the shares. In ruling for the Commissioner, the Court stated that the original regulation was invalid because it was “both inconsistent with the statute and unreasonable.” Pointing out that only Congress has the power to make law, the Court concluded the original regulation was a “mere nullity” on which the taxpayer was not entitled to rely. The doctrine of Manhattan General has been applied sometimes even when the taxpayer has acted in reliance on an erroneous regulation or ruling. The doctrine has also been extended to erroneous

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104 Id. at 876.
105 Galler, supra note 6, at 1059.
106 See id.
108 See Galler, supra note 6, at 1059.
110 Id. at 629; see also Pepcol Mfg. Co. v. Commissioner, 98 T.C. 127, 136 n.4 (1993) (stating revenue rulings are entitled to some consideration).
111 297 U.S. 129 (1936).
113 Id. at 133.
114 Id. at 133-34.
115 Id. at 135.
116 Id. at 134.
regulations and rulings that remain outstanding and have not been revoked or amended.\textsuperscript{17}

Finally, recognizing the harsh effects that the Manhattan General rule had on taxpayers over the years, I.R.C. § 7805(b), as amended by the Taxpayer Bill of Rights 2, section 1101(a),\textsuperscript{18} states that Proposed Regulations generally may not apply retroactively to any taxable year ending before they are filed with the Federal Register.\textsuperscript{19} Final regulations generally may not apply retroactively to any taxable year ending before the Proposed Regulations were filed with the Federal Register.\textsuperscript{20} The Ways and Means Committee Subcommittee on Oversight explained the reason for the amendment as follows:

The complexity of the tax regulations and the lengthy period of time it takes the IRS to publish them, creates a significant hardship for taxpayers who seek in good faith to comply with the statutory tax law in the period of time before the regulations are published. If the taxpayer interprets the law in a way which is different from the position taken in a subsequent regulation, the taxpayer may be subject to additional taxes, penalties and interest. The Subcommittee believes taxpayers should have more protections from the retroactive application of regulations.\textsuperscript{21}

C. THE REMEDY

What is one to make of the hodgepodge of court decisions spewing forth differing standards regarding the deference that should be accorded to both private letter and revenue rulings? How much guidance do they really provide? The answer is mixed with uncertainty and ambiguity. First and foremost, it should be understood that irrespective of the wording of the standard, none of them actually remove the discretion of the court to decide as it pleases. A court could give "controlling weight" to a revenue ruling and then decide against the Service. Another court could determine that a private letter ruling is strong evidence of the Service's position and decide for the taxpayer. Yet another court

\textsuperscript{17} See Benjamin J. Cohen & Catherine A. Harrington, \textit{Is the Internal Revenue Service Bound by its Own Regulations and Rulings?}, \textit{51 TAX LAW.} 675 (1998).


\textsuperscript{19} See Cohen & Harrington, \textit{supra} note 117, at 696 (citing I.R.C. § 7805(b)(1)(A)(1994)).

\textsuperscript{20} Id. at 697 (citing I.R.C. § 7805(b)(1)(B)(1994)).

\textsuperscript{21} Cohen & Harrington, \textit{supra} note 117, at 697 (citing U.S. HOUSE OF REPRESENTATIVES WAYS AND MEANS SUBCOMM. ON OVERSIGHT, 104th CONG., 2d Sess., \textit{Explanation of Taxpayer Bill of Rights 2}, (1995)).

\textsuperscript{12} See generally TexasGulf, Inc. v. Commissioner, 172 F.3d 209, 217 (2d Cir. 1999). The Commissioner had denied a foreign tax credit for Ontario Mining Tax (OMT). \textit{Id.} The Commissioner had issued a revenue ruling stating that OMT payments are not royalties and, therefore, may not be excluded from the taxpayer's gross income. \textit{Id.} The court, in deciding for the taxpayer, stated: "While Revenue Rulings are entitled to great deference, (citations omitted), we are not swayed in this instance \textit{because the comment on OMT's creditability is not part of the Revenue Rulings holding and because we read § 1.901-2 (providing for the tax credit) to dictate a contrary conclusion." \textit{Id.} (emphasis added); Internal Revenue Service v. Kaplan, 104 F.3d 589, 599 (3d Cir. 1997). The Court states that "Revenue Rulings are entitled to great deference, but courts may disregard them if they conflict with the statute they purport to interpret or its legislative history, or if they are otherwise unreasonable." \textit{Id.} (emphasis added).
could decide that a ruling was not reasonable and consistent with the statute even though the rule was, in fact, reasonable and consistent. For example, one writer has commented that the three approaches adopted by the district courts “have absolutely no bearing on a courts ultimate decision whether to defer to a revenue ruling. It thus should not be surprising that courts pick and chose among these approaches in justifying their decisions.”

Thus, it seems as if both private letter and revenue rulings are just like any other piece of admissible evidence to which the court refers when making a decision. It is my opinion that both lawyers and taxpayers should treat them as such. “You take your chances.”

To resolve the uncertainty and ambiguity, the Court or the Congress could do one of two things: (1) mandate a uniform standard for both private letter and/or revenue rulings, for example, as stated above, why should not private letter and revenue rulings be considered as just another piece of evidence that informs the court’s decision without regard to considerations of “weight” or deference? (2) prohibit the citation of such rulings in either correspondence to the Service or in court cases. Many United States courts of appeals have instituted noncitation rules with respect to their unpublished opinions.

The Ninth Circuit Rule 21(c) states: “A disposition which is not for publication shall not be regarded as precedent and shall not be cited to or by this court or any district court of the Ninth Circuit, either in briefs, oral argument, opinions memoranda, or orders.” (emphasis added). Only in this way will some consistency and predictability be infused into the process resulting in rulings that both taxpayers and their lawyers can take to the bank.

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124 See Galler, supra note 6, at 1094 (stating “I believe the issue of [the varying standards of] deference is best resolved by the Supreme Court. The plethora of diverse and conflicting approaches followed by the lower courts suggests a need for higher court resolution.”).
125 See Holden & Novey, supra note 8, at 345.
126 Holden & Novey, supra note 8, at 345-46.
PHYSICIANS VERSUS MANAGED CARE: 
IS IT TIME FOR PHYSICIAN UNIONS?
by E. Douglas Baldridge, Jr., M.D., FACS

I. INTRODUCTION

Antitrust analysis . . . requires a search for understanding of markets, an understanding that, experience shows, may be founded on elements that lie well below the surface of what even those in a particular industry may readily comprehend . . . . When neither the parties nor the [Federal Trade] Commission fully comprehends the justifications, "ignorance leads straight to condemnation," Chicago Professional Sports Limited Partnership v. NBA, 961 F.2d 667, 676 (7th Cir. 1992), and condemnation without understanding may lead to consumer harm . . . . [I]t is well . . . to keep in mind the admonition of the court in Chicago Professional Sports Limited Partnership . . . that "explanations of problematic conduct take time to develop and more time to test . . . . Understanding novel practices may require years of study and debate."

The rising number of physician unions within a markedly changing health care industry is exactly such a novel issue. Lest physician unions be condemned out of ignorance with the end result of consumer harm, antitrust enforcement agencies and courts must look for "elements that lie well below the surface." Physician unions must not be condemned as per se illegal in a conclusory manner. The changing climate of antitrust policy is favorable for evaluation of physician unions under a rule of reason. In some cases physician unions may be procompetitive, even within the existing antitrust case law. Furthermore, good arguments exist for allowing physicians to collectively bargain, based on well-founded legal principles outside the antitrust arena. Finally, social and economic conditions are ripe for permitting collective bargaining by physicians, especially in light of a complex, changing health care industry.

Although the origin of physician unions may be traced to housestaff organizations in the 1930s, the first physician union of independent physicians occurred in 1972 through the organization of the Union of American Physicians

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1 E. Douglas Baldridge, Jr., M.D., FACS is a surgeon in private practice in Northern Kentucky. He is board-certified in general surgery, vascular surgery, and critical care. B.A., Transylvania University, M.D. University of Kentucky. He is also a student in the part-time program at Northern Kentucky University, Salmon P. Chase College of Law.


3 Id.

and Dentists in California by Dr. Sanford Marcus. By 1975, there were twenty-six physician unions in the United States, with 16,000 members. Authors suggested the increase in number of physician unions and physician membership was due to crises of the 1970s and as the crises in medicine resolved, the trend toward unionization decreased. In the 1980s and 1990s, in response to managed care, the number of unionized physicians has again increased to approximately 700,000 of which about half are housestaff.

The Union of American Physicians and Dentists, with about 5,000 members, merged with the American Federation of State, County, and Municipal Employees representing 3,000 physicians and over 350,000 healthcare workers. The Federation of Physicians and Dentists, based in Florida, represents 7,500 physicians who are largely in private practice. The Doctor’s Council represents 3,400 physicians employed in New York City. The Physicians Healthcare Networks Group has 1,300 members in Naples, Florida. The Professional Employees International Union represents 12,000 podiatrists and 2,100 physicians. One thousand New Jersey physicians have joined the International Association of Machinists and Aerospace Workers. Nationwide, physician unions have grown by 250% over the past three years. Despite the growth of physician unions, their value (or lack of value) has been the topic of academic debate.

The purpose of the present article is to advocate that physicians, on behalf of themselves and their patients, be allowed to collectively bargain with insurers and other payors. In order to understand the rationale for collective bargaining by physicians, one must first appreciate the paradigm shift from traditional indemnity health care insurance to managed care that has occurred over the past

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5 See Ellen L. Luepke, White Coat, Blue Collar: Physician Unionization and Managed Care, 8 ANNALS HEALTH L. 275, 279 (1999) [hereinafter Luepke, White Coat].
6 Id.
7 In 1974, 55,000 physicians were members of unions in response to perceived crises of: (1) medical malpractice; (2) increased governmental regulations, and (3) threat of national health insurance. See Robert L. Lowes, Strength In Numbers: Could Doctor Unions Really be the Answer?, MED. ECON. - GEN. SURGERY ED. (July/Aug. 1998) at 42, 45 [hereinafter Lowes, Strength In Numbers].
8 See Luepke, White Coat, supra note 5, at 279.
9 Id. at 280.
10 Id. at 281.
11 Id.
12 See Lowes, Strength In Numbers, supra note 7, at 45.
13 See Luepke, White Coat, supra note 5, at 282.
14 Id.
15 See Lowes, Strength In Numbers, supra note 7, at 48.
16 See Tanya Albert, More Doctors Following Trend to Unionize, AM. MED. NEWS, Nov. 27, 2000, at 1 [hereinafter Albert, More Doctors].
With the ongoing, dynamic evolution of managed care, physicians have found themselves trapped between their traditional role as patient advocates and their new role as business managers trying to control rising costs in order to make a profit. Single physicians, small groups, and even large multispecialty groups have been powerless to individually negotiate with ever-growing, powerful third party payors who control delivery of health care and even access of physicians to patients and/or patients to physicians. Collective bargaining is one way to remedy the difference in power between physicians and insurers. Despite the need to collectively bargain, physicians have been straight-jacketed by antitrust law. Antitrust law traditionally precludes price-fixing, boycotts, and various other concerted activities. Therefore, antitrust law is an inherent threat to any collective bargaining agreement between physicians.

The author advocates change in antitrust policy to analyze any physician collective bargaining on a rule of reason basis rather than find such relationships per se illegal under the guise of price-fixing, boycotts, or other horizontal agreement. Significant societal benefits can be realized by permitting physicians to collectively bargain and equity requires that physicians not be relegated to accept contracts that they are powerless to negotiate, yet force them to maintain their traditional role as patient advocates. The solution requires that physician unions be recognized as an exemption to the antitrust laws like any other employee union.

This article will first examine the changing aspects of health care with comparison of traditional indemnity plans to managed care and, particularly, focus on current issues. Next, an overview of pertinent traditional antitrust law is compared to changing enforcement policy as stated in the 1996 Statements of Antitrust Enforcement Policy in Health Care. Finally, four reasons exist to

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18 See George W. Whetsell, The History and Evolution of Hospital Payment Systems: How Did We Get Here?, NURSING ADMIN. Q. (Summer 1999) at 1,1 [hereinafter Whetsell, History and Evolution].


20 See Tanya Albert, Collective Bargaining Bill Dies; Supporters Vow To Try Again, AM. MED. NEWS, Nov. 6, 2000, at 1 [hereinafter Albert, Bargaining Bill Dies].

21 See generally J. James Rohack, M.D., HMOs Don't Have To File Antitrust Lawsuits When FTC Does It For Them, AM. MED. NEWS, Oct. 23/30, 2000, at 20 (stating that managed care organizations rarely take private action against a provider group); Leigh Page, HMO Sues Group for Antitrust Violations, AM. MED. NEWS, Oct. 2, 2000, at 22 [hereinafter Page, HMO Sues].


23 Grace Budrys, PhD, a professor of sociology at DePaul University in Chicago and author of the book When Doctors Join Unions, during an address to the 86th Congress of the American College of Surgeons, stated doctors must choose between being governed by antitrust law or labor law. See Frangou, Doctors' Unions, supra note 19, at 1.

justify a change in antitrust policy to allow collective bargaining by physicians: (1) contract principles mandate equality of bargaining power between physicians and insurers; (2) physicians should be treated as employees under the National Labor Relations Act and should be given collective bargaining rights; (3) physician unions, analyzed under a rule of reason, can be procompetitive; and (4) principles of equity, in light of socio-economic changes precipitated by managed care, should be followed.

II. CHANGING ASPECTS OF HEALTH CARE

An understanding of the present health care system and the trends in its development is necessary in order to put physician unions and antitrust issues in their proper perspective. One can understand the rationale of permitting physicians to bargain collectively only if one understands the unique, complex health care delivery system and its effects on both physicians and consumers. Many physicians have become frustrated with the present managed care system and, increasingly, consumers are also becoming frustrated. Legislative and governmental response has been largely ineffective in solving many of the current issues. Physician unions represent a tool for dealing with many of these frustrations and current issues; however, traditional antitrust law is a barrier to the effectiveness of such physician unions.

In order to understand the rationale for permitting collective bargaining by physicians, one must appreciate the historical development of managed care, the current issues, and the failure of current methods to deal with these problems. The following discussion will focus on comparison of traditional fee-for-service medical care and managed care, definition of important terms, current issues, and responses of various market participants to the ongoing problems.

A. Health Care Under Traditional “Fee for Service”

The traditional method of health care delivery and payment was the fee for service system, whereby an individual, either independently or through an employer, paid premiums to an insurer, i.e., a third-party payor. When the need arose, the individual went to his choice of physicians for testing and treatment. The patient presented his insurance information and the physician submitted a bill to the third-party payor and was paid. Such indemnity plans often involved payment of a deductible and, probably, a percentage of the bill by the individual.

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26 See Frangou, Doctors’ Unions, supra note 19, at 1. See also Roderick T. Beaman D.O., Medicine Now Just a Job; We’re All Just Cogs in the Machine, AM. MED. NEWS, Nov. 20, 2000, at 18.
28 See Frangou, Doctors’ Unions, supra note 19, at 1.
29 See Whetsell, History and Evolution, supra note 18, at 1.
30 Id.
31 Id.
Physicians versus Managed Care

Insurers then began to contract with providers, i.e., physicians and hospitals for the providers' services. Based on a particular service, insurers paid the providers a certain set fee for the particular service. With experience over time, the insurers were able to average the fees paid for a particular service and each service was tied to a "usual, customary, and reasonable" ("UCR") fee. In some cases, the insurers might request this UCR information directly from providers. Thus, the insurers could develop a UCR fee schedule for each provider and for each procedure.

In the interest of minimizing costs and maximizing profits, insurers preferred to contract with providers for discounted fees. Contracted providers were then described as being on the insurer's provider panel. Typically, physicians were paid either a percentage of the UCR or the actual fee they charged, whichever was lower.

B. Managed Care

1. Definition

A single definition of managed care is difficult due to the evolution of health care products over time. In the 1970s, managed care predominantly meant health maintenance organizations ("HMOs"). A decade later health insurers created preferred provider organizations, ("PPOs"), typically with narrowly-defined provider panels. Today, managed care includes a variety of health care delivery systems unimagined in the 1970s. A definition of managed care might also vary by the goals of the market participants: Managed care might mean

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32 Id.
33 See Chris Cameron et al., Assessing Capitation, Financial Opportunities and Risk 1 (Ohio State Medical Association 1995) [hereinafter Cameron, Assessing Capitation].
34 Id. See also J. Harper Gaston, M.D. et al., Managing Managed Care In The Medical Practice 17 (Kay Stanley, American Medical Association 1996) [hereinafter Gaston, Managing Managed Care].
35 The consent decree was modified in United States v. Vision Service Plan to permit the defendant to use the UCR fee information obtained from its provider panel doctors to calculate its own payment fees. See Vision Service Plan, 61 Fed. Reg. 9487, 9488 (1996) (public comment). UCR in that case was defined as "the fees for services and materials that are charged before any discounting, by VSP panel doctors to their private patients (patients not covered by Medicare or Medicaid programs)." Vision Service Plan, 60 Fed. Reg. 57017, 57018-57019 (1995) (revised final judgment and revised competitive impact statement).
36 See Chris Bostick, JD, OSMA et al., What Is Managed Care? 38 (Ohio State Medical Association 1995) [hereinafter Bostick, What Is Managed Care?].
37 See Cameron, Assessing Capitation, supra note 33, at 1.
38 See Court to Health Plan: Say How You Pay, AM. MED. NEWS, Aug. 7, 2000, at 23 [hereinafter Court to Health Plan].
39 See Gaston, Managing Managed Care, supra note 34, at 1.
40 See Bostick, What Is Managed Care? supra note 36, at 3.
41 Id.
42 E.g., IPAs, PHOs, MSOs, ASOs, PPOs, multiprovider networks, physician network joint ventures, etc.
management of a delivery system of health care, or management of health care costs, or exerting control of the delivery system.

In general, managed care is "a type of health care financing and delivery that seeks to contain costs through using administrative procedures and granting financial incentives to providers and patients." The definition incorporates the concepts of management of services, monitoring of use and quality of health care delivery, and cost containment.

2. Analysis of "Alphabet Soup"

The development of managed care products bred a host of acronyms. Understanding the acronyms is useful for a couple of reasons. First, several acronyms represent insurance products or groupings of providers that will be encountered in antitrust law within the realm of health care. For example, one must realize that insurance products differ when defining a relevant market. Managed care includes a variety of products that are distinct and not interchangeable from the consumer's perspective. Such differences may be important in evaluation of the antitrust implications of a merger of insurance companies. Another example is that independent physician associations

43 "[M]anaged care is defined as follows: A means of providing health care services within a defined network of health care providers who are given the responsibility to manage and provide high quality, cost-effective health care to a defined population." GASTON, MANAGING MANAGED CARE, supra note 34, at 1 (citing DAVID E. VOGEL, THE PHYSICIAN AND MANAGED CARE (American Medical Association 1993)).

44 The National Association of Children's Hospitals has defined managed care as: "An attempt to contain health care costs by controlling how and where patients obtain health care services. Any health insurance or health financing control mechanism or financial inducement intended to direct or restrict the patient's choice of provider or the patient/physician's choice of treatment modality." GASTON, MANAGING MANAGED CARE, supra note 34, at 1.

45 The American Society of Internal Medicine (ASIM) defines managed care as: "A system of health care delivery through contracted providers in which the entities responsible for financing the cost of health care exert influence on the clinical decision-making of those who provide health care in an attempt to provide health care which is cost-effective, accessible, and or acceptable quality." GASTON, MANAGING MANAGED CARE, supra note 34, at 1 (emphasis added).


48 Such acronyms include AHPs (accountable health plans), ACP (accredited capitated provider), ASO (administrative services only), CQI (continuous quality improvement), EOB (explanation of benefits), HMO (health maintenance organization), IDS (integrated delivery system), IPA (independent practice association; aka independent physicians association), IPN (integrated provider network), MCO (managed care organization), MSO (management services organization), MLP (mid-level practitioner), PRO (peer review organization), POS (point-of-service organization), PPO (preferred provider organization), RBRVS (resource-based relative value scale), TPA (third-party administrator), TQM (total quality management), and PHO (physician-hospital organization). See BOSTICK, WHAT IS MANAGED CARE?, supra note 36, at 10.


50 Id.

51 Id.
("IPAs") and physician-hospital organizations ("PHOs") are frequently parties in health care antitrust litigation, because such associations of independent physicians or physician-hospitals create issues of unlawful agreements to restrain trade.\textsuperscript{52}

Understanding the differences between insurance products may also provide insight into current problems with managed care.\textsuperscript{53} Managed care began with HMOs (health maintenance organizations) that were of two varieties: staff model HMOs or group model HMOs.\textsuperscript{54} Staff model HMOs typically use salaried physicians who are employed by the HMO,\textsuperscript{55} whereas group model HMOs are typically independent physicians who function as a multi-specialty group or who are independently contracted to provide services for an HMO product.\textsuperscript{56} Managed care later included products such as PPOs (preferred provider organizations) and PSOs (point of service organizations).\textsuperscript{57} Some products are hybrids of these three basic types of plans.\textsuperscript{58} These three products differ in aspects of access to physicians and relative cost of the products:

[H]MO and HMO-POS products differ from PPO or indemnity plans in terms of benefit design, cost, and other factors. . . . For example, HMOs provide superior preventive care benefits, but they place limits on treatment options and generally require use of a primary care physician "gatekeeper." PPO plans, which do not require enrollees to go through a "gatekeeper" and do not emphasize preventive care, are generally more expensive than HMOs. POS plans can be based on either an HMO or PPO network and fall between HMO and PPO plans in terms of access and cost. That is, POS plans offer patients more flexibility at a higher cost relative to HMOs. In general, then, PPOs and indemnity options are more expensive, provide better benefits with respect to coverage when ill, and allow greater access to providers. In contrast, HMO and HMO-based POS options are generally less expensive, provide better benefits with respect to health


\textsuperscript{53} See Carol Wright Mullinax et al., OSMA Special Report: Managed-Care and You 10 (Ohio State Medical Association 1995) [hereinafter \textit{Mullinax, OSMA Special Report}]. A brief but adequate comparison of the different characteristics of fee-for-service and various models of managed care systems is provided. \textit{Id.}

\textsuperscript{54} See Bostick, What Is Managed Care? \textit{supra} note 36, at 10.

\textsuperscript{55} Physicians employed by a staff model HMO may bargain collectively, whereas those in a group model HMO are not considered employees for purpose of collective bargaining.

\textsuperscript{56} See Bostick, What Is Managed Care, \textit{supra} note 36, at 10.

\textsuperscript{57} See Mullinax, OSMA Special Report, \textit{supra} note 53, at 10.

maintenance or preventive [sic] care, place greater limits on treatment, and restrict access to providers. 59

One must also understand that through various agreements, providers may function as preferred providers and/or as an HMO, providing services to insurers or directly to employers. 60 Such provider groups include IPAs (independent physician associations) 61 or PHOs (physician-hospital organizations) 62 that associate in order to contract with insurers or employers for services of the association. Such group ventures have become an integral part of managed care and frequently run afoul of antitrust law because such organizations represent a cooperative effort among otherwise competing providers. Additional acronyms used within this article will be defined at the appropriate point.

3. Development and Expansion of Managed Care

Prior to the 1970s the traditional fee-for-service, third-party payor system was the overwhelming, dominant health care system. 63 By mid-1988 there were 700 PPOs covering 42 million lives and accounted for 13%-15% of physicians’ gross income. 64 In mid-1989 there were 590 HMOs covering an additional 33 million lives and accounting for 9%-12% of physicians’ gross income. 65 The trend was toward a higher concentration of these managed care products in larger groups of physicians. 66

By 1996, 20% of the U.S. population was covered by an HMO (health maintenance organization), but an HMO is only one type of managed care product. 67 In 1996, 63 percent of employees who were covered by a health care plan were enrolled in an HMO or some other form of managed care. 68 The number of patients enrolled in HMOs grew from a little over five million in 1980 to almost forty million in 1994. 69 The proportion of managed care in the form of HMOs and, particularly, PPOs has continued to rise. 70

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59 Id.
60 See, e.g., Bostick, What is Managed Care?, supra note 36.
61 See Gaston, Managing Managed Care, supra note 34, at 9-10.
62 Id. at 11.
63 See Whetsell, The History and Evolution, supra note 18, at 1.
64 See James Norman, The Flowering of Managed Care, MED. ECON. GEN. SURGERY ED., Apr. 1990, at 23, 23 [hereinafter Norman, The Flowering].
65 Id.
66 Id.
67 See Gaston, Managing Managed Care, supra note 34, at 2.
68 Id.
69 Id.
4. Rationale for Change from Traditional “Fee for Service” to Managed Care

Under a traditional fee for service plan, consumers had freedom of choice of providers. The distribution of financial risk depended upon one’s perspective. On one hand, financial risk was entirely upon the insurers who paid the bills. Insurers had to compete with one another in price for the consumers’ business while having no control over costs of health care delivery. The providers had the best deal since they were paid as long as they provided the services. They also had “control” over the costs in the system, i.e., testing and treatment and their own charges. Consumers, i.e. patients and their employers, had little risk – only to the extent of deductibles and a fixed percentage of costs.

On the other side of the argument is the view that insurers were not at risk because they simply increased the premiums to cover any rise in costs. Insurers only had to compete with one another for the consumers’ business. Consumers were the ones at risk because of the rising premiums. Providers assumed essentially no risk for the rising costs, since under a fee for service, they were paid as long as they provided the services. Providers’ major risk was from competition with other similar providers who competed for the same consumers or insurance contracts.

Regardless of one’s viewpoint, the rising costs of health care in the 1960s and 1970s resulted in generalized concern, and perhaps disgruntlement, on the part of many participants in the health care system. With the overall purpose of containing health care costs, and perhaps a desire by some groups to redistribute the perceived financial risk of health care, the concept of managed care was born.

C. Current Issues

Controversies currently exist in the health care arena. Whether the effects of managed care are good or bad depends on one’s perspective. Complexities of

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71 See Mullinax, OSMA Special Report, supra note 53, at 10.
72 For information concerning the shifting of financial risk under various managed care products, see, e.g., Cameron, Assessing Capitation, supra note 33.
73 Id.
74 Id.
75 Id.
76 See generally Paul M. Ellwood Jr., M.D. & George D. Lundberg, M.D., Managed Care - A Work in Progress, 276 J. AM. MED. Ass'n 1083 (2000) [hereinafter Ellwood, Managed Care - A Work in Progress].
77 See Cameron, Assessing Capitation, supra note 33.
78 Id.
79 See Whetsell, History and Evolution, supra note 18, at 1.
80 See Gaston, Managing Managed Care, supra note 34, at 1-2.
81 One example of a current issue is who should be liable for medical decisions and bad outcomes – physicians, medical directors, or insurers? The role of federal preemption due to ERISA-covered insurance plans is one issue that affects such liability issue. See generally Mary Chris Jaklevic, Texas Ruling Another Victory for HMOs, Modern Healthcare, Sept. 2000, at 24, 24 [hereinafter Jaklevic, Texas Ruling] (regulatory reach of state medical board that found health plan medical
health care are important to understand because antitrust laws must be applied within the framework of the unique nature of health care. Antitrust policy should be responsive to social changes since the consumer is the ultimate beneficiary of antitrust law. From the consumer’s perspective, physician unions can have a positive effect by maximizing the beneficial aspects of managed care and minimizing the deleterious effects. To decide whether current antitrust policy regarding physician unions should be changed, one must appreciate the effects of present managed care on both the physicians and the consumers. Any change must be equitable to physicians and beneficial to consumers.

1. Costs

Despite managed care’s goal of cost containment, costs of medical care remain high. Reasons include high malpractice costs and new, complex technology.

a. Malpractice Costs

Recent trends in medical malpractice are attributable directly or indirectly to managed care i.e.: (1) median jury rewards have risen dramatically; and, (2) there has been a shift from procedural-type inpatient cases to diagnostic, outpatient cases. This second trend may be due, in part, to increased volume and complexity of outpatient procedures as well as patients having to deal with multiple physicians rather than an individual doctor. More complex procedures

director was engaged in the practice of medicine through insurer’s denial of benefits was preempted by ERISA); Joan R. Rose, If At First You Don’t Succeed... , MED ECON., Oct. 2000, at 11, 11 (Connecticut attorney general failed in action against insurers due lack of state standing to bring suit against the ERISA-covered plan); Peter D. Jacobson, The Supreme Court's View of the Managed Care Industry's Liability for Adverse Patient Outcomes, 26 J. AM. MED. ASSN 1516 (2000) (letter to the editor describing the implications of a Supreme Court decision, Peagram v. Herdich, 530 U.S. 211 (2000), that patients covered by an ERISA plan cannot sue on the basis of a managed care plans' use of financial incentives for providers). Other cases have found HMOs liable under the HMO Act of 1973. See Tanya Albert, New York Court Backs Physician’s Judgment Over HMO Rule, AM. MED. NEWS, Nov. 6, 2000, at 13. HMOs have also been held liable on a theory of institutional negligence at the state level. See Miles J. Zaremski, Illinois Court Hits HMO for Institutional Negligence, AM. MED. NEWS, Jul. 10, 2000, at 11. (The case referred to in the article was Jones v. Chicago HMO, 730 N.E.2d 1119 (Ill.2000)). Still another litigated theory of liability was racketeering. See Mixed Decisions in Two Aetna Lawsuits, AM. MED. NEWS, Sep. 4, 2000, at 29. Another legal issue is whether managed care issues should be addressed under a theory of contract law or a theory of tort. One alternative theory is fiduciary responsibility. See Peter D. Jacobson & Michael T. Cahill, Applying Fiduciary Responsibilities in the Managed Care Context, 26 AM. J.L. & MED. 155 (2000).


83 See Linda O. Prager, Malpractice Perils Mounting, AM. MED. NEWS, Aug. 7, 2000, at 10 [hereinafter Prager, Malpractice Perils Mounting].

84 Id.
are being done on an outpatient basis in an effort to contain costs. When procedures fail or diagnoses are missed, patients are less tolerant of complications, especially when they feel like victims of the system. By interference with the traditional doctor-patient relationship managed care results in higher malpractice awards and higher malpractice premiums.

b. New Technology

Expensive technological developments have revolutionized patient treatment: laparoscopic surgical procedures, laser treatments, coronary and peripheral angioplasty, endovascular stents, and, more recently, endovascular “stent-grafts” are examples. Research and development are major components of the ever-escalating costs of technology as well as pharmaceutical costs of newer and better drugs. As a byproduct of technological development, the trend is toward development of new specialties and concomitant changes in accreditation. In addition to the direct costs associated with certification examinations, specialists expect to be compensated for additional investment in time and expense of specialty training. On the other hand, managed care insurers increasingly require board certification and re-certification for physicians to participate in managed care products. Such requirements may have devastating

85 The hospital admission rate fell from 159 per 1,000 population in 1980 to 118 per 1,000 in 1997; whereas, the outpatient visits per 1,000 population increased from 890 in 1980 to 1,682 in 1997. See STATISTICAL ABSTRACT, supra note 82, at 137.
86 See Prager, Malpractice Perils Mounting, supra note 83, at 10.
87 These procedures are examples of minimally invasive surgery that have become routine in the author’s own practice and field of general and vascular surgery over the past ten to fifteen years. Such minimally invasive techniques result in significant reduction in patient discomfort and savings in hospitalization; however, cost savings are largely offset or exceeded by the expensive equipment required to perform such minimally invasive procedures.
88 The expenditures for medical research rose from $5.5 billion in 1980 to $18 billion in 1997. See STATISTICAL ABSTRACT, supra note 82, at 118.
89 See Prescription Drugs Largely to Blame for Health Care Cost Increase, AM. MED. NEWS, Nov. 27, 2000, at 7. See also Jane Cys, Price Relief Coming? Congress Passes Drug Importation Bill, AM. MED. NEWS, Nov. 6, 2000, at 5; Jane Cys, Rising Care, Drug Costs Trigger Hikes in Medigap Premiums, AM. MED. NEWS, Sep. 18, 2000, at 5 [hereinafter Cys, Rising Care].
90 See Fred G. Donini-Lenhoff & Hannah L. Hedrick, Growth of Specialization in Graduate Medical Education, 284 J. AM. MED. Ass’n 1284 (2000). See also G. Patrick Clagett, M.D. et. al., The Vascular Surgery Sub-board: Progress Report, 31 J. OF VASCULAR SURGERY 1060 (2000). The driving force for such specialization includes the growth of knowledge from research, new technology, and desire of physicians for expertise. See Jeremiah A. Barondess, Specialization and the Physician Workforce - Drivers and Determinants, 284 J. AM. MED. Ass’n 1299 (2000).
91 Despite the expectation of increased compensation, the trend in recent years has been to shift payments to primary care specialists and away from surgical specialists, at least in terms of Medicare reimbursement through the Resource Based Relative Value Score (RBRVS) system. RBRVS is a scale that measures the relative value of a medical service or intervention, based on the amount of physician resources involved. See generally Howard Isenstein, The Medicare Fault Line: Government Efforts to Keep Soaring Payment Rates Under Control Puts Specialists and Generalists at Odds, 40 MODERN PHYSICIAN 813 (2000).
consequences for physicians who fail re-certification examinations or for the 15% to 20% of licensed physicians who are ineligible to take board examinations due to failure to complete a residency or because they are foreign medical graduates. Some managed care insurers use such qualifications of their panel physicians as a marketing tool. The overall effect is that physicians must continually learn new skills, maintain certification in order to participate in managed care products, and work in an environment of technically demanding, complex outpatient treatment of patients with whom they have little contact and little chance to develop a traditional physician-patient relationship - all for the sake of cost containment and efficiency as paramount goals of managed care.

2. Effects of High Costs

Continued high costs of health care has resulted in several changes. In an effort to contain costs, health care services are increasingly provided by non-physicians. High costs and low profit margins have resulted in many physician groups failing financially, as exemplified by recent unsuccessful attempts to market managed care products in the Medicare patient population. Also, insurers have developed products that limit consumers' choice of providers. Another effect is that health care insurance has become a new investment market for capitalists. Savings at the level of delivery, for example, the patient-provider level, is often passed on as profit to the investors. Finally, high costs

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93 Id.
94 Id.
95 "When corporations and company doctors strip away patient particulars, when they quantify away the nuances of a disease, when they rationalize away patient needs as just matters of economics, they vitiate a 3,000-year tradition of patient-focused medicine. For this they should be held accountable, not only for the harm done to particular individuals, but for the harm done to the profession and the practice of medicine as a whole." Linda Peeno, Plain and Simple: Denying Payment Denies Care, 77 MED. ECON. 213, 221 (2000) [hereinafter Peeno, Plain and Simple].
96 See Jay Greene, Physician Extenders in Greater Demand, AM. MED. NEWS, Jul. 24, 2000, at 11 [hereinafter Greene, Physician Extenders].
97 For example, in California thirteen IPAs have failed financially in the past five months. See Leigh Page, California Doctors Have Had It with IPAs, AM. MED. NEWS, Nov. 27, 2000, at 14 [hereinafter Page, California Doctors].
98 See generally Linda Boone Hunt, Hurting in the Heartland (Loss of Medicare Managed Care Providers in Rural Communities), 4 MODERN PHYSICIAN 68 (2000) [hereinafter Hunt, Hurting in the Heartland] (32% of all rural Medicare beneficiaries will be dropped by their managed care plans).
99 The range of products typically include: (1) fee-for-service or self-pay where patients have freedom to choose their providers; (2) point-of-service-plans where they pay more if they go out of the provider network; (3) preferred provider organizations where patients must choose one of usually several designated providers; and (4) HMOs where the patient may have little, if any, choice. The amount of choice ranges along that continuum, depending on the type of plan, the number of providers, etc.
100 See MULLINAX, OSMA SPECIAL REPORT, supra note 53, at 19. See also Cheryl Jackson, Biggest HMOs Reap Strong Profits, AM. MED. NEWS, Nov. 20, 2000, at 16 [hereinafter Jackson, Biggest HMOs].
101 See Jackson, Biggest HMOs, supra note 100, at 16.
of health care have resulted in breakdown of the patient-physician relationship in terms of price elasticity – patients are now more willing to change physicians rather than incur higher out-of-pocket expenses.

a. Non-Physician Health Care Providers

The use of physician extenders such as physician assistants and nurse practitioners has increased, especially in plans that reimburse for their services. On the other hand, many insurers will not reimburse for services provided by physician extenders. Physicians may not recoup the costs of using physician extenders. Efficiency of health care delivery may be maximized by use of physician extenders, but the burden of cost of such personnel should not be borne solely by the physicians.

b. Managed Care Replaces Traditional Medicare

In 1985, the Health Care Financing Administration, (HCFA), initiated HMO for Medicare beneficiaries. The number of HMO-Medicare products grew from 154 in 1985 to 426 in 1998. Following a shift of millions of elderly to the managed care products, recently several of the Medicare-managed care insurers have dropped out of the market, citing "inadequate payments and excessive regulatory burdens as their reasons for withdrawal." As a result of costs of care, many managed care provider groups fail when they assume financial risk through participation in discounted plans or, especially, capitated plans. Delay of payments by insurers to providers has also contributed to the failure of many medical practices. Many of these

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102 See Greene, Physician Extenders, supra note 96, at 11. See also Jay Greene, Mississippi to License Physician Assistants, AM. MED. NEWS, Aug. 28, 2000, at 12.
103 The author has used a physician assistant for the past eight years. Although reimbursements have increased over time, many insurers still do not cover any services provided by a non-physician.
104 See Greene, Physician Extenders, supra note 96, at 11.
105 One example of state legislative relief was the passage of legislation in 2000 requiring insurers to reimburse for services of certified surgical assistants. See Frederick P. Franko, 2000-2001 Legislative and Regulatory Update, AORN J., Dec. 1, 2000, at 2000 WL 26408276.
106 See Whetsell, History and Evolution, supra note 18, at 1.
107 Id.
108 See Susan J. Landers, Medicare Managed Care Plans Drop Seniors - Again, AM. MED. NEWS, Jul. 24, 2000, at 8 [hereinafter Landers, Medicare Managed Care Plans Drop Seniors]. See also Hunt, Hurting in the Heartland, supra note 98, at 68.
109 The California Medical Ass'n estimates that 80% of California IPAs are in serious financial trouble and fail at a rate of one every two to three weeks. See Leigh Page, Doctor Discovers Capitation Being Lost in Costly HMO Limbo, AM. MED. NEWS, Oct. 9, 2000, at 20 [hereinafter Page, Doctor Discovers Capitation].
110 See Cheryl Jackson, Health Plans Under Payment Pressure as States Get Tough, AM. MED. NEWS, Oct. 9, 2000, at 24 [hereinafter Jackson, Health Plans Under Payment Pressure].
problems can readily be addressed through enhanced negotiations with insurers by physician unions.\textsuperscript{111}

c. New Market for Investors

During the 1990s, health care became an investment market on two levels: (1) hospitals invested in purchasing medical group practices; and, (2) stock market investors invested in health insurance corporations. Although their reasons for investment were different, the financial success of both groups was limited. Managed care's goals of efficiency and cost containment are inherently incongruent with an investor's goal of profit. Once maximum efficiency is attained, the only way one can achieve profit is by increasing price.\textsuperscript{112} In effect, investment in health care for profit causes an increase in overall price.\textsuperscript{113}

On the first level, in order to try to control patients and insure a steady market, hospitals in the 1990s invested in purchasing physicians' practices, mainly primary care practices on the theory that the primary care doctors "controlled" the patients.\textsuperscript{114} This trend is now reversing as hospitals are selling the practices back to physician groups, usually at a hefty loss.\textsuperscript{115}

On the second level, stock investors invested in the health care insurance companies in order to make a profit.\textsuperscript{116} In order to perform well for stock investors, major managed care organizations have attempted to control costs and have increased prices to consumers: "Stocks of HMOs, in particular, have soared 36\% this year, far outpacing the broader market, fueled by premium-rate increases that, at least in the short run, appear to offset the rising medical-care costs that caused many investors to ditch HMOs in the last two years."\textsuperscript{117} To make a profit, HMOs had to increase prices, i.e. premiums, because they could not further control medical costs.\textsuperscript{118} Analysts predicted lower earnings based on creeping medical costs due to less favorable Medicare pricing, heightened competition, aging population, and high drug costs.\textsuperscript{119}

\begin{footnotesize}
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\item[111] E.g., even if doctors continue to be financially at risk, through capitation or other similar arrangements, by negotiation through physician unions they may gain access to information possessed by insurers, such as actuarial data on the covered patient population, that may improve chances of IPAs being financially successful.
\item[112] See Jackson, Biggest HMOs, supra note 100, at 16.
\item[113] Id.
\item[114] For example, "Several hospitals statewide [in Ohio] have begun purchasing physician practices to assure their primary and specialty care referral base. . . . Physician practice acquisition is not limited to hospitals. For example, Blue Cross/Blue Shield of Ohio has been attempting in recent months to buy practices in Toledo and other markets. And Paragon (a firm that began as an emergency care network in Florida) has been acquiring primary care physicians' practices in Ohio." MULLINAX, OSMA SPECIAL REPORT, supra note 53, at 19.
\item[115] See Julie A. Jacob, Physicians Buying Back their Practices, AM. MED. NEWS, Aug. 21, 2000, at 1.
\item[116] See Jackson, Biggest HMOs, supra note 100, at 16.
\item[117] Leslie Scism & Rhonda L. Rundle, Health-Care Stocks Regain Their Health, WALL STREET J., May 6, 1998, at C1 [hereinafter Scism, Health Care Stocks Regain Their Health].
\item[118] Id. See also Cys, Rising Care, supra note 89, at 5.
\item[119] See Scism, Health Care Stocks Regain Their Health, supra note 117, at C1-C2.
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d. Effects on an Inelastic “Product”

Once individuals find a physician and embark upon treatment, they generally prefer to continue that patient-physician relationship. In the past, those individuals have been willing to pay higher fees out-of-pocket, rather than change physicians. Demand for the “product” can, thus, be described as price-inelastic. Short-term proof is provided by the success of point-of-service (“POS”) plans whereby patients are required to pay higher deductibles, co-payments, and/or premiums for the privilege of choosing or remaining with physicians not on the preferred panel of providers. Over time, however, there has generally been a shift away from such plans, perhaps because of the higher aggregate costs to the patients. “[T]he elasticity of demand for HMO and HMO-POS plans is sufficiently low that a small but significant price increase for all HMO and HMO-POS plans would be profitable because consumers would not shift to PPO and indemnity plans in sufficient numbers to render such an increase unprofitable.”

Another effect is the widespread political pressure to develop regulations to insure patient choice of physicians, portability of insurance, and overall continuity of care. Although patients want to keep their own physicians, they are less and less willing to pay higher out-of-pocket expenses. Demand for health care is, thus, becoming more price-elastic.

3. Control of Delivery of Health Care and Control of Resources

Managed care has interfered with the traditional physician-patient relationship in several ways. One effect is a loss of patients’ choice of physicians. Patients must go to physicians on their insurance’s panel of providers. Another effect of managed care is loss of physicians’ power to use diagnostic tests and to decide treatment. Utilization review and policy

120 See Ellwood, Managed Care - A Work in Progress, supra note 76, at 1083.
121 Id.
122 “Elasticity of demand is a numerical measure of how responsive demand is to changes in price. It is calculated by the percentage change in quantity demanded divided by the percentage change in price.” ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS 29 (Scott, Foresman, and Company 1988) (stating that an inelastic demand has a numerical value >1 and an elastic demand has a numerical value <1). In application to the present discussion, if a patient would rather pay a higher price than switch doctors, the demand is “inelastic;” if a patient would rather switch doctors than pay a higher price, the demand is “elastic.” Employers’ motivation is likewise controlled mainly by price, i.e. the demand is elastic. See John M. Eisenberg & Elaine J. Power, Transforming Insurance Coverage Into Quality Health Care: Voltage Drops from Potential to Delivered Quality, 284 J. AM. MED. ASS’N 2100 (2000).
123 See Ellwood, Managed Care, supra note 76, at 1083.
124 Id.
127 See GASTON, MANAGING MANAGED CARE, supra note 34, at 11.
128 See Peeno, Plain and Simple, supra note 95, at 213.
provisions often limit physicians' ability to make decisions. These limitations are often the result of insurers' emphasis of cost-control over quality of care. Collective bargaining can allow physicians to effectively negotiate with insurers on behalf of both physicians and patients in order to solve some of these control issues regarding patients, physician access, and resource utilization.

a. Control of Patients and Resources

From a consumer's standpoint, one issue is the right to choose a physician. From the standpoint of a physician, another issue is the right to exercise independent judgment in the care of patients.

Managed care has an obvious effect on direct control of the patient in the sense of who pays the bills and calls the shots in terms of treatment. Contracts usually determine where a patient goes for care, who his physician is, and what services are "covered" within a plan.

One less obvious aspect of control, however, is who controls the records in terms of access:

Demands for access to medical information are put forward in the name of cost savings, quality improvement, public health, advances in research, and other laudable goals. Managed care companies insist on reviewing medical charts to determine if care should be authorized; accrediting bodies want to ascertain that clinicians' notes are detailed and complete; government agencies seek identifiable information for planning purposes and to prevent fraud; and law enforcement agencies see in medical records a means to identify and convict wrongdoers. Most of the time, access to these records is sought without patients' knowledge or (in more than a formalistic way) consent.

Not only does such access to confidential information violate the traditional patient-physician relationship, but its purpose is to control whether or not a particular treatment plan or diagnostic modality is authorized or not. Insurers are, thereby, invading the traditional role of physicians.
b. Control of Providers

Insurers control providers through a variety of methods. First, they control physicians' decisions by requirement of pre-authorization for referrals, diagnostic studies, or treatment. They may set standards for how many patients a doctor must see in a day. They control access to patients by granting or denying initial contracts. Managed care insurers often track results of physicians' treatment plans, especially costs and create a physician "profile" for each doctor. Sometimes physicians are "deselected" from provider panels. The Supreme Court of California, in a recent decision, held that such a "deselected" physician has a common law right to fair procedure if the insurer possesses power so substantial as to impair the physician's ability to practice his specialty in a particular geographic area and thereby affect an important economic interest. Although resort to the legal process is an important right of such physicians, physician advocacy by a physician union would be a much more practical and less costly alternative to ensure that physicians are treated equitably by insurers.

D. Response to Managed Care

While recognizing that goals of managed care are laudable, whether managed care is good or bad depends to a great deal on one's perspective. Patients want universal coverage, portability of insurance and choice of providers, as well as quality care. Physicians want to avoid onerous contractual clauses and unnecessary financial risks. While maintaining control of patient care decisions and limiting malpractice risks, they want to reduce the workload of pre-authorizations and administrative reviews. Employers want to provide health care coverage of employees with reasonable costs. Nearly all entities must recognize there are problems with our current health care delivery
system, including access to health care and high costs. Despite the current problems already discussed, the reaction of various market participants in dealing with the issues has been largely ineffective. The following discussion will evaluate the response of various participants including federal and state governments, patients, providers, and physician societies.

1. Government

While problems with managed care are of national concern there has been no overall, widespread response to deal with problems on a systematic basis. The response of both federal and state legislatures is best described as “piecemeal.”

For example, Congress currently is considering variations of patients’ “bill of rights” to address issues of patients’ choice of physicians, continuity of care, and right to sue insurers in federal court. Despite recognition of the need for national health care reform, no comprehensive plan has yet been adopted. On both the state and federal levels, individual bills are designed to deal with only one particular issue at a time. A single legislative enactment results in tremendous expenditure of time and money, especially with heavy lobbying by interested parties. Many issues could be addressed more effectively by giving physicians equal power to bargain with insurers on behalf of patients and physicians.


150 See generally Wayne J. Gugliemo, Managed Care Perform? Sure - But Don’t Look to Washington (State Governments Take Lead in Regulating Care), 77 MED. ECON. 40 (2000) [hereinafter Gugliemo, Managed Care Perform?].

151 Id. at 7 (stating that “[S]tate lawmakers point with pride to their crazy quilt of health care reforms . . . .”) (emphasis added).


153 See Gugliemo, Managed Care Perform?, supra note 150, at 40. See also Susan J. Landers, Patient Protection Bill Reborn - But Fails Crucial Tests, AM. MED. NEWS, Nov. 20, 2000, at 5.

154 See Gugliemo, Managed Care Perform?, supra note 150, at 40.

155 For example, in the 2000 election, Massachusetts’ initiative to adopt universal health coverage was narrowly defeated, 52% to 48%. “The measure was strongly opposed by HMOs and insurance companies, which mounted a $5 million advertising campaign urging its defeat.” Susan J. Landers & Vida Foubister, Universal Health Care, Assisted Suicide Initiatives Fail, AM. MED. NEWS, Nov. 27, 2000, at 5 [hereinafter Landers, Universal Health Care].

156 Even the passage of specific laws is often ineffective in the final analysis: for example, passage of law to bring medical directors within the control of state medical boards was unsuccessful in stopping insurer’s onerous practice of denying benefits because the law was pre-empted by ERISA. See Jakleivic, Texas Ruling, supra note 81, at 24.
a. "Piecemeal" Legislation

Current issues are usually addressed on an individual basis by state legislatures through "piecemeal," rather than comprehensive legislation. Examples of such piecemeal state legislation include adoption of legislation calling for prompt payment of physicians and hospitals and enactment of bills to enforce prompt payment. Some states, like Kentucky, have enacted other laws dealing with issues of "any willing provider," "gag clauses," "most favored nation" clauses, emergency care without prior authorization, patient information protection, provider panel selection and termination, prompt payment, and qualifications of an insurance medical director. Passage of such piecemeal legislation is necessary due to lack of other good options to deal with inequitable insurance practices. Physicians have no realistic expectation of negotiating on an equal basis with insurers.

Currently, non-legislative options to deal with inequitable insurance practices really do not exist. For example, one new type of bill, recently passed by California legislatures, requires an HMO using a capitated plan to notify the patient member when a physician provider resigns. This bill was prompted when physicians realized that the insurer was delaying reassignment of patients to a new primary care doctor in order to keep capitation payments rather than making contractually-obligated payments to a newly assigned physician. If a healthy patient did not go to a doctor for several months, the result was that the

158 See Gugliemo, Managed Care Perform?, supra note 150, at 40.
159 See Jackson, Health Plans Under Payment Pressure, supra note 110, at 24.
161 See KY. REV. STAT. ANN. § 304.17A-270c (Baldwins 2000).
162 See KY. REV. STAT. ANN. § 304.17A-530c (Baldwins 2000).
163 See KY. REV. STAT. ANN. § 304.17A-560c (Baldwins 2000).
164 See KY. REV. STAT. ANN. §§ 304.17A-515c and 304.17A-500c(3) (Baldwins 2000).
165 See KY. REV. STAT. ANN. §§ 304.17A-505c; 304.17A-510c(1); 304.17A-510c(2); 304.17A-515c; 304.17A-520c; and 304.17A-545c(2) (Baldwins 2000).
166 See KY. REV. STAT. ANN. §§ 304.17A-545c(4) and 304.17A-525c(4) (Baldwins 2000).
167 See KY. REV. STAT. ANN. § 304.12-235 (Baldwins 2000).
168 See KY. REV. STAT. ANN. § 304.17A-545c (Baldwins 2000).
169 See Frangou, Doctors' Unions, supra note 19 at 1.
170 Capitation is a method of reimbursement whereby the provider receives a flat fee per capita (fee per member per month) in return for providing full health care services to the insured persons. If the patients are healthy and use little or no services, then the provider makes extra profit; if the patients are ill and need a lot of care, the provider suffers the loss.
171 See Page, Doctor Discovers Capitation, supra note 109, at 20.
172 Id.
insurer did not make a capitation payment to any physician. 173 Physicians in the capitated plan were providing care for all patients in the capitated plan but not receiving the actual payments on capitated patients who were not reassigned to a new physician. 174 Even passage of individual bills, much less comprehensive reform, is often nearly impossible due to heavy lobbying by interested parties.175 The political process is simply inefficient and ineffective in many cases to achieve meaningful health care reform.176

b. Quality Health Care Coalition Act of 2000 – H.R. 1304 (Campbell Bill)

A bill, co-sponsored by Representative Tom Campbell and others, passed in the House of Representative in June, 2000.177 The bill provided a right of physicians to collectively bargain over a three-year period, but not to strike, under the auspices of the National Labor Relations Act.178 Opponents of the bill claimed it would lead to cartels, less competition, higher prices, and boycotts.179 Prospects for ultimate passage of the bill into law were guarded according to an American Medical Association ("AMA") article in July, 2000.180 The AMA's fears were correct; the bill failed the 2000 legislative session by not finding a
sponsor in the Senate. The bill is expected to be reintroduced in the next legislative session.

**c. Medicare – a Leader in Health Care**

The major exception to federal inactivity in health care has, of course, been Medicare. In order to understand the problems with the present managed care system, one must appreciate Medicare's role in health care. Not only is Medicare one of the lowest paying insurers, Medicare is the leader in health care, because private insurers generally follow Medicare's changes. Participating providers have no choice but to abide by Medicare rules and regulations. Other insurers follow Medicare's lead, yet, providers have no ability to effectively negotiate changes in the contracts. In essence, under the present system of managed care, providers are forced to accept whatever changes insurers adopt in response to Medicare's changes.

Examples of such major changes over the past twenty years include: change to a resource-based relative value scale ("RBRVS") of reimbursement to providers, institution of payment to hospital providers based on "diagnosis-related groups" ("DRGs"), and development and modification of "evaluation and management" ("E & M") coding. In an effort to control cost of health care for Medicare, Congress has mandated HICFA to adopt a budget-neutral approach to reimbursement. Under the budget-neutral plan, providers get paid less for procedures or treatment if they do a higher volume of the procedures/treatments. The rationale is to offset an increase in total cost that might arise due to providers' behavior in doing more procedures in order to make up in volume the income lost by decreased reimbursements. As a result

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181 See Albert, Bargaining Bill Dies, supra note 20, at 1.
182 Id.
183 See Whetsell, History and Evolution, supra note 18, at 1. See also Frank G. Opelka, M.D., In Their Own Words: Practice Expenses and the RBRVS Revisited, BULL. AM. C. SURGEONS, Jan. 2000, at 36 (hereinafter Opelka, In Their Own Words).
184 See Whetsell, History and Evolution, supra note 18, at 1.
185 See Opelka, In Their Own Words, supra note 183, at 36. See also, infra, "Medicare Sets a Benchmark for Insurer's to Fix Prices."
186 See Whetsell, History and Evolution, supra note 18, at 1.
187 See Opelka, In Their Own Words, supra note 183, at 36.
188 Id.
189 Id.
190 See Whetsell, History and Evolution, supra note 18, at 1.
191 See Opelka, In Their Own Words, supra note 183, at 36. See also, infra, "Medicare Sets a Benchmark for Insurer's to Fix Prices."
192 Id.
193 See Whetsell, History and Evolution, supra note 18, at 1 (stating that the Balanced Budget Act of 1997 instituted a five-year plan to reduce the increase of Medicare expenditures by $115 billion over a five-year period).
195 Id.
of changes in Medicare, over the past several years there has been a trend to pay non-primary care specialists lower fees and increase the reimbursement to primary care physicians.\textsuperscript{195} Such changes in reimbursement have usually been disproportionate among various physician specialties.\textsuperscript{196} Obviously, practitioners often do not accept with open arms Medicare's changes, much less similar changes forced upon them by other insurers who follow Medicare's lead.\textsuperscript{197}

In summary, federal and state government has been ineffective in providing comprehensive health care reform. The present legislative approach has been inefficient overall, since the solution has been a piecemeal approach. To the detriment of providers, insurers follow the changes initiated by Medicare in health care. Collective bargaining by physicians would provide a workable solution to many problems with managed care; however, specific legislative exemption from antitrust law pursuant to the National Labor Relations Act for physician unions has not yet been adopted.

2. Patients

During the 1990s, public opinion has turned against HMOs (representing managed health care).\textsuperscript{198} Eighty-six percent of those polled in a 1998 survey said: "HMOs and other managed care plans are more concerned with holding down costs than with providing good care."\textsuperscript{199} The main points of dissatisfaction with managed care concerned the patients' desire for a long-term patient-doctor relationship, doctors rather than insurers controlling treatment decisions, and access to patients' choice of physicians.\textsuperscript{200} On the other hand, patients were generally satisfied with the cost aspects of the managed care plans.\textsuperscript{201} Employers are likewise dissatisfied with premium increases of managed care plans.\textsuperscript{202}

\textsuperscript{195}See Jane Cys, Hike in Medicare Fee Schedule Good News for Physicians, AM. MED. NEWS, Nov. 20, 2000, at 2. The trend to pay primary care providers more and specialists less results from Medicare's increasing reimbursement for evaluation and management (E & M) services and decreasing reimbursement for procedural-based services. See also Opelka, In Their Own Words, supra note 183, at 36.

\textsuperscript{196}See Cys, Hike in Medicare, supra note 195, at 2.

\textsuperscript{197}See Opelka, In Their Own Words, supra note 183, at 36.

\textsuperscript{198}See Christina Duff, Americans Tell Government to Stay Out - Except in Case of Health Care, HMOs Are Target of Ire and Many Want Regulation, WALL STREET J., Jun. 25, 1998, at A9 [hereinafter Duff, Americans Tell Government to Stay Out]. For an emotion-packed situation exemplifying the battle between HMOs and beneficiaries/providers, see Lucette Lagnado, Deja's View - In a Poor Baby's Fight to Survive, a Parable of a Medicaid HMO, WALL STREET J., Dec. 27, 2000, at A1. A lighter, but equally dramatic portrayal of managed care occurred in the popular film AS GOOD AS IT GETS, starring Jack Nicholson and Helen Hunt. She, portraying a mother whose son had been denied appropriate diagnostic tests in the name of cost efficiency referred to the insurers as "Fucking, bastard, pieces of shit!" AS GOOD AS IT GETS (Tristar Pictures, Inc. 1997). The author is aware of at least one theater audience that responded by cheers and ovation.

\textsuperscript{199}Duff, Americans Tell Government to Stay Out, supra note 198, at A9.

\textsuperscript{200}Id. at A9, A14.

\textsuperscript{201}Id. at A14.

\textsuperscript{202}See Page, Taking Charge, supra note 148, at 21.
Patients are more willing to change doctors to avoid increased out-of-pocket expenses. Patients are also aggravated by other aspects of managed care. For example, with increased pressure on physicians to save money and avoid "unnecessary" tests or treatment, there is growing concern that providers are more interested in making money than providing good care. An example is a recent malpractice suit wherein the patient sued not only her physician, but also the health insurer, for the allegedly negligent treatment of the patient's skin cancer. The claim against the insurer revolves around an express warranty of "assurance of appropriate care" and the financial disincentives for the doctor to refer patients to other physicians.

Patients have growing concerns about cost containment methods (e.g. physician disincentives), physician credentials (quality of care), medical necessity (control of treatment options), appeal procedures (legal rights), choice of physicians, where revenue is spent (patient care vs. administrative expenses), prescription costs (i.e. out-of-pocket expenses), and emergency care. These concerns represent growing dissatisfaction with today's managed care systems.

3. Providers

The growth of physician unions reflects increasing dissatisfaction of physicians with managed care. The overall response of physicians to managed care has been mixed. For example, residency directors, like managed care medical directors, have recognized the importance of clinical competence in skills related to managed care (e.g. cost-effective decision making, ethics, case management, gatekeeping, practice guidelines, etc.). Other studies have documented a negative attitude of some physicians toward managed care. Likewise, physicians or professional societies have spearheaded many attempts at legislative reform.

203 See Ellwood, Managed Care, supra note 76, at 1083.
204 Duff, Americans Tell Government to Stay Out, supra note 198, at A9.
205 Id.
207 See Miles J. Zaremski & Ila S. Rothschild, Malpractice Claim Preempted by ERISA, AM. MED. NEWS, Oct. 9, 2000, at 18.
210 See Michael J. Yedidia et al., Specific Clinical Competencies for Managing Care: View of Residency Directors and Managed Care Medical Directors, 284 J. AM. MED. ASS'N 1093 (2000).
211 See James Gray, "They Really Should Call It Managed Doctors," MED. ECON. - GEN. SURGERY ED., May 1991, at 62. See also Jay Greene, Businesses Lure More Doctors from Practice, AM MED. NEWS, Nov. 6, 2000, at 13 [hereinafter Greene, Businesses Lure].
212 See Have Your Say In Organized Medicine: There's a Place for You on the AMA's Advocacy Team, AM. MED.NEWS, Nov. 6, 2000, at 31 [hereinafter Have Your Say].
One reason for dissatisfaction with managed care is the effect it has had on physicians' salaries. One recent study of current medical school faculty's salaries compared to 1988 showed a decrease in the rate of growth of clinical faculty's salaries that did not keep up with inflation in some specialties. The reason was change in federal reimbursement under Medicare (i.e. adoption of the RBRVS system), rather than the penetration of managed care. Medicare's methods of reimbursement have, in fact, substantially affected reimbursement rates and procedures of all physicians, but have been disproportionately harsh on surgical specialists: "While the actual cost of a surgeon's practice increases, decreased reimbursements in the fee schedule impair the delivery of surgical care with every passing year." The expected impact of the most recent Medicare fee schedule is that several key surgical procedures and many surgical specialties will suffer further cuts in reimbursements through 2002.

4. Professional Societies

Medical societies are becoming more pro-active in dealing with perceived inequities of managed care. For example, some state medical societies are joining as parties in litigation against insurance companies for alleged abuses in insurer's failure to make prompt payments to providers. Medical societies are also active in lobbying for legislation on both the state and federal levels. Medical societies have traditionally been opposed to physicians unions. However, as a result of the paradigm shift from traditional fee-for-service to managed care, medical societies are not only tolerant of physician unions, but endorse collective bargaining activities. The American Medical Association has even organized a physician union in recent months.

213 Various reports have shown: (1) any increases in salaries of various physician specialties to be less than the rise in the cost of living index; see Joel H. Goldberg, Surgeons' Earnings: A Decent Year, A Disappointing Decade, MED ECON., - GEN. SURGERY ED., Nov./Dec. 1999, at 7; (2) regardless of charges, surgeons' reimbursements are being cut; see Mark Crane, Charge What You Will . . . Surgeons' Reimbursements Are Shrinking, MED. ECON. - GEN. SURGERY ED., Oct. 1998, at 33; see also Mark Crane, General Surgeons' Fees vs. Reimbursements: The Gap Widens, MED ECON. - GEN. SURGERY ED., Nov./Dec. 1999, at 16; and, (3) there is a shift in payment priority from surgical specialists to internists and primary care doctors, see Polly Miller, Doctors' Incomes: Who's Up, Who's Down?, MED ECON. - GEN. SURGERY ED., Oct. 1998, at 27.


215 Id. at 1135.

216 Opelka, In Their Own Words, supra note 183, at 36.

217 See Brown, What Surgeons Should Know, supra note 193, at 8.

218 See Tanya Albert, TMA OKs Suing Insurers Over Late Physician Payments, AM. MED. NEWS, Nov. 6, 2000, at 16.

219 Id.

220 See Have Your Say, supra note 212, at 31.


222 Id.
E. Summary of Changing Aspects of Medical Care

In summary, the change from traditional indemnity coverage of health care to managed care represents a paradigm shift. Although the goals of managed care are laudable, in practice many problems exist. High costs of medical care continue. New problems have developed, such as lack of choice of providers. Both providers and consumers have increasing dissatisfaction with managed care. Despite the dissatisfaction, present methods of solving problems, e.g. legislation, have been inefficient and ineffective. Physician unions could efficiently solve many current problems by providing negotiating power to deal with insurers on behalf of physicians and patients; however, specific legislation providing antitrust exemption for physician unions has not yet been enacted.

III. ANALYSIS OF ANTITRUST ISSUES

A. Introduction

Physicians are likely to find antitrust law generally confusing or, at least, unsettled as it pertains to health care issues. One reason both Congress and the courts have failed to provide clarity of standards in antitrust may be that they have been responsive to changing social and political pressures. Several other factors contribute to the difficulty in understanding appropriate standards of antitrust law. First, the courts from time to time have issued decisions that seem diametrically opposed and irreconcilable. Second, the method of analysis to be applied in any particular case, i.e. per se rule versus rule of reason, depends on the nature of the restraint and particular characteristics of the restraint; yet, within any given category of antitrust case, the U.S. Supreme Court’s actual application of one or the other analyses has been historically inconsistent.

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224 See, e.g., Appalachian Coals, Inc. v. United States, 288 U.S. 344 (1933) (applying a liberal rule of reason to allow a combination of coal companies to fix prices in order to stabilize their market during the Great Depression). Cf. United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940) (enunciating a per se rule against price fixing although the fact pattern was quite similar to that in Appalachian Coals).

225 Compare use of per se rule in horizontal price fixing in United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940) with use of rule of reason in horizontal merger of United States v. Phillipsburg National Bank & Trust Co., 399 U.S. 350 (1970). Price fixing may be held to be per se illegal; however, mergers will not be per se illegal and will be evaluated under a rule of reason.

226 In horizontal price fixing, the Supreme Court in Socony-Vacuum, 310 U.S. 150 applied a per se rule, whereas in a vertical price fixing agreement, the Court in State Oil Co. v. Khan, 522 U.S. 3 (1997) advocated a rule of reason analysis.

227 For example, see National Society of Professional Engineers v. United States, 435 U.S. 679, 692 (1978) (wherein the Supreme Court advocated a rule of reason yet, in short order found the agreement of competitors to be unlawful noting “[N]o elaborate industry analysis is required to demonstrate the anti-competitive character of such an agreement”). See also National Collegiate Athletic Association v. Board of Regents of the University of Oklahoma, 446 U.S. 85, 1 (1984) (wherein footnote 26 the Supreme Court noted “Indeed there is often no bright line separating per
Finally, courts have only rarely expressly overturned prior decisions even though their later decisions are inconsistent with precedent.\textsuperscript{228}

Before embarking on an analysis of antitrust law as it relates to health care in general and to physician unions specifically, one must appreciate that there is a paucity of cases directly on point. Thus, the author's analysis of the involved issues is based generally on antitrust precedent as related to issues likely to arise when an appropriate challenge to physician unions actually makes its way into and through the judicial system.

Any such analysis must consider issues of price fixing as well as concerted action. Price fixing may arise in circumstances of direct\textsuperscript{229} or implicit\textsuperscript{230} price fixing, both horizontally\textsuperscript{231} and vertically.\textsuperscript{232} Finally, the challenge to properly

\footnote{228} Although the inconsistency between Appalachian Coals and Socony-Vacuum, Appalachian Coals was not expressly overruled. \textit{See also} State Oil Co. v. Khan, 522 U.S. 3 (1997) (wherein the Supreme Court overturned Albrecht v. Herald Co., 390 U.S. 145 (1968) following a critical opinion by Judge Posner wherein he made it clear his decision was based solely on authority of \textit{Albrecht} "despite all its infirmities, its increasingly wobbly, moth-eaten foundations. \textit{Albrecht} was unsound when decided, and is inconsistent with later decisions by the Supreme Court. It should be overturned." Khan v. State Oil Co., 93 F.3d 1359, 1363 (7th Cir. 1996).

229 Direct price fixing includes setting specific prices. \textit{See} Appalachian Coals, Inc. v. United States, 288 U.S. 344 (1933) (a company comprised of coal producers set the price of coal to sell at the best prices obtainable); United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940) (major oil companies set the tank car prices and retail prices of gasoline); United States v. Trenton Potteries Co., 273 U.S. 392 (1927) (members of a trade organization set the prices for sanitary pottery). Direct price fixing also includes setting minimum prices. \textit{See} Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975) (bar association published a minimum fee schedule for attorneys fees). Finally, direct price fixing includes setting maximum prices. \textit{See} Arizona v. Maricopa County Medical Soc'y, 457 U.S. 332 (1982) (physician-administered foundations set maximum fees that member physicians could charge for services was held to be unlawful price fixing); Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc., 467 U.S. 752 (1984) (agreement among liquor distillers to set maximum prices that distributors could charge was unlawful). \textit{But see} State Oil Co. v. Khan, 522 U.S. 3, (1997) (setting maximum prices in a vertical arrangement was judged by a rule of reason).


231 An agreement among physicians within a union to fix prices would be a horizontal price fixing agreement because the agreement is among competitors.

232 An agreement between a managed care plan (i.e. insurer) and a physician union (representing physician providers) to fix prices for consumers (e.g. employers or individuals as purchasers of health care) would represent a vertical price fixing arrangement because the agreement would be between different levels of participants in the distribution of health care.
apply antitrust policies and principles to the analysis of physician unions, like nearly all cases under antitrust law, will likely be very fact specific.\textsuperscript{233}

The specific issue for this article’s analysis is whether physician unions should be evaluated by a per se rule or a rule of reason when questions of price fixing or concerted action arise. Thus, the first step is to evaluate appropriate case law in order to determine which method of analysis is appropriate. Then, combined Health Care Guidelines of the Department of Justice and the Federal Trade Commission must be considered for their practical impact on antitrust issues related to the health care field, including tension with established case law.

\textbf{B. Case Law and Statutory Precedent of Antitrust Issues Involved in Health Care}

\textit{1. Per Se Rule Versus Rule of Reason – A Historical Review of Case Law}

Physician unions may run afoul of two major antitrust areas: price fixing and concerted action, i.e. boycotts. In fact, opponents of physician unions primarily fear two things: physician’s controlling prices or striking.\textsuperscript{234} Rather than condemning physician unions because of fear or in the case of antitrust law, per se illegality, physician’s collective bargaining agreements should be analyzed by a rule of reason. In order to understand the rationale of applying a rule of reason, case law must be reviewed with regard to: (1) price fixing; and (2) boycotts.

\textit{a. Price fixing}

Price fixing is defined by case law and includes more than literally fixing prices at a stated level:

\begin{quote}
\[ \text{P} \text{rice-fixing includes more than the mere establishment of uniform prices.} \ldots \text{P} \text{rices are fixed} \ldots \text{if the range within which purchases or sales will be made is agreed upon, if the prices paid or charged are to be at a certain level or on ascending or descending scales, if they are to be uniform, or if by various formulae they are related to the market price. They are fixed because they are agreed upon.} \textsuperscript{235} \]
\end{quote}

\textsuperscript{233} In \textit{Chicago Board of Trade v. United States}, Justice Brandeis wrote:

To determine that question [legality under a rule of reason analysis] the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint, and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts.


\textsuperscript{235} United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 222 (1940).
Although the judicial view on price fixing has essentially been a long-standing, steadfast decision of illegality, the mode of analysis has fluctuated historically. Although the terms "per se rule" and "rule of reason" were not coined until later, the early cases also involved tension between these modes of analysis. For example, United States v. Trans-Missouri Freight Association, was the first price fixing case to reach the United States Supreme Court. The lower court agreed with the defense that the Sherman Act did not apply to setting of fees as long as reasonable, yet the United States Supreme Court held that the reasonableness of an agreement to set prices was immaterial as all agreements that restrained trade were violations of the Sherman Act.

The Court also referred to "competition" but failed to give competition the importance it would later have in the decision analysis under the rule of reason. By failing to consider the reasonableness of the agreement of the railroad companies to fix rates, and more importantly to consider the effect on competition, the Court, in essence, applied a per se rule of illegality to price fixing.

The following year, the same Supreme Court took the analysis a step further by considering the effect of the railroad defendants' rate-setting on competition: "An agreement of the nature of this one, which directly and effectually stifles competition, must be regarded under the statute as one in restraint of trade . . . ." Furthermore, the Court went on to consider the effect on competition in the overall efficiency of the economy:

There can be no doubt that the general tendency of competition among competing railroads is towards lower rates for transportation, and the result of lower rates is generally a greater demand for the articles so transported, and this greater demand can only be gratified by a larger supply, the furnishing of which

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236 "Thus for over forty years this Court has consistently and without deviation adhered to the principle that price-fixing agreements are unlawful per se under the Sherman Act . . . ." United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 218 (1940).

237 The per se rule was applied in United States v. Trenton Potteries Co., 273 U.S. 392 (1927), but was not coined "per se." The term "per se" was used specifically in United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940). Likewise, Standard Oil Co. of New Jersey v. United States, 221 U.S. 1 (1911) is usually credited with first applying the rule of reason, but the rule of reason was further defined in Chicago Board of Trade v. United States, 246 U.S. 231 (1918). Finally, the opinion of Justice Stone coined the term in United States v. Trenton Potteries Co., 273 U.S. 392, 396 (1927). Both the origin of the rule and the term "rule of reason" were solidified by Justice Douglas' later opinion: "This Court pointed out [in United States v. Trenton Potteries Co., 273 U.S. 392] that the so-called "rule of reason" announced in Standard Oil Co. of New Jersey v. United States, 221 U.S. 106, had not affected this view of the illegality of price-fixing agreements . . . ." United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 213 (1940).

238 United States v. Trans-Missouri Freight Ass'n, 166 U.S. 290 (1897).


240 See Trans-Missouri, 166 U.S. at 328.

241 "Competition, free and unrestricted, is the general rule which governs all the ordinary business pursuits and transactions of life." Id. at 337.

242 See Standard Oil Co. of New Jersey v. United States, 221 U.S. 106 (1911).

increases commerce. This is the first and direct result of competition among railroad carriers.244

Although not called the rule of reason, the Court’s analysis of competition and its efficiency represents the first steps in development of such a rule.

United States v. Addyston Pipe & Steel Co.245, a Sixth Circuit case decided the same year but modified and affirmed only one year later, in 1899, stands in sharp contrast to United States v. Joint-Traffic Association.246 Therein, William Howard Taft247 clearly opined that price fixing is illegal per se rule.248

Standard Oil Company of New Jersey v. United States249 is traditionally credited with enunciation of the rule of reason.250 The actual language, however, is less than clear:

The mere generic enumeration which the statute [Sherman Act] makes of the acts to which it refers and the absence of any definition of restraint of trade as used in the statute leaves room for but one conclusion, which is, that it was expressly designed not to unduly limit the application of the act by precise definition, but while clearly fixing a standard, that is, by defining the ulterior boundaries which could not be transgressed with impunity, to leave it to be determined by the light of reason, guided by the principles of law and the duty to apply and enforce the public policy embodied in the statute, in every given case whether any particular act or contract was within the contemplation of the statute.251

What a rule of reason analysis should entail is far from clear in that opinion. An agreement’s effect on competition is certainly not touted as the test of unlawfulness by the Supreme Court in Standard Oil of New Jersey.252 Clarification of the rule of reason is provided by Justice Brandeis’ majority opinion in Chicago Board of Trade v. United States:

[T]he legality of an agreement or regulation cannot be determined by so simple a test as whether it restrains competition. Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint, and its effect, actual or probable. The history of the restraint, the

244 Id. at 576.
245 85 F. 271 (6th Cir. 1898).
246 171 U.S. 505 (1898).
247 William Howard Taft later became Governor of the Philippine Islands, the President of the United States of America, then the Chief Justice of the United States Supreme Court.
249 Standard Oil Co. of New Jersey v. United States, 221 U.S. 1 (1911).
251 Standard Oil Co. of New Jersey v. United States, 221 U.S. 1, 63 (1911) (emphasis added).
252 See id.
evil believed to exist, the reason for adopting the particular remedy, and the 
purpose or end sought to be attained, are all relevant facts.253

Thus, the inevitable conclusion is that the rule of reason entails analysis of 
numerous factors specific to each case and the overall effect of a contract, 
conspiracy, or agreement on competition. Within less than a decade, the tide 
shifted back to a per se rule.254

In 1927, as justification of their view of per se illegality, the United States 
Supreme Court noted: “The power to fix prices, whether reasonably exercised or 
not, involves power to control the market and to fix arbitrary and unreasonable 
prices. The reasonable price fixed today may through economic and business 
changes become the unreasonable price of tomorrow.”255

At the other, extreme end of the spectrum of analysis lies Appalachian 
Coals, Inc. v. United States.256 The Court upheld the lawfulness of Appalachian 
Coals, Inc., a company formed to sell the entire coal production of its producer-
owners at the best prices obtainable, with the selling prices to be set by officers 
of the company.257 The Court went well beyond abrogating a per se rule for the 
analysis of price fixing.258

“[A] close and objective scrutiny of particular conditions and purposes is 
necessary in each case. Realities must dominate the judgment. The mere fact 
that the parties to an agreement eliminate competition between themselves is not 

enough to condemn it . . . .”259 The Court not only ignored the effect of the price-
fixing agreement on competition, but seemed to revert to a total “reasonableness 
derunder the circumstances” test, advocating consideration of factors such as 
economic conditions peculiar to the industry, reasons for the price-fixing 
agreement, probable consequences of the agreement on the market prices, and 
“other matters affecting the public interest . . . .”260

Without overruling Appalachian Coals, Inc.,261 the United States Supreme 
Court in Socony-Vacuum Oil Co262 claimed that it had long advocated a per se 
rule against price fixing: “Thus for over forty years this Court has consistently 
and without deviation adhered to the principle that price-fixing agreements are 
unlawful per se . . . .”263 Although the track record of the Court may not have 
been as solid as claimed in the opinion, especially since none of the above

253 Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918) (emphasis added).
255 Id. at 397.
256 Appalachian Coals, Inc. v. United States, 288 U.S. 344 (1933).
257 Id. at 357-58.
258 Id. at 373-74 (finding no evidence for price fixing and even if it existed would allow it on the 
basis of procompetitive effect for a troubled industry in a depressed economy).
259 Id. at 360.
260 Id. at 361.
261 United States v. Socony-Vacuum Oil Co, 310 U.S. 150, 216 (1940)(distinguishing Appalachian 
Coals, Inc., rather than overruling it).
263 Id. at 218.
mentioned cases had been overturned, the ultimate conclusion was clear: price-fixing is per se illegal.264

The majority of the United States Supreme Court seemed to follow a per se rule in United States v. Container Corporation of America,265 a case dealing with an implicit agreement to fix prices.266 However, a subsequent case referred to Container Corporation of America as advocating a rule of reason.267 Neither Justice Fortas in his concurring opinion268 nor Justice Marshall in his dissent would have applied the per se rule.269 In the words of Justice Marshall:

Per se rules always contain a degree of arbitrariness. They are justified on the assumption that the gains from imposition of the rule will far outweigh the losses and that significant administrative advantages will result . . . . I do not believe that the agreement in the present case is so devoid of potential benefit or so inherently harmful that we are justified in condemning it without proof that it was entered into for the purpose of restraining price competition or that it actually had that effect . . . .

To summarize case law under the issue of price fixing, one must realize that the courts have remained unsettled between a rule of reason and a per se rule. The standard to be applied to issues of boycotts is also unsettled. After examining traditional case law regarding the issue of boycotts, our analysis will shift to more recent cases with emphasis on antitrust issues as related to professionals.

b. Boycotts and Refusals to Deal

A physician union could potentially deal with an insurer or other market participant by means of a strike or other refusal to deal, e.g. refusal to accept certain contract provisions or price schedules. While an individual may lawfully refuse to deal, refusal to deal based on an agreement of competitors may be unlawful.270 Whether such concerted action violates antitrust law obviously depends on case law. The legal tests for boycotts and refusals to deal, like those for price fixing, are unsettled.

264 Id. at 223.
266 Id.
267 See United States v. United States Gypsum Co., 438 U.S. 422 n.16 (1978) which states:

The exchange of price data and other information among competitors does not invariably have anticompetitive effects; indeed such practices can in certain circumstances increase economic efficiency and render markets more, rather than less, competitive. For this reason, we have held such exchanges of information do not constitute a per se violation of the Sherman Act. See, e.g., United States v. Container Corp. . . . .

Id. (emphasis added).
269 Id. at 340 (Marshall, J., dissenting).
270 Id. at 341.
271 See Eastern States Retail Lumber Dealers' Ass'n. v. United States, 234 U.S. 600 (1914).
In Paramount Famous Lasky Corp. v. United States, the Court rejected a defense argument that provisions of an agreement were good for the industry as a whole, while noting that "unusual arrangements which unreasonably suppress normal competition" are unlawful. Such consideration of the arrangements and the effect on competition suggests a rule of reason analysis. Another notable fact in that case is that defendants controlled 60% of the relevant market. Illegality of boycotts, or other refusals to deal, may depend on whether the offenders have market power.

The Court in Fashion Originators Guild of America, Inc. v. Federal Trade Commission recognized the power of the trade guild and the Court refused to allow the guild to use its power for anticompetitive purposes. Although the case essentially appears to be a per se approach, the Court's consideration of power of the guild and alternative avenues for the guild to accomplish its goal of preventing style piracy by competitors suggests that the Court really used a limited rule of reason analysis. Regardless of the means, the end result is that competitors acting under guise of self-regulating an industry cannot eliminate competition by a group boycott.

Klor's Inc. v. Broadway-Hale Stores, Inc. reinforced the per se rule of boycotts:

"Group boycotts, or concerted refusals by traders to deal with other traders, have long been held to be in the forbidden category. They have not been saved by allegations that they were reasonable in the specific circumstances . . . . Even when they operated to lower prices or temporarily stimulate competition they were banned." Likewise, the United States Supreme Court appears to have followed a per se method in other cases.

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272 282 U.S. 30 (1930).
273 282 U.S. at 43.
274 282 U.S. at 36.
276 312 U.S. 457 (1941).
277 Id.
281 359 U.S. at 212.
282 See, e.g., Radiant Burners, Inc. v. Peoples Gas & Coke Co., 364 U.S. 656 (1961) (concluding that an implied boycott was unlawful because a non-objective test was used by a regulatory body to limit competition). The Court's decision was made on facial evidence of the arrangement without consideration of actual effects on competition. Id. "The conspiratorial refusal . . . falls within one of the classes of restraints which from their nature or character are unduly restrictive, and hence forbidden by both the common law and the statute . . . ." Id. at 659-60.
Refusal to deal for other than a valid business reason may be inferred to be anticompetitive and, therefore, unlawful.\(^{283}\) Although a party has no duty to cooperate with competitors, refusal to deal may be unlawful if such cooperation would be beneficial to the public and competition is harmed, but only in the absence of a valid business reason not to deal.\(^{284}\) Thus, one limitation on the per se approach is the need to consider the purpose of the agreement as well as its effect on competition.\(^{285}\)

Application of the per se rule to boycotts was further limited to three situations: (1) efforts to disadvantage competitors by persuading or coercing suppliers or customers to not deal with the competitors when such relationships are necessary for the competitors to compete; (2) a boycott to cut off access to necessary supply, facility or market necessary for the boycotted firm to compete; and, (3) refusal to deal is not justified by plausible reasons of efficiency and enhancing competition.\(^{286}\) Even though the Court applied a label of "per se" to those limited situations, one must obviously inquire as to the effect of a refusal to deal on competition before applying the "per se" rule. In the context of an office supply-purchasing cooperative, the Court adopted a rule of reason decision:

"Unless the cooperative possesses market power or exclusive access to an element essential to effective competition, the conclusion that expulsion is virtually always likely to have an anticompetitive effect is not warranted . . . . Absent such a showing with respect to a cooperative buying arrangement, courts should apply a rule-of-reason analysis."\(^{287}\)

The rule of reason standard was reinforced and clearly adopted in *Federal Trade Commission v. Indiana Federation of Dentists*.\(^{288}\) That case involved refusal of dentists to submit X-rays to insurers for purpose of determining whether treatments were covered by patients' insurance benefits.\(^{289}\) The facts could be quite analogous to situations of a physician union-insurer relationship. Although the Court rejected the dentists' argument that quality care concerns motivated the boycott, the importance of the case is the clear adoption of the rule of reason.\(^{290}\)


\(^{284}\) Id.

\(^{285}\) Another exception to illegality of boycotts is a boycott whose principle purpose is political speech, a situation analogous to a hypothetical physician union refusing to deal with insurers for political motives (e.g. as a statement against onerous contract clauses like "gag rules"). *See* NAACP v. Claiborne Hardware Co., 458 U.S. 886 (1982) (allowing a boycott as political speech). *Cf.* Federal Trade Comm'n v. Superior Court Trial Lawyers Ass'n, 493 U.S. 411 (1990) (rejecting the defense's argument based on political speech and noting that the argument "exaggerates the significance of the expressive component . . . ."). *Id.* at 430.


\(^{287}\) *Id.* at 296-97.


\(^{289}\) *Id.*

\(^{290}\) Perhaps the Supreme Court, in 1986, gave more credit to insurers' quality concerns than they would receive today:
A per se approach was revived in Federal Trade Commission v. Superior Court Trial Lawyers Association; however, the boycott issue was, perhaps, overshadowed by the price fixing issue. In a more recent decision, use of per se analysis was limited to horizontal boycotts. Although the use of per se rule has not been abrogated with finality, the recent trend of case law is to analyze agreements under a rule of reason.

c. Status of Professionals – A Sub-Issue

The Court in Socony-Vacuum Oil Co. remarked that “the Sherman Act, so far as price-fixing agreements are concerned, establishes one uniform rule applicable to all industries alike.” The uniform application of the per se rule has been subsequently challenged by various groups. Lawyers, as defendants in Goldfarb v. Virginia State Bar, argued in 1975 that “learned professionals” were not within the scope of the Sherman Act and thus the bar associations’ activities in providing advisory minimum fees to its members were exempt from the Act. In addition to holding that the bar associations’ activities “constitute a classic illustration of price fixing,” the Court held: “The nature of an occupation, standing alone, does not provide sanctuary from the Sherman Act, nor is the public-service aspect of professional practice controlling in determining whether §1 includes professions.” In essence, the Court applied a per se rule against price fixing, finding the argument of exemption for professionals unconvincing.

They [insurers] are themselves in competition for the patronage of the patients – or, in most cases, the unions or businesses that contract on their behalf for group insurance coverage – and must satisfy their potential customers not only that they will provide coverage at a reasonable cost, but also that coverage will be adequate to meet their customers’ dental needs.

Id. at 463.


292 See id. at 436 n. 19.


294 A final example of this trend is noteworthy: in NCAA v. Board of Regents of the Univ. of Okla., the district court found an illegal boycott between the NCAA and the television networks who threatened to expel colleges who refused to adhere to NCAA’s television plan. 546 F.Supp. 1276 (W.D. Okla. 1982). The 10th Circuit reversed that decision since the schools had only a non-competitive vertical relationship with the networks. See 707 F.2d 1147 (10th Cir. 1983). The boycott issue was not even mentioned by the Supreme Court in the final analysis. See National Collegiate Athletic Ass’n v. Board of Regents of Univ. of Okla., 468 U.S. 85 (1984).


297 Id. at 786.

298 Id. at 783.

299 Id. at 787.

300 Id. (citing Associated Press v. United States, 326 U.S. 1, 7 (1945)).

301 Id. (citing United States v. National Ass’n of Real Estate Bds., 339 U.S. 485, 489 (1950)).

In *National Society of Professional Engineers v. United States*, the Court again found the learned profession of engineering to be subject to the Sherman Act, however, in holding that the Society's Code of Ethics' prohibition of soliciting and submitting price information as bids for jobs was an implicit price fixing, the Court used not a per se rule, but rather the rule of reason. The Court noted in its opinion that the rule of reason had its "origin in common law precedents long antedating the Sherman Act . . . ." The Court also described the nature of the rule of reason: "Contrary to its name, the Rule does not open the field of antitrust inquiry to any argument in favor of a challenged restraint that may fall within the realm of reason. Instead, it focuses directly on the challenged restraint's impact on competitive conditions." In addition, the opinion serves to shed some light on how individual cases are to be analyzed:

There are, thus, two complementary categories of antitrust analysis. In the first category are agreements whose nature and necessary effect are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality -- they are "illegal per se." In the second category are agreements whose competitive effect can only be evaluated by analyzing the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed. In either event, the purpose of the analysis is to form a judgment about the competitive significance of the restraint; it is not to decide whether a policy favoring competition is in the public interest, or in the interest of the members of the industry.

The Court in *National Society of Professional Engineers* found the refusal of professional engineers to discuss prices during negotiations with their customers was anticompetitive: "While this is not price fixing as such, no elaborate industry analysis is required to demonstrate the anticompetitive character of such an agreement." Such language tends to blur the distinction between a per se rule and a rule of reason; however, the case was one of implicit price fixing and a detailed analysis was not required since the agreement was clearly anticompetitive.

The Court does acknowledge that cases involving professionals may require some special consideration: "We adhere to the view expressed in Goldfarb that, by their nature, professional services may differ significantly from other business services, and, accordingly, the nature of the competition in such services may vary." The dissent by Justice Blackmun opined that requiring professionals to meet the procompetitive effect under the rule of reason might be to construe the

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304 See id.
305 Id. at 692.
306 Id. at 687-92.
307 Id. at 688 (citing Mitchel v. Reynolds, 1. P. Wins. 181, 24 Eng. Rep. 347 (1711)).
309 Id. at 692.
310 Id. (emphasis added).
311 Id.
312 Id. at 696.
Act too narrowly when applied to professionals, especially in agreements concerning ethical rules or professional competency. 313 Historically, the next major exception to application of the per se rule was Broadcast Music, Inc. v. Columbia Broadcasting System, Inc. 314 in 1979. Broadcast Music, Inc. (BMI) sold a blanket license to Columbia Broadcasting Systems, Inc. (CBS) for use of copyrighted musical compositions rather than such licenses being sold individually by the artists. 315 The United States Supreme Court overturned the Second Circuit’s opinion that the blanket license, as a form of price fixing, was illegal per se. 316 The United States Supreme Court found application of a per se rule inappropriate in situations novel to the court: “Consequently, as we recognized in United States v. Topco Associates, Inc., . . . ‘[i]t is only after considerable experience with certain business relationships that courts classify them as per se violations . . . .’” 317 The Court seems to indicate that the rule of reason is the default test unless the court has such prior experience that it can dispense with such analysis and go immediately to a per se rule: “[T]he Court has held that certain agreements or practices are so ‘plainly anticompetitive’ and so often ‘lack . . . any redeeming virtue,’ that they are conclusively presumed illegal without further examination under the rule of reason generally applied in Sherman Act cases.” 318 The United States Supreme Court went on to apply a rule of reason analysis and defined a “new product” or “different product” exception to application of the per se rule. 319

d. NCAA v. Board of Regents – What Dichotomy?

The last major development in the issue of antitrust analysis was National Collegiate Athletic Association v. Board of Regents of The University of Oklahoma. 320 The Court decided it would be inappropriate to apply the per se rule, not because of lack of judicial experience, nor because of the character of the NCAA as a non-profit organization, nor the Court’s respect for NCAA’s historic role in college sports, but rather “what is critical is that this case involves an industry in which horizontal restraints on competition are essential if the product [competition] is to be available at all . . . .” 321 Justice Stevens rationalized that there is no real difference in per se analysis and rule of reason analysis since the ultimate question under either a per se analysis or rule of

313 Id. at 700-01 (Blackmun, J., dissenting).
315 Id. at 4-5.
316 Id. at 7.
317 Id. at 9 (citing United States v. Topco Associates Inc., 405 U.S. 596, 607-08 (1972)) (internal citations omitted).
318 See Broadcast Music, 441 U.S. at 8 (emphasis added).
319 Id. at 22.
321 Id. at 100-01.
reason "remains the same - whether or not the challenged restraint enhances competition."322

Thus, the implication is that the application of a per se rule or rule of reason analysis should result in the same outcome in a given case. This rejection of the dichotomy between per se versus rule of reason analysis implies a significant change in application of the per se rule: "Indeed, there is often no bright line separating per se from Rule of Reason analysis. Per se rules may require considerable inquiry into market conditions before the evidence justifies a presumption of anticompetitive conduct."323 Does not such a "considerable inquiry" before a presumption imply, at least, an abbreviated rule of reason analysis?

In applying the rule of reason, the NCAA Court defines the product as competition;324 it defines the market as college football television broadcasts;325 and, it defines the anticompetitive effects of NCAA’s regulatory agreement – higher price, lower output, (effects that are unresponsive to consumer demand), and elimination of competitor’s from the market326 in a circumstance whereby NCAA has essentially total control of the market.327 At that point in the analysis, the Court notes: "Under the Rule of Reason, these hallmarks of anticompetitive behavior place upon petitioner [NCAA] a heavy burden of establishing an affirmative defense which competitively justifies this apparent deviation from the operation of a free market . . ."328 In the final analysis, although “most of the regulatory controls of the NCAA are justifiable means of fostering competition among amateur athletic teams and therefore procompetitive because they enhance public interest in intercollegiate athletics,”329 on balance the court found the anticompetitive harm outweighed the procompetitive benefits and upheld the Court of Appeal’s affirmation of the District Court’s injunction against the NCAA’s practice.330

NCAA is particularly important for several reasons. First, it abrogates the dichotomy between per se rule and rule of reason. Second, even if a per se analysis is applied, it may require considerable inquiry into market conditions before a presumption of per se illegality can be decided. Finally it is instrumental in defining the appropriate steps in the rule of reason analysis: define the product, define the market, assess the anticompetitive effects and balance them against the pro-competitive benefits.

322 Id. at 104.
323 Id. at 104 n.26 (emphasis added).
324 Id. at 101.
325 Id. at 112.
326 See National Collegiate Athletic Ass'n, 468 U.S. at 105-108.
327 Id. at 112.
328 Id. at 113.
329 Id. at 117.
330 Id. at 120.
2. Statutory Precedent – Exemptions from Antitrust

History illustrates that the per se rule so clearly advocated by *Socony-Vacuum, Inc.* is no exception to the common cliche: “Rules are made to be broken.” Congress has been one such “rule-breaker.” Numerous industries are statutorily exempt from antitrust action: agricultural cooperatives; insurance industry; rail and motor carrier rate-fixing bureaus; and, newspaper joint-operator agreements. Professional sports are exempt from antitrust laws for joint marketing of television rights. Collective bargaining of employees within labor unions is a statutory exemption of antitrust laws under the National Labor Relations Act. Finally, the following discussion of the 1996 Health Care Guidelines illustrates yet another break from the traditional per se rule in theory and current practice.

C. 1996 Health Care Guidelines

From time to time, the enforcement agencies of federal antitrust law, i.e. the Department of Justice and the Federal Trade Commission (“Agencies”), have issued statements to provide practical guidance for activities that fall within limits of antitrust law. In 1992, the Agencies issued Horizontal Merger Guidelines that were subsequently amended in 1997. Although the Horizontal Merger Guidelines were not developed specifically for the health care field, they are applicable to mergers within the health care industry as evidenced by reference to the merger guidelines within the 1996 Statements of Antitrust Enforcement Policy in Health Care (“Health Care Guidelines”).

The 1996 Health Care Guidelines actually represent a modification and extension of similar guidelines developed and disseminated by the Agencies in...

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PHYSICIANS VERSUS MANAGED CARE

1993 and revised in 1994. Under the 1993 health care guidelines, the Agencies issued six statements of their antitrust enforcement policies in the health care area: (1) hospital mergers; (2) hospital joint ventures involving high-technology or other expensive medical equipment; (3) physicians’ provision of information to health care purchasers; (4) hospital participation in exchanges of price and cost information; (5) health care providers’ joint purchasing arrangements; and (6) physician network joint ventures.

In response to comments received, the Agencies revised and expanded the 1993 guidelines in 1994; the new guidelines superceded the 1993 version and added three additional guidelines. The Agencies’ stated goal is “to ensure a competitive marketplace in which consumers will have the benefit of high quality, cost-effective health care and a wide range of choices, including new provider-controlled networks that expand consumer choice and increase competition.” The changes in the 1996 Guidelines were mainly to expound upon the guidelines for physician network joint ventures and for multiprovider networks, especially in light of evolution of health care markets, consumer demand, and competition in the marketplace.

Under the area of physician network joint ventures, one major change from the 1994 guideline is the expansion of the concept of integration beyond financial risk to include clinical integration.

“The revisions focus on the analysis of networks that fall outside the safety zones contained in the existing [i.e., 1994] statement, particularly those networks that do not involve the sharing of substantial financial risk by their physician participants . . . . [W]here physicians’ integration through the network is likely to produce significant efficiencies, any agreements on price reasonably necessary to accomplish the venture’s procompetitive benefits will be analyzed under the rule of reason.”

Thus, the new test is not just substantial financial risk sharing; such physician networks “may be lawful if the . . . joint venture creates significant efficiencies and the venture, on balance, is not anticompetitive.” The Agencies use a balancing test, under a rule of reason analysis, such that if either (1) procompetitive effects outweigh anticompetitive effects, or (2) in the absence of anticompetitive effects significant benefits are achieved in either cost-

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341 See id. at 1-3.
342 See id. at 2.
343 See id. at 1.
344 See id. at 2. The additional three guidelines added in 1994 are the same as Statements 7, 8, and 9 under the 1996 guidelines: Statement 7 Joint Purchasing Arrangements Among Health Care Providers, Statement 8 Physician Network Joint Ventures, and Statement 9 Multiprovider Networks. Id.
345 Id. at 3.
346 Id. at 2-3.
347 Id. at 2.
348 Id. at 3-4.
349 Id.
350 Id. at 70.
containment or improved quality of care, the venture is not unlawful, despite presence or lack of financial integration, i.e., financial risk. 351

Substantial financial risk sharing may include capitation, provision of care based on a pre-determined percentage of premiums or revenue, financial incentives to achieve specified cost containment goals, or global fees, i.e. all-inclusive care for a predetermined payment. 352 If a physician joint network has substantial integration, either through substantial financial risk-sharing and/or non-financial integration, it is analyzed under the rule of reason, but if it has little or no integration, it is per se illegal. 353 Per se violations are rarely mentioned in the 1996 Guidelines. 354

The final 1996 guideline, dealing with multiprovider networks, provides five new hypothetical examples; four deal with physician-hospital organizations (PHOs) and one involves a "messenger model." 355 The 1996 Guidelines generally describe "antitrust safety zones, which describe conduct that the Agencies will not challenge under the antitrust laws, absent extraordinary circumstances." 356 The Guidelines repetitively state that conduct outside the safety zones will not necessarily be challenged. 357 "Antitrust analysis is inherently fact-intensive... The statements outline the analysis the Agencies will use to review conduct that falls outside the safety zones." 358 The analysis adopted by the Agencies in the 1996 Guidelines is nearly always a rule of

352 Id. at 68-69.
353 Id. at 4.
354 See United States Dep't of Justice & Fed. Trade Comm'n, Statements of Antitrust Enforcement Policy in Health Care (Aug. 1996) (also available at <http://www.ftc.gov/reports/hlth3s.htm>). Although the words "per se" appears literally 21 times (including footnotes) in the Guideline, it is used in very limited circumstances: (1) A network that involves little or no integration among physician participants may be per se illegal if participants share price information or engage in boycotts or similar conduct; see id. at 4, 46, 82; (2) sharing of specific price or cost information outside that permitted by the Guidelines; see id. at 51; (3) An agreement that simply fixes the price each purchaser will pay is not a legitimate joint purchasing agreement; see id. at 54; (4) A price agreement or market allocation of integrated competitors is analyzed under rule of reason rather than per se rule if such agreement is reasonably necessary to accomplish pro-competitive benefits; see id. at 71, 107, 108; (5) A unilateral decision to eliminate a service is not a per se illegal market allocation; see id. at 112; (6) An agreement that facially appears to be the kind that would reduce output or increase prices, but is not per se unlawful, will be evaluated without an elaborate analysis of market definition and market power; see id. at 113; (7) Arrangements that minimize the costs of contracting between parties without collective determination of price or price-related terms are not per se illegal, see id. at 125, but if a third party engages in negotiations or decisions, such arrangements may be per se illegal as price fixing; see id. at 127. Several references to "per se" rules are simply within hypothetical situations described by the Health Care Guidelines. Id.
355 Id. at 5.
356 Id.
357 Id.
358 Id. at 5-6.
reason. Finally, the 1996 Guidelines set forth an expedited review procedure\textsuperscript{359} whereby the Department of Justice will issue business letters or the Federal Trade Commission will provide advisory opinions regarding potential antitrust problems of specific proposed activity by health care participants.\textsuperscript{360}

1. Tension Between Antitrust Precedent and Health Care Guidelines

\textit{a. Method of Analysis}

First, despite the historical fluctuation between the per se rule and the rule of reason, case law precedent in the area of price fixing suggests price fixing is per se illegal.\textsuperscript{361} Furthermore, in the health care arena and specifically with reference to price fixing by physicians, courts use per se rule analysis.\textsuperscript{362} Whether the courts' analysis is a forthright, quick, uncritical decision of per se illegality\textsuperscript{363} or an abbreviated rule of reason masquerading as a long version of per se analysis,\textsuperscript{364} the court has traditionally held that price fixing is illegal.\textsuperscript{365}

On the other hand, the routine mode of analysis adopted by the Department of Justice and the Federal Trade Commission in the 1996 Health Care Guidelines is clearly a rule of reason.\textsuperscript{366} The Guidelines' variation of the rule of reason, although different in some respects than what may be outlined in case law, is nonetheless a rule of reason analysis.\textsuperscript{367}

\textsuperscript{359} Id. at 6-7 (stating that the Agencies will respond within 120 days of receiving all required information for hospital mergers outside the safety zone, multiprovider networks, or non-merger health care matters; otherwise, the limit is within 90 days).

\textsuperscript{360} The business review procedure for proposed hospital mergers is authorized by 28 C.F.R. § 50.6 (1992); the business review procedure for other proposed health care activity is authorized by 58 Fed. Reg. 6132 (1993); the advisory opinion procedure for both proposed bank mergers and other health care activity is authorized by 16 C.F.R. §§ 1.1-1.4 (1993).


\textsuperscript{362} See Arizona v. Maricopa County Medical Soc'y, 457 U.S. 332 (1982).

\textsuperscript{363} See United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).


\textsuperscript{366} Review of each of the nine statements shows a rule of reason analysis, and as noted previously, per se rules are used only in very limited situations. See United States Dep't of Justice & Fed. Trade Comm'n, \textit{Statements of Antitrust Enforcement Policy in Health Care} (Aug. 1996) (also available at <http://www.ftc.gov/reports/hlth3s.htm>), supra note 354.

\textsuperscript{367} For example, the Health Care Guidelines permit price sharing among competitors with certain restrictions. See United States Dep't of Justice & Fed. Trade Comm'n, \textit{Statements of Antitrust Enforcement Policy in Health Care} 50 (Aug. 1996) (also available at <http://www.ftc.gov/reports/hlth3s.htm>). Any agreements that violate traditional antitrust case (e.g. price fixing or market allocation) must be reasonably necessary in order to achieve pro-competitive benefits. See id. at 71, 107, 108.
An excellent example of the Agencies' application of the rule of reason rather than per se rule is illustrated by the consent decree of United States v. Vision Service Plan.\(^ {368} \) Vision Service Plan ("VSP") is organized as a non-profit corporation conducting its business in 46 states by contracting with businesses, government agencies, health care insurers, and other organizations to provide pre-paid vision care coverage.\(^ {369} \) In turn, it contracts with doctors to provide those contracted services. Antitrust violations were alleged based on VSP's use of a most-favored nation clause\(^ {370} \) and its method of collection of data regarding charges by its panel of doctors.\(^ {371} \) In the final order of settlement, VSP was permitted to obtain usual, customary, and reasonable fee schedules from the panel doctors on a yearly basis and use that information to calculate the fee schedule it offers.\(^ {372} \) Although there was some contention over whether or not the VSP plan was controlled by the doctors or not,\(^ {373} \) the Antitrust Division made the following comment:

> Even if VSP were controlled by optometrists, as the states apparently believe they can prove, its setting of fees to its panel doctors, as an activity related to the offering of a separate and additional product – insurance – might in some [sic] circumstances be analyzed under the rule of reason rather than the per se rule . . . . VSP's fee-setting policies may be reasonably ancillary to its operation of a vision-care insurance plan, and, if so, they would be subject to the rule of reason analysis.\(^ {374} \)

The final decree did not challenge the VSP's method of using panel doctor's usual, customary and reasonable fees ("UCR") to set reimbursements, indicating therefore that a per se analysis was not used.\(^ {375} \) This result is in direct opposition to the stance of Arizona v. Maricopa County Medical Society.\(^ {376} \) "The anticompetitive potential inherent in all price-fixing agreements justifies their facial invalidation even if pro-competitive justifications are offered for some."\(^ {377} \)

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\(^ {370} \) Most-favored nation clauses, clauses which prevent a provider from charging a competitor of a contracting insurer less than the contracted insurer, reduce price competition by essentially setting a price floor on providers' rates.


\(^ {373} \) See Vision Service Plan, 61 Fed. Reg. 9487, 9488 (1996) (public comments regarding proposed revised final judgment). The issue of who controls the insurance plan, i.e. competing doctors or others, may be important in the analysis of whether there is a horizontal price fixing arrangement. See Hahn v. Oregon Physicians' Service, 868 F.2d 1022, 1027-1030 (9th Cir. 1988).


\(^ {376} \) 457 U.S. 332 (1982).

\(^ {377} \) Id. at 351.
b. Application of Method of Analysis

Under the Agencies' rule of reason analysis, four steps are involved: (1) Define the relevant market, i.e. relevant product and geographical market), (2) Evaluate the competitive effects of the arrangement, (3) Evaluate the impact of procompetitive efficiencies, and (4) Evaluate any collateral agreements. The middle two steps, an agreement among competitors is allowed if either: (1) the arrangement is not anticompetitive and has societal benefits in terms of improved health care quality or containment of health care costs, or (2) the arrangement is procompetitive “in the balance.”

The subtle distinction of allowing a competition-neutral arrangement if societal benefits are shown is, at least on a theoretical basis, beyond a traditional rule of reason analysis. A traditional rule of reason analysis looks only to the effect of an arrangement on competition and decides whether, based solely on the effect of the agreement on competition, the agreement is lawful or unlawful. The traditional rule of reason analysis relies completely on the conclusive presumption that competition is good for the market place and, hence, good for society. The Guidelines allow actions that may be anticompetitive as long as, on balance, they benefit the consumer.

The Agencies’ rule of reason analysis also differs from traditional analysis in other ways. First, if any price agreements exist, they are evaluated to determine if they are reasonably necessary to the arrangement in order to achieve the expected procompetitive effects. Second, any market allocation must also be

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378 See, e.g. UNITED STATES DEP’T OF JUSTICE & FED. TRADE COMM’N, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE 16-18 (Aug. 1996) (also available at <http://www.ftc.gov/reports/hlth3s.htm>) (describing in Statement 2 how the Agencies will evaluate the competitive effects of a hospital joint venture involving high-technology or other expensive health care equipment when such ventures fall outside the antitrust safety zone).

379 For example, a joint venture may reduce competition; however, it would be lawful under the Health Care Guidelines because it promoted cost savings to the consumer through efficiency and avoidance of duplicate expensive equipment. See Chicago Bd. of Trade v. United States, 246 U.S. 231 (1918) (stating the test of legality is “whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition”). Id. at 238.

380 The concept of “pro-competitive efficiencies” used in the Health Care Guidelines is consistent with the goal of consumer welfare espoused by ROBERT BORK, ANTITRUST AND MONOPOLY – THE GOALS OF ANTITRUST POLICY.

381 “The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promote competition, or whether it is such as may suppress or even destroy competition.” Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918).

382 As a result of this policy: “The Agencies have never challenged a joint venture among hospitals to purchase or otherwise share the ownership cost of, operate and market high-technology or other expensive health care equipment and related services.” UNITED STATES DEP’T OF JUSTICE & FED. TRADE COMM’N, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE 12 (Aug. 1996) (also available at <http://www.ftc.gov/reports/hlth3s.htm>).

383 For language limiting the rule of reason in price fixing circumstances to agreements “reasonably necessary” to achieve procompetitive benefits, see UNITED STATES DEP’T OF JUSTICE & FED. TRADE COMM’N, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE (Aug. 1996) (also available at <http://www.ftc.gov/reports/hlth3s.htm>). See id. at 72, 73, 75, 86, 107, 108, 131.
reasonably necessary. Finally, the Agencies’ rule of reason examines whether there are any collateral agreements that violate antitrust principles or policy, and, if they are also reasonably necessary to the agreement.

2. Result: Steadfast Illegality or “Procompetitive” Tolerance of Unlawful Behavior

The unfailing result from traditional case precedent is that the finding of horizontal price fixing is always illegal under the per se rule. Yet the Health Care Guidelines, while providing lip service to the per se rule, not only analyze facts based on a rule of reason, but also will allow horizontal price fixing within some limitations.

For example, if an arrangement such as horizontal sharing of price information by competitors is procompetitive or at least not anticompetitive and has some societal benefit, the arrangement will be evaluated to see if it has any “spillover effect” or collateral agreements that would be illegal. Finally, any price agreement that is not necessary for the attainment of the procompetitive effect is unlawful. But if these criteria are met, implicit price fixing by sharing of price information is lawful under this form of rule of reason analysis. Thus, there is clearly tension between the 1966 Health Care Guidelines and case law precedent.

In an attempt to ease this tension, the Guidelines contain several requirements. For example, horizontal sharing of price information should satisfy additional requirements:

1. Information must be collected by a third party;
2. Current information may be provided to purchasers, but information shared among competitors must be at least three months old; and,
3. At least five competitors must report data with no individual competitor representing >25% of the statistic on a weighted basis.

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385 For collateral agreements that would otherwise violate antitrust law to be allowable, they must be reasonably necessary to the main agreement. See id. at 4, 18, 19, 28, 36, 38, 81, 105, 113.
387 The price agreement must either be reasonably necessary for the consumer benefit or the price agreement must be collateral and reasonably necessary in order to carry out the main, pro-competitive agreement, e.g. a lawful joint venture.
389 Required criteria are: (1) sharing of price information is reasonably necessary to achieve procompetitive benefits; (2) any otherwise-unlawful collateral benefit or “spillover effect” is reasonably necessary. See id.
390 See id. at 44-45.
Such requirements are designed to minimize matching of price or cost data with any particular competitor. To the extent that the limitations avoiding sharing of specific price information that can be used to implicitly fix prices, the Guidelines are consistent with some case law.\textsuperscript{391}

The Guidelines remain at tension with case law holding that explicit or implicit sharing of any information that tends to stabilize prices is per se illegal.\textsuperscript{392} Certainly sharing of any price information within a localized market will tend to stabilize prices. The Guidelines permit such information even on a local basis.\textsuperscript{393}

For example, having national data that suggests the price for procedure A is on the average $100 and ranges from $80 to $120 across the country among 100,000 physicians surveyed is less likely to stabilize prices in an isolated rural community with 10 doctors compared with a local survey in the same community where data suggest the cost of procedure A averages $90 and ranges from $85 to $95. The average physician will find local information much more useful in dealing with local health care purchasers and may be willing to drop his price by $5 to be competitive, based on the local data, but not to drop his price to $80 based on the national data. The overall result of the price sharing may be increased competition that is desirable under the Guidelines, but the final result is still implicit price fixing.

The value of knowledge of local conditions in the market increases the threat of implicit price fixing; the smaller the locale, the greater the threat. The doctrine of parallel business decisions makes such behavior safe from prosecution as a conspiracy if the action is unilateral and independent.\textsuperscript{394} The point of this example is that, despite the safeguards in the Guidelines to prevent price fixing, they may still allow price stabilization that is clearly in violation of case law precedent. Not only do the Guidelines allow such arrangements, but encourage them based on procompetitive effect or even societal benefit in the absence of anticompetitive effect.

3. \textit{"Messenger Model"}

Another point of tension between traditional case law and the new 1996 Guidelines is in the area of communication of price information.\textsuperscript{395} Traditional

\textsuperscript{391} See American Column & Lumber Co. v. United States, 257 U.S. 377 (1921) (holding that sharing specific information is implicit price fixing). \textit{See also} United States v. Container Corp. of Am., 393 U.S. 333 (1969).


\textsuperscript{395} The Health Care Guidelines permit sharing of price information that is limited by the 3 criteria previously noted; however, traditional case law hold sharing of price information is either unlawful under a per se rule, \textit{see} Arizona v. Maricopa County Med. Soc'y, 457 U.S. 332, 351 (1982); or, unlawful under a rule of reason, \textit{see} United States v. Container Corp. of Am., 393 U.S. 333 (1969).
antitrust law has held the sharing of specific price information is per se illegal.\textsuperscript{396} On the other hand, within the ninth Statement dealing with multiprovider networks,\textsuperscript{397} the Agencies permit use of a “messenger model”\textsuperscript{398} which, of itself, may serve to ease tension with traditional case law.\textsuperscript{399}

The messenger clearly has only a role as a communicator of information on a vertical basis between insurer and provider.\textsuperscript{400} He cannot negotiate, nor give an opinion on a contractual issue.\textsuperscript{401} Furthermore, he clearly cannot allow information to be shared on a horizontal basis among competitors.\textsuperscript{402} Any decisions must be made independently and unilaterally by the physician.\textsuperscript{403} The stated goal is to facilitate communication and provide a cost savings.\textsuperscript{404} The “network” within which a messenger operates does not need to be integrated either financially or clinically.\textsuperscript{405} The most that a messenger seems capable of doing is gathering information of various contract offers from various insurers and presenting them simultaneously to a single physician/provider for his individual consideration and independent, unilateral action.\textsuperscript{406} Similarly, within the concept of a messenger model, a messenger should be able to gather information from individual physicians without disclosing to them their competitor’s information, and take the individual physicians’ information to insurers for their individual, unilateral consideration and independent action.\textsuperscript{407}

Several cases of collective bargaining by an IPA on behalf of member physicians have resulted in consent decrees.\textsuperscript{408} Illegal bargaining by PHOs has resulted in consent decrees.\textsuperscript{409} Occasionally the negotiating body has been a

\textsuperscript{396} See American Column & Lumber Co. v. United States, 257 U.S. 377 (1921).

\textsuperscript{397} See United States Dep’t of Justice & Fed. Trade Comm’n, Statements of Antitrust Enforcement Policy in Health Care 106 (Aug. 1996) (also available at \url{http://www.ftc.gov/reports/hlth3s.htm}).

\textsuperscript{398} Id. at 125.

\textsuperscript{399} Id. at 126.

\textsuperscript{400} See United States Dep’t of Justice & Fed. Trade Comm’n, Statements of Antitrust Enforcement Policy in Health Care 125-27 (Aug. 1996) (also available at \url{http://www.ftc.gov/reports/hlth3s.htm}).

\textsuperscript{401} See id. at 127.

\textsuperscript{402} See id.

\textsuperscript{403} See id. at 126.

\textsuperscript{404} See id. at 125-26.

\textsuperscript{405} "Some networks that are not substantially integrated use a variety of ‘messenger mode’ arrangements to facilitate contracting . . . ." Id. at 125.

\textsuperscript{406} See id. at 125-27.

\textsuperscript{407} See id.


professional trade organization like a medical society or an independent party who failed to follow the limitations of a messenger model, or even an ill-structured physician joint venture. Occasionally unlawful collective bargaining and/or price fixing agreements have involved other groups such as groups of private chiropractors, pharmacists, nursing homes, or hospitals.

The Colgate doctrine relieves tension between antitrust case law and messenger model, allowing the messenger model to be a beneficial, “procompetitive” tool for relaying information between parties of a contract. Similarly, physician unions can be a beneficial tool for negotiation between parties; however, in order for physician unions to work effectively, they need exemption from antitrust. Such exemption may be either legislative or judicial.

IV. ADVOCACY FOR PHYSICIAN UNIONS

A. Contract Principles Mandate More Equality of Bargaining Power

The first argument in favor of allowing physicians to collectively bargain is based on the fact that the physician is, in reality, involved in an oppressive contract situation with an insurer that has such superior strength in an unequal bargaining situation as to make enforcement of such contracts unconscionable. In essence the insurer-physician contract is an adhesion contract, defined as:

Standardized contract form offered to consumers of goods and services on essentially “take it or leave it” basis without affording consumer realistic

417 See United States v. Colgate & Co., 250 U.S. 300 (1919) (holding that a manufacturer has the right to exercise his own independent discretion as to parties with whom it will deal and the circumstances under which it will deal).
opportunity to bargain and under such conditions that consumer cannot obtain desired product or services except by acquiescing in form contract. Distinctive feature of adhesion contract is that weaker party has no realistic choice as to its terms.420

A popular contracts hornbook explains why such a contract is unconscionable:

Superior bargaining power is not in itself a ground for striking down a resultant contract as unconscionable. There must be additional elements, as for example, a lack of meaningful choice as in the case of an industry wide form contract heavily weighted in favor of one party and offered on a take it or leave it basis, or a situation where freedom of contract is exploited by a stronger party who has control of the negotiations . . . .421

The following discussion will explain how physician contracts are typically non-negotiated form contracts clearly favoring insurers, presented functionally on a "take it or leave it basis," and in a situation of markedly disproportionate bargaining power.422

1. Physicians Have No Bargaining Power – Economic Analysis and Practical Experience

In a market where an insurer has significant market power, in terms of market share, a physician has limited ability to change a contract.423 Furthermore they cannot, in practicality, terminate a contract.424 For example, the Antitrust Division, in forcing a divestiture of Aetna in the Dallas and Houston markets as part of approval of the merger of Aetna and Prudential, noted the anticompetitive effect upon physicians if Aetna were allowed to continue its position of dominance in those geographical areas.425

Physicians, however, generally have only a limited ability to encourage patients to switch health plans . . . . To retain a patient after terminating a plan requires the physician to convince the patient either to switch to another employer-sponsored plan in which the physician participates . . . or to pay considerably higher out-of-pocket costs . . . .426

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423 Id. See also Jacob, Rhode Island Doctors, supra note 146, at 21.
The United States in that case also alleged that the "acquisition would enable Aetna to unduly depress physicians' reimbursement rates in Houston and Dallas, resulting in a reduction of quantity or a degradation in quality of physicians' services in those areas." The conclusion can be inferred that based on market power of insurers, physician reimbursements may be decreased and physicians cannot, in reality, decline those contracts.

The Aetna example is also important because Aetna contracts typically contained an "all products clause." Such a clause "requires physicians to participate in all of Aetna's current and future health plans as a precondition to participating in any current Aetna health plan." The consequence of such a clause is that it significantly increases the bargaining power of an insurer; if a physician decides not to participate in one Aetna product (e.g. HMO), he may lose a significant volume of business from other products (e.g. PPO). Furthermore, if the insurer later adds a product that the physician finds intolerable (e.g. a highly discounted product or a high-risk product like a capitation plan), he is powerless to not participate, lest he breach his contract or, worse, lose the volume of business in all other products. Ironically, an "all products" clause in a North Carolina state employee health coverage contract caused eight of eleven HMO's to withdraw from coverage of the state's employees, and resulted in a temporary shift of those employees covered by the withdrawing HMOs to indemnity plans. The case represents the HMOs getting a taste of their own medicine!

Other typical but onerous contract clauses include, "medical necessity" clauses, "hold harmless" clauses, "unilateral amendment" clauses, and "penalty" clauses. The problem with medical necessity clauses is described in a public comment on the Aetna-Prudential merger by the Medical Association of Georgia wherein it cites Congressional testimony of Linda Peeno, M.D., a former medical executive for several managed care companies:

[She] stated that "the definition of 'medical necessity' is the 'smart bomb' of managed care. [M]anaged care companies can appear to offer all sorts of options and decision-making power ... but as long as they retain control of what is, and what is not, medically necessary, they have unfettered control over what medical treatment they will pay for ..."

"Hold harmless" clauses have been used in an attempt to decrease insurers' medicolegal liability. "Unilateral amendment" clauses serve to allow insurers

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428 Id. at 66652.
429 Id. at 66650.
430 Id. at 66652-53 and 66657.
431 Id.
434 Id. at 66653.
435 Id.
to change condition of the contracts by simple notification by the insurer to the provider, without express agreement by the provider. 436 "Penalty clauses" are often intended to be punitive, have the effect of being punitive, or bear no relation to the alleged wrongdoing of providers. 437 For example, if a physician renders treatment without preauthorization required by a contract, he likely will not be paid for his services, even if the treatment was clearly appropriate and otherwise would have been covered by the plan. Such clauses, generally, and conduct, specifically, are against general contract principles of good faith and fair dealing. 438 Finally, "gag clauses" are onerous clauses frequently included in a physician's contract. 439

A prime example of the disparate bargaining power is the fact that physicians frequently are not informed of what the fee schedule is for reimbursements nor how that schedule is computed:

[H]ealth plans, whose market clout often makes them a must to sign up with, typically won't tell the doctors what they can expect to be paid until after a contract is signed. Plans are also often vague or silent about how payments are determined. It's a system designed to help insurers by keeping doctors in the dark, unaware of whether they are being treated fairly or not. 440

A recent case on point is Medical Association of Georgia v. Blue Cross & Blue Shield of Georgia, Inc. 441 The insurer contracted with Georgia physicians to pay them based on the usual, customary, and reasonable fee ("UCR"). 442 Such fee schedule is typically based on physicians' charges. 443 In accordance with a clause allowing unilateral change of reimbursement by the insurer upon 30 days prior notice, Blue Cross changed the meaning of UCR to be based upon the fees physicians had actually received for their services. 444 The plaintiff's contention that the insurer had breached a duty of good faith was rejected by the appellate court, finding that Blue Cross "did nothing more than what the contracts and rules expressly allowed." 445 However, the plaintiff also claimed that the terms of the contract regarding reimbursement were unascertainable because Blue Cross refused to divulge either the fee schedule or how the reimbursements were calculated. 446 The court agreed:

436 Id.
437 Id. at 66654.
439 Gag clauses preclude physicians from discussing with patients or the public the onerous nature of an insurer's policy; detrimental aspects of policy provisions with regard to care or quality; or, otherwise speaking out against an insurer.
440 Court to Health Plan, supra note 38, at 23.
442 Id. at 185.
443 Id.
444 Id.
445 Id. at 186.
446 Id.
Blue Cross’ refusal to provide participating physicians with a fee schedule and the precise methodology used to determine the uniform, customary, and reasonable fee for services is improper. A promise of future compensation must be for an exact amount or based upon a formula or method for determining the exact amount, and that amount or formula should be ascertainable from the contract. Without such fee information, there is no way for doctors to calculate for themselves whether they have been fully paid for a particular service. Such information is critical to the doctors so that they can ensure that Blue Cross is fulfilling its obligations under the contracts.

The logical course of action for physicians who disagree with provisions of a contract seems to be either negotiate for different terms, or simply not participate in the insurer’s plan. Negotiation of terms might be the ideal action if time permitted such negotiations and insurers were amenable to negotiation; however, experience shows such option is futile. Clearly, the least time consuming and most effective method of avoiding onerous contracts is simply not to participate. Non-participation is simply not an option when plans constitute a significant portion of a physician’s income.

In addition to the example of Aetna’s market share in Houston and Dallas, other consent decree cases have pointed to the harsh effect on physicians who try to or cannot avoid onerous contracts. The rationale is clearly illustrated by cases involving “most favored nation” (“MFN”) clauses. The cases consistently show that a provider will not violate the MFN clause and give more discounted fees to non-contracted insurers or other parties, for fear that the provider will suffer significant economic loss by the contracted insurer’s enforcement of the MFN.

For example, in United States v. Delta Dental of Rhode Island, the MFN clause was in violation of antitrust law because it tended to stabilize prices, stifled competition among insurance providers, caused some market participants to exit the market, and prevented new market entrants. The reason such MFN clauses are anticompetitive is based on their effect on providers’ salaries. In the case of Delta Dental of Rhode Island: “Delta provides so much more of dentists’ income than would any entering managed care plan that if these dentists were to reduce their fees to such plans, the resulting reduction in their income from Delta would be much greater than their added income from the

447 See Medical Ass’n of Georgia, 536 S.E.2d at 186.
448 Obvious time constraints have an adverse affect on the ability of individual physicians to negotiate contracts, especially in markets where numerous insurers are active. Authorized third party negotiations through physician unions has obvious time savings over the 1996 messenger model, whereby the third-party can do nothing but transfer information back and forth.
449 One example is Aetna’s stance that its “all products” policy is non-negotiable. See Aetna Inc., 64 Fed. Reg. 66647, 66657 (1999).
450 “Most favored nations” clauses are any clauses that serve to guarantee the contracting insurer that the physician (or other provider in the case of a hospital, dentist, etc.) will not charge any other insurer or self-paying patient a lower fee than the contracting party pays.
452 “[D]elta’s MFN clause brought about the collapse of the Dental Blue PPO . . . .” Id. at 9810.
453 Id.
entrant plan." Although Delta Dental was the largest dental insurer in the state, it provided insurance to only 35-45% of residents, it contracted with over 90% of the dentists and accounted for a substantial percentage of their incomes.

The same situation, result, and rationale occurred in United States v. Oregon Dental Service ("ODS"). A MFN clause precluded dentists (who received a substantial part of their income from ODS's contracted plan) from discounting their fees to non-ODS patients or competing dental care plans because the cost in terms of income was too great to justify discounting.

A similar case is United States v. Vision Service Plan ("VSP"). "Since many VSP panel doctors . . . receive a significant portion of their professional income from treating VSP patients, they have found that discounting their fees . . . to non-VSP patients . . . and consequently reducing their income from VSP by virtue of the MFN clause, is unprofitable." Other cases have also illustrated the same effects of MFN clauses.

The key is not whether the insurer is a dominant player in the market, but rather to what extent a physician's income will be affected by the loss of that insurer's contract. If, for example, an insurer controlled 99% of a geographic market, but the physician's business was only 1% based on that controlling insurer, dropping the contract would likely have little effect on the physician's income, i.e. only 1% decrease. However if a plan controls only 1% of the market, but it constitutes 100% or even only a "substantial part" of the physician's income, he is not likely to drop the contract. What represents a "substantial part" of a physician's income is determined by the physician.

In today's health care market three other facts are clear. First, the rationale for accepting discounted fees, is based on an expectation for the loss of income to be offset by an increased volume of business. Second, an understanding of the relationship between price and marginal cost is critical. Finally, the health insurance market is becoming increasingly concentrated.

The first reality is that one must accept discounted fees in order to compete in the market. The rationale of the present system is explained in United States v. Morton Plant Health Systems, Inc., a consent decree case involving a proposed hospital merger:

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454 Id. at 9809.
455 Id.
457 Id.
459 Id. at 5215.
461 The behavior of physicians to increase volume in order to offset discounted fees is the rationale for HCFA's reduction of Medicare fees. See Brown, What Surgeons Should Know, supra note 193, at 8.
These [managed care] plans contract with a select number of competing hospitals and employ financial incentives to encourage plan enrollees to use the contracted facilities. Hospitals reduce the prices of services provided to managed care plan enrollees in return for the plans' commitment to increase the volume of patients hospitals receive. Managed care plans . . . rely on competition among hospitals to obtain hospital services at competitive rates.463

Although the example uses hospitals, any provider, including physicians could be substituted in the example. The discount for volume exchange fails in only two ways: (1) demand exceeds supply, i.e. provider is too busy to accept further increased work, or (2) the law of diminishing returns, the provider decides that further increased volume is not worth the discount in price. Examples illustrating the first limitation are: refusal of primary care physicians to take in new patients, shortage of physicians in certain geographical areas, or shortage of particular specialists. Examples of the second limitation include situations where a physician may be spread too "thin" that further work is less valuable than personal time off, desire not to take call, cover emergencies, tax consequences of further income, etc. The other pertinent example is if the cost of doing business (marginal cost) is not sufficiently offset by the income (price).

Second, as the marginal cost approaches the price paid, the profit will decrease. The concept of marginal cost and price are critical to the understanding of when a physician considers a particular contract to be important as a "substantial" part of his total income. When fees become so discounted that a contract is not profitable, i.e. marginal costs are greater than or equal to price, physicians will drop contracts.464 (Managed care companies followed the same economics by dropping managed care products for Medicare.465 Hospitals follow the same economic principle.)466 Based on the same rationale, physicians are likely to drop the least profitable contract before the more profitable one, as long as such a decision does not substantially affect their income.

Long-term effects upon society include decrease in quality and availability of health care, loss of existing physicians to other professions, loss of future applicants to become physicians, etc. A recent report in the Journal of the American Medical Society does show a recent trend in the decrease of applicants to medical school.467 The total number of applicants peaked in 1996 and has dropped by 8.4%, 4.7%, and 6.0% in each successive year.468 More importantly, the number of applicants per available opening in medical school has decreased

463 Id. at 35756.
464 Practices across the nation are beginning to drop contracts because the cost to the physicians exceed the reimbursements. See Page, Doctors Find Bargaining Clout, supra note 147, at 1.
465 See Landers, Medicare Managed Care Plans Drop Seniors, supra note 108, at 8.
466 See Cheryl Jackson, Doctors Dangle as Hospitals Jettison Money-Draining HMOs, AM MED. NEWS, Aug. 28, 2000, at 1.
467 See Barbara Barzansky, Educational Programs in U.S. Medical Schools, 1999-2000, 284 J. AM. MED. ASS'N 1114 (2000).
468 Id. at 1115-16.
from 2.7 in 1996 to 2.2 in 1999.\textsuperscript{469} Also, 31\% of the attrition in 1999, was due to "personal reasons or a desire for a career change."\textsuperscript{470} Finally, of those who graduated in 2000, 1.7\% did not plan to enter residency programs.\textsuperscript{471} A recent study of attrition in medical school graduates who started a surgical residency in 1993 showed the rate of attrition overall to be 11.5\%, but of those, about 19\% left the field of medicine altogether and nearly 81\% switched to a non-surgical field.\textsuperscript{472} Studies also show an increasing number of physicians are retiring, often earlier than would be expected, and dissatisfaction with managed care hassles is a significant factor in the decision to retire.\textsuperscript{473}

The third pertinent fact of today's health care market is that the ongoing trend is toward a concentration of the insurers, i.e. fewer insurers controlling increasing shares of the market.\textsuperscript{474} As insurers merge and larger companies acquire smaller ones, there are fewer insurers, each controlling a substantial portion of the market.\textsuperscript{475} A physician is likely to have fewer insurers with which to contract and those contracts are likely to represent larger proportions of his total income. Hence, because the physician determines what is "substantial," he is not likely to drop a contract that represents a substantial portion of his income especially in today's market where fewer insurers control a larger "piece of the pie."

In summary, today a physician must accept discounted contracts in order to compete in the market place. He will discount his prices as long as he trades loss of income from discounts for increased income due to a higher volume of business. He will no longer trade discounts for volume when either he reaches a point of diminishing returns (e.g. no longer profitable) or his capacity to work is reached (demand exceeds supply). He is the one who decides when loss of a contract is "substantial" in terms of his income, but in today's market where fewer insurers control larger portions of the market any contracts with which the physician deals are likely to be "substantial" in terms of their share of his income, especially as he operates on a diminishing profit margin. In the final analysis, a physician simply cannot bargain with an insurer by not participating in a proffered contract.

In reality he has no significant bargaining power as an individual physician. An exception would be if the physician supply was such that an insurer's demand for contracted physicians could not be met (for example, not enough doctors existed in a given market or a currently contracted physician carried such a load of patients that the insurer could not provide sufficient coverage if that

\textsuperscript{469} Id. at 1116.
\textsuperscript{470} Id.
\textsuperscript{471} Id.
\textsuperscript{473} See Jay Greene, Physicians Enticed Into Early Retirement, AM. MED. NEWS, Nov. 6, 2000, at 13. See also Greene, Businesses Lure, supra note 211, at 13.
\textsuperscript{475} Id.
busv doctor dropped out of the plan), then the additional loss of the individual physician might be significant.\textsuperscript{476} Otherwise, the loss of an individual physician is absorbed into the supply of available contracted physicians or new physicians are contracted to replace the lost physician. Thus, physicians have no significant bargaining power as individuals.\textsuperscript{477}

Unfortunately, collective bargaining frequently runs afoul of current antitrust law including the healthcare enforcement policies, despite physicians’ motive to protect patients and negotiate reasonable contracts rather than to fix prices.\textsuperscript{478} In an antitrust challenge, physicians may have to settle just to avoid legal costs.\textsuperscript{479} For example, “Dr. Cobden [president of the defendant organization, Alaska Healthcare Network] said the physicians agreed to settle, which is not an admission of guilt, to avoid court costs that could reach $400,000 to $500,000.”\textsuperscript{480}

2. \textit{Medicare Sets a Benchmark for Insurers to Fix Prices}

The setting of allowable rates by Medicare, combined with the lawful distribution and widespread publication of those rates has provided a convenient, irresistible means for insurers to fix prices they will offer contractually to providers.\textsuperscript{481} Such is not necessarily the intent of such provisions, but in practicality is the result. This strain of principle and practice is described in \textit{United States v. Vision Service Plan}:

\textit{[N]othing in the Judgment should be construed to prevent VSP from gathering fee information required by Medicare or Medicaid, while precluding VSP from using that fee information in setting the fees that VSP pays its panel doctors for providing services to VSP patients not covered by Medicare or Medicaid programs.}\textsuperscript{482}

To the contrary, evidence suggests insurers base their own fee schedules on Medicare’s. “The Medicare fee schedule stretches beyond Medicare. Numerous insurance carriers now adopt the fee schedule and implement their own payment policies using MFS [Medicare fee schedule] as its base.”\textsuperscript{483} Information not reflected in the opinion in \textit{Medical Ass’n of Georgia v. Blue Cross & Blue Shield of Georgia, Inc.} confirmed that the insurer used Medicare’s fee schedule to

\textsuperscript{476} See Page, \textit{HMO Sues}, supra note 22, at 22.


\textsuperscript{479} \textit{Id.}

\textsuperscript{480} \textit{Id.}

\textsuperscript{481} See United States v. Container Corp. of Am., 393 U.S. 333 (1969) (stating that the implicit sharing of price information is unlawful price fixing). \textit{See also} American Column & Lumber Co. v. United States, 257 U.S. 377 (1921) (holding that the sharing of specific price information is unlawful). Use of published Medicare fee schedules by insurers to set their respective fee schedules is analogous to unlawful implicit sharing of specific price information.


\textsuperscript{483} Opelka, \textit{In Their Own Words}, supra note 183, at 39.
develop their own. A spokesman for Blue Cross said: "Blue Cross relies on a combination of Medicare rates and the company's own payment experience, but the exact payment methodology is proprietary information that the company does not want competing physicians or its doctors to know." The AMA and the Medical Society of the State of New York also filed a suit in March 2000, over methodology of fee calculations by Metropolitan Life Insurance Company.

In June, 2000, the New York State Dept. of Health requested that Capital District Physicians' Health Plan Inc., a 200,000 member physician-managed HMO, divulge its fee schedule, but as of October 9, 2000 it had failed to do so. Such requests to divulge fee schedules have not met with success in other areas. For example, the Kentucky Supreme Court ruled against the public disclosure of health insurer's fee schedules at insurance rate hearings. On one hand, insurers claim disclosure violates antitrust laws and, on the other hand, physicians claim a contractual right to know material terms of the contract.

Keeping in mind that insurers generally follow the lead of Medicare, the long-term affect of decreased reimbursements will likely be an affect on quality. Inability to meet patient demands and provide appropriate employee work environment and wage structure changes the quality of personnel available throughout the industry and ultimately affects quality of care. If the health care industry cannot keep pace with changes in the consumer price index or inflation, good employees will seek other opportunities, resulting in staff shortages. Surgical practices have pared down their office staff. Ultimately, care from physicians and their office personnel becomes sub-optimal.

B. Physician Unions May Be Procompetitive and, Therefore, Lawful

One factor that is imperative in the judgment of physician unions is that they must be analyzed under the rule of reason, rather than being considered per se illegal. Courts and antitrust enforcement agencies should not "throw out the

484 See Court to Health Plan, supra note 38, at 23.
485 Leigh Page, Georgia Court Upholds Physicians' Right to Know Payment Rates, AM. MED. NEWS, Jul. 31, 2000, at 1.
486 Id.
488 See United Medigroup, Inc. v. Hughs, 952 S.W.2d 195 (Ky. 1997).
491 Id.
492 See Opelka, In Their Own Words, supra note 183, at 39.
493 The Court in Broadcast Music, Inc., implied that a rule of reason is the default analysis: "[T]he Court has held that certain agreements or practices are so 'plainly anticompetitive' and so often 'lack . . . any redeeming virtue,' that they are conclusively presumed illegal without further examination under the rule of reason generally applied in Sherman Act cases." Broadcast Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 8 (1979) (emphasis added). See also, Justice Powell's dissent in Maricopa:
baby with the bath water.” Initially, physician unions must be envisioned as units capable of achieving efficiencies in health care, rather than as naked price fixing arrangements. Analysis of physician unions under a rule of reason is entirely consistent with both the 1996 Health Care Guidelines and with prior case law precedent.494

Furthermore, physician unions are lawful under a rule of reason if either (1) they are procompetitive or (2) are not significantly anticompetitive and provide some beneficial efficiencies. Restoring contracting power to physician providers via collective bargaining is procompetitive. Under the present system, insurers may offer competitive premiums, but they “squeeze” reimbursements to providers under the guise of promoting “efficiency” when in reality that is the easiest way to reduce costs, especially since physicians are essentially powerless to negotiate. As a result, providers are dissatisfied; some leave the field of medicine; financial “disincentives occur;” and, in the end, quality of care suffers. Permitting collective bargaining by physicians can potentially reverse the deleterious effects of managed care.

First, physicians in unions sharing opinions on how to provide cost-efficient, high quality care, and sharing necessary data including costs of health care delivery and price information can deal more knowledgeably and negotiate more effectively with insurers. One advantage to the collective bargaining arrangement, rather than the “integrated” physician joint venture models described in the 1996 Health Care Guidelines, is that the physicians can participate in a physician union without a lot of up-front, high risk in terms of capital investment or risk sharing. Physician unions can accomplish the same procompetitive effects without the risk of establishing expensive, and often inefficient, infrastructures of IPAs, PHOs, etc. For example, by negotiations with insurers, physicians may gain access to important actuarial data of the patient population so that the physicians can safely and fairly negotiate a capitated reimbursement plan. Similarly, the physicians and insurers may share quality control data and utilization data so that together greater efficiencies may be achieved. Such efficiencies are less likely to be achieved in a “take-it-or-leave-it” situation of gross inequality in bargaining positions.

Not all the activity of physician unions is likely to be geared toward price. Negotiations undoubtedly will involve onerous contract clauses that have heretofore been non-negotiable. Contractual negotiation to remove such clauses is likely to be much more effective than lobbying efforts on the part of medical

Only if it is clear from the record that the agreement among physicians is “so plainly anticompetitive that no elaborate study of [its effects] is needed to establish [its] illegality” may a court properly make a per se judgment. And as our cases demonstrate, the per se label should not be assigned without carefully considering substantial benefits and procompetitive justifications. This is especially true when the agreement under attack is novel, as in this case.


groups and non-physician advocacy groups. In all likelihood, collective bargaining by physicians will also be beneficial to patients, since physicians have traditionally been patient advocates. History supports the viewpoint that physician and patient interests are much more closely aligned than are those of insurers to either physicians or patients.

By effective negotiating strength as a group, unions may prevent some doctors from loss of contracts or deselection by insurers. Keeping such physicians in the market is pro-competitive on the basis of number of competitors as well as the consumer benefits of increased access and choice of their doctors. Some insurers currently only offer certain contracts to provider groups with a minimum number of doctors. By physicians banding together, those contracts are potentially available to a greater number of doctors – thus physician unions may be procompetitive in terms of creating a market for individual doctors or small groups who would otherwise not be able to get those contracts.495

Second, the physicians in unions will continue to compete for the best insurance contracts with other physicians not in their union as well as other unions. Furthermore, if the unions are non-exclusive, the unions will even compete against its own physicians who can deal and contract with the insurers individually.

Through contract negotiations, unions may be able to gain access for physicians to other products – an effect similar to “any-willing provider” legislation, but at less cost and effort than the political process requires. The upshot of increased numbers of doctors on managed care panels is that it will actually increase competition and improve patients’ options of choosing a physician. Any effect that increases the number of physicians available to the consumer is, in fact, procompetitive.

Third, and most importantly, insurers will increase competition with one another. Once physicians have some true bargaining power through collective bargaining, insurers will have to be more competitive with one another in order to negotiate providers’ contracts: insurers will compete to get the best quality group of doctors who are the “best buy for the money” and the most efficient. Such qualities will appeal to the consumers who want to pay the least premiums, but not at the sacrifice of quality of care.

Collective bargaining by physicians is analogous to a legal “tying” arrangement. The United States Supreme Court in Jefferson Parish Hospital District No. 2 v. Hyde,496 stated:

It is clear, however, that every refusal to sell two products separately cannot be said to restrain competition. If each of the products may be purchased separately in a competitive market, one seller’s decision to sell the two in a single package imposes no unreasonable restraint on either market, particularly if competing supplies are free to sell either the entire package or its several parts . . . . Our cases have concluded that the essential characteristic of an invalid tying arrangement lies in the seller’s exploitation of its control over the tying product

to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms.\textsuperscript{497}

A physician union selling services of its member physicians as a package is like selling another product as a package. If the combined product (services of several physicians) is sold in a competitive market, i.e. a market where according to 1996 Health Care Guidelines no more than 20% of physicians are participants if the arrangement is exclusive or no more than 30% of physicians are participants if the arrangement is non-exclusive, then the buyer (insurer) has alternatives. Alternatives for the insurer/buyer include (1) dealing with member physicians on an individual basis, or (2) dealing with other, similar physicians on an individual basis, or (3) dealing with other physician unions. The fact that the insurer may deal with a single “seller,” i.e. the physician union, for all its needs holds advantages in terms of decreased time and direct costs of dealing individually with physicians. Likewise, costs of individual negotiations are saved also by the physicians. Such efficiency of time and communication cost is recognized also within the “messenger model” under the 1996 Health Care Guidelines; however, the messenger’s role is extremely limited under that model.

As long as the physician union is not forcing the insurer to buy its tied product by exploitation of control, the “tied product” is lawful. Assuming all physicians joined a union and that each union is limited to include only 20% to 30% of the market’s physicians (depending on whether the union is exclusive or non-exclusive), there must be at least three to five alternatives for the insurer to contract with. \((100\% = 30\% \times 3 + \text{or}, 100\% = 20\% \times 5)\). Therefore, even if negotiations are unsuccessful or if an unlawful boycott occurred with one union, the insurer would have alternates in terms of other groups. Thus, under an analogy of a “tying” arrangement, collective bargaining is lawful as long as market power is limited.

C. Legislatures and Courts, in Response to Changing Social Conditions, Should Permit Physician Unions

The overpowering nature of managed care insurers requires adaptation of antitrust laws to permit collective bargaining by physicians in order to protect consumers and physicians. Both Congress and the Courts have a rich history of adapting law to meet the needs of a changing society. Antitrust law is no exception.\textsuperscript{498} Changes in antitrust law have reflected adaptation to social conditions.\textsuperscript{499}

\textsuperscript{497} \textit{Id.} at 11-12.

\textsuperscript{498} See \textit{ANDERSEN, ANTITRUST LAW, supra} note 223, at v which states:

Change remains the norm in antitrust law, although sometimes in seemingly contrary directions. Government enforcement during the Clinton years has been aggressive and often high profile. Hard-core antitrust offenses such as price fixing and bid rigging now bring multimillion dollar fines and prison terms . . . . In contrast, the federal judiciary appears to be becoming more focused on narrowly defined competitive injury as antitrust’s sole concern. The rule of reason continues to expand, while the per se categories contract. Some offenses which the courts continue to label per se offenses (such as tying) are hard to distinguish from conventional rule of reason cases. The courts are increasingly using the “quick look” rule of reason to see if a full-blown rule of reason inquiry is even necessary . . . . Private class action suits are on the upswing, just
1. Judicial (Non-statutory) Exemptions to Antitrust Law

Judicial construction, under guise of a rule of reason, has created a couple of non-statutory exemptions to antitrust law. For example, in *National Collegiate Athletic Ass'n v. Board of Regents of the University of Oklahoma*, horizontal price-fixing and output restriction, normally condemned as a per se violation, were permitted. "Rather, what is critical is that this case involves an industry in which horizontal restraints on competition are essential if the product [intercollegiate competition] is to be available at all." Likewise, in *Broadcast Music, Inc.*, the Court created a "new product exception" to antitrust law.

The ultimate example of non-statutory, judicial exemption of antitrust law is professional sports, particularly baseball. In 1922, the United States Supreme Court held that baseball was exempt from antitrust because it was not interstate commerce. Although later cases recognized that professional baseball is engaged in interstate commerce, the judicially-created baseball exemption continued on the basis that Congressional inaction in response to *Federal Baseball Club of Baltimore, Inc. v. National League of Professional Baseball Clubs* and the principle of stare decisis upheld baseball's immunity. The unique nature of professional sports has continued to be problematic for courts and is an area of well-recognized non-statutory exemption.

—as the total number of private suits appears to be in decline. With the merger wave of the late 1990s, the government reviewed an unprecedented number of mergers, successfully challenged several, and was criticized for not challenging more.

*Id.* at v.

499 An example illustrative of the adaptation of antitrust law to the rapidly changing health care environment is the FTC's modification of a 1976 Consent Order upon petition by the American Academy of Orthopaedic Surgeons, 60 Fed. Reg. 30542 (1995). The American Academy of Orthopaedic Surgeons had circulated a relative-value scale of orthopedic services amongst its members and according to the 1976 consent decree were illegally price-fixing. American Academy of Orthopaedic Surgeons, 88 F.T.C. 968 (1976). The order was modified in 1985 to permit the Academy to discuss relative-value scales with the government and with third-party payors. See 105 F.T.C 248 (1985). After Congress enacted Medicare's resource-based relative-value scale, the FTC again modified the Consent Order due to changed conditions in the health care industry that made the previous orders inequitable.

500 With even less finesse the court has responded to challenging social conditions in the Great Depression era, by *Appalachian Coals*, a case that can only be seen as extreme compared to other case law. See Appalachian Coals, Inc. v. United States, 288 U.S. 344 (1933).


502 *Id.* at 100-101.


506 259 U.S. 200 (1922).

507 See ANDERSEN, ANTITRUST LAW, *supra* note 223, at 942.

These examples of non-statutory exemptions are important for their effect on application of antitrust in situations where Congress has not spoken. Judicial exemption, perhaps under a rule of reason, is one potential way to provide physicians antitrust relief for collective bargaining.

2. Legislative Responses to Changing Social Conditions

The following examples provide evidence of legislative modification of antitrust law. Some responses have been temporary measures whereas others have been long-term exemptions from antitrust law.

First, the Sherman Act itself was enacted in response to the need for public protection from the great railroad cartels and trusts. An analogy to contemporary managed care insurers comes to mind when reading Representative Kelly's 1914 address to Congress:

Enterprises with great capital have deliberately sought not only industrial domination but political supremacy as well. Great combinations of capital for many years have flaunted their power in the face of the citizenship, they have forced their corrupt way into politics and government, they have dictated the making of laws or scorned the laws they did not like, they have prevented the free and just administration of law. In doing this they have become a menace to free institutions, and must be dealt with in patriotic spirit, without fear or favor.

Like the great trusts of the past, ever-consolidating, profit-oriented insurance companies today have, to the detriment of consumers, controlled decisions of providers who are powerless to negotiate their contracts, heavily attempted to influence legislation designed to abrogate evils of managed care, and scorned the laws they do not like.

Another example of Congressional response to the perceived needs of society was the Year 2000 Information and Readiness Disclosure Act that provided antitrust exemption for sharing of information to prepare for the

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511 Id. at 297.

512 See supra text accompanying notes 126-43, under the section Control of Delivery of Health Care and Control of Resources of this article.

513 See supra text accompanying notes 422-79, under the section Physicians Have No Bargaining Power — Economic Analysis and Practical Experience of this article.

514 For example, heavy lobbying in the 2000 election prevented passage of a Massachusetts' initiative to adopt universal health coverage. See Landers, Universal Health Care, supra note 155, at 5.

515 For example, health insurance companies frustrate portability statutes by increases in premiums by 140% to 600% over standard premiums. See Health-Insurance Law, supra note 176, at B5. Still another example is the action of insurers to frustrate the intent of prompt-payment laws. See Page, "Clean Claim," supra note 176, at 1. See also Page, Prompt-Payment Laws, supra note 176, at 16.
perceived Y2K problem.\textsuperscript{516} Others include the Small Business Act\textsuperscript{517} and the Newspaper Preservation Act.\textsuperscript{518} Still other amendments to antitrust laws in the past have been temporally applicable to socioeconomic conditions, but have been subsequently repealed.\textsuperscript{519} Congress clearly makes exception to antitrust law, based on socioeconomic conditions.

Congress has passed numerous exemptions to the antitrust laws in response to perceived needs of market participants. The labor exemption of §6 of the Clayton Act\textsuperscript{520} was perceived as inadequate to protect agricultural cooperatives.\textsuperscript{521} The Capper-Volstead Act\textsuperscript{522} was adopted particularly to provide relief for farmers who had no individual ability to deal with market conditions including the power of processors and distributors to control profits.\textsuperscript{523} "Congress hoped to bolster their [farmers''] market strength and to improve their ability to weather adverse economic periods and to deal with processors and distributors."\textsuperscript{524} The relationship of physicians to insurers today is analogous to farmers and processors/distributors at the time of passage of the Capper-Volstead Act. Like farmers, physicians have no individual market power and are under control of insurers. Like farmers, many physician groups are unable to "weather" current economic conditions of the market.\textsuperscript{525}

Like the Capper-Volstead Act, the Fisherman's Collective Marketing Act\textsuperscript{526} provides antitrust exemption for fishermen.\textsuperscript{527} "[T]he two Acts provide exemptions from antitrust liability for essentially the same activities, the primary difference being the fact that one Act applies to the agricultural industry and the other to the fishing industry."\textsuperscript{528}

\textsuperscript{517} See Small Business Act, 15, U.S.C. §638 (1997) (permitting small businesses to engage in joint ventures of research and development on that basis that such ventures promote free enterprise and are good for the national economy).
\textsuperscript{520} The Clayton Act provides that antitrust laws are not applicable to labor organizations. See 15 U.S.C. § 17 (1997).
\textsuperscript{524} Id. at 826.
\textsuperscript{525} For example, in California thirteen IPAs have failed financially in the past five months. See Page, California Doctors, supra note 97, at 14. The California Medical Ass'n estimates that 80% of California IPAs are in serious financial trouble and fail at a rate of one every two to three weeks. See Page, Doctor Discovers Capitation, supra note 109, at 20.
Lest one think exemptions to antitrust law are only made for historically low-paid market participants, a factor critics will quickly point out that is inappropriate to doctors, Congress has also provided antitrust immunity to professional sports in agreements dealing with media coverage and limited exemption to mergers of professional football leagues. Professional sports salaries far exceed those of physicians and often raise the ire of the general public.

The McCarran-Ferguson Act was a quick Congressional reaction to a case wherein the United States Supreme Court held that “insurance transactions were subject to federal regulation under the Commerce Clause, and that the antitrust laws in particular were applicable to them.” Although the primary purpose of the McCarran-Ferguson Act is to permit states to regulate the business of insurance, the secondary purpose is to provide limited antitrust liability to the insurance industry in the context of allowing them to share information with regard to underwriting and risk spreading functions. “The McCarran-Ferguson Act was designed primarily to enable insurers to collaborate on cooperative rate making without violating the antitrust laws.” The need for physicians to share information in order to discern financial risk, e.g. calculating risk under capitation plans, is analogous to the need for insurance collaboration for setting rates.

A final and pertinent example of Congressional response to social changes is the Wagner-Connery Labor Relations Act. Congressional intent should be determined by looking at the expressed purpose of the National Labor Relations Act (“NLRA”). The NLRA notes that an inequality of bargaining power between employees and employers tends to have a harmful economic effect. It declares that the policy of the United States is to eliminate the causes of obstructions to commerce by encouraging collective bargaining. Another purpose is “protecting the exercise by workers of full freedom of association, self-organization, and designation of representatives of their own choosing, for

530 For documentation one need only remember the usual rhetoric of salary negotiations reported by newspapers, radio, or television. Few readers will not remember (with some degree of ire) the baseball strike of the late 1990s.
534 “[O]nly the core activities of a traditional insurance company, viz., the underwriting and risk spreading functions, fall within the McCarran-Ferguson Act exemption for the business of insurance.” Hahn v. Oregon Physicians Service, 689 F.2d 840, 843 (9th Cir. 1982).
540 See id.
the purpose of negotiating the terms and conditions of their employment or other mutual aid or protection.”

The NLRA’s primary purpose was to redress imbalance of economic power between labor and management. The remedy was intended to strengthen rather than weaken the cooperation between the two parties. “The purpose of the NLRA is to encourage collective bargaining, which by its very nature is a mutual undertaking.”

The Act also implies a good faith effort in negotiations. The NLRA is also intended to cover contractual relationships between labor and management. Finally, the purpose of the NLRA is to protect working men in crafts and unskilled labor, to enable them to bargain collectively for such things as job security, adequate wages and fair working conditions. Today’s doctors face many of the same threats.

The NLRA is an excellent example of Congressional response to a socioeconomic need. These multiple and varied, but related, purposes make the NLRA an appropriate vehicle for addressing the needs of today’s health care delivery system. By permitting collective bargaining by physicians, many of the problems of managed care can be solved through a cooperative effort of physicians, hospitals, and insurers. Such problems include rising costs, poor access to health care, onerous contract provisions that harm the public as well as physicians, and improvement in quality of care by return of decision-making to doctors where it rightfully belongs.

D. Physicians Should Be Given Collective Bargaining Rights Via a Labor Law Theory

Three reasons exist for recognition of physicians’ rights to collectively bargain: (1) Congress intended to permit professionals to bargain collectively under the NLRA; (2) Under present conditions of managed care, physicians are treated more as employees than as independent contractors; and (3) The recent history of labor law is on a continuum to recognize independent physicians’ collective bargaining rights.

541 Id. (emphasis added).
543 See N.L.R.B. v. Knuth Bros., Inc., 537 F.2d 950, 957 (7th Cir. 1976).
544 Houston Shopping News Co. v. N.L.R.B., 554 F.2d 739 (5th Cir. 1977) (emphasis added).
545 See N.L.R.B. v. Westinghouse Air Brake Co., 120 F.2d 1004, 1006-07 (3rd Cir. 1941).
546 Id.
548 For example, job insecurity in the sense of ever-present threat that a contract will not be granted or renewed, a doctor may be deselected on the basis of his utilization profile or for no reason whatsoever; inadequate wages in the sense of reimbursements that do not keep up with inflation and rising costs; and, unfair working conditions in the sense of onerous contract clauses, loss of control of patient-care decisions, and risk of malpractice that is unshared by insurers who “call the shots.”
1. The NLRA Recognizes Collective Bargaining Rights of Professionals

Historically, the stumbling block to recognition of physicians' collective bargaining rights has been the categorization of doctors as independent contractors or supervisory employees rather than as employees.\(^{549}\) The NLRA recognizes professional employees.\(^{550}\) Obviously, doctors have been recognized as professionals.\(^{551}\) Physicians and other hospital professionals have also been recognized as appropriate bargaining units in the health care industry.\(^{552}\)

2. "Employee" or "Independent Contractor"

Under various aspects of federal law, however, physicians are usually recognized as independent contractors. Examination of several federal torts cases provides a sense of the types of facts that determine status as an independent contractor rather than an employee. For example, the status may depend on whether the contract describes the relationship as one of an independent contractor, who pays the physician's malpractice insurance, and whether he is paid directly or via a fee schedule paid to his employer.\(^{553}\)

Several legal tests of independent contractor status have evolved.\(^{554}\) The traditional common law test has been primarily one of "control,"\(^{555}\) although numerous factors are considered, depending on the court.\(^{556}\) Some courts have referred to consideration of these other factors as hybrid tests or "economic reality considerations," reflecting the degree of economic dependence of the

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\(^{549}\) Supervisory employees do not have bargaining rights under the NLRA. Determination of supervisory status depends on meeting three criteria: (1) the employee has the authority to engage in one of the 12 listed activities in § 2(11) of the Act; (2) the employee exercises that authority using independent judgment; and (3) the employee holds authority in the interest of the employer. See Third Coast Emergency Physicians, 330 N.L.R.B. 117 (2000) (citing N.L.R.B. v. Health Care & Retirement Corp., 511 U.S. 571, 573-574 (1994)).


\(^{552}\) See 29 C.F.R. § 103.30 (2000).


\(^{554}\) In addition to the two tests discussed herein (common law test of control and hybrid or economic reality test), in some cases a test of apparent agency test has been used. See Ballard v. Advocate Health and Hosp., 1999 WL 498702 (N.D. Ill. Jul. 7, 1999).

\(^{555}\) In applying Pennsylvania law, a federal district court used the state law test of "exclusive control over the manner of performing [work]," but considered an alternate test of "ostensible agency" in the context of the tort case. Morales v. Guarini, 57 F.Supp.2d 150 (E.D. Pa. 1999).

\(^{556}\) See, e.g., Linkous v. United States, 142 F.3d 271 (5th Cir. 1998) (considering ten factors, but finding that "control" is most critical); Rodriguez v. Sarabyn, 129 F.3d 760 (5th Cir. 1997) (considering eight factors in addition to "control"). In consideration of independent contractor status in a Title VII case, the 7th Circuit applied a five-factor test. See Ost v. West Suburban Travelers Limousine, Inc. 88 F.3d 435, 438 (7th Cir. 1996). See also Alexander v. Rush North Shore Med. Center, 101 F.3d 487, 492 (7th Cir. 1996).
worker on the putative employer. Factors reflecting economic dependence include:

(1) the kind of occupation, with reference to whether the work usually is done under the direction of a supervisor or is done by a specialist without supervision; (2) the skill required in the particular occupation; (3) whether the "employer" or the individual in question furnishes the equipment used and the place of work; (4) the length of time during which the individual has worked; (5) the method of payment, whether by time or by the job; (6) the manner in which the work relationship is terminated; i.e., by one or both parties, with or without notice and explanation; (7) whether annual leave is afforded; (8) whether the work is an integral part of the business of the "employer"; (9) whether the worker accumulates retirement benefits; (10) whether the "employer" pays social security taxes; and (11) the intention of the parties.

Courts have modified the hybrid test to more appropriately apply to certain health care settings, like the hospital. One court held that "the real test is control over the primary activity contracted for and not the peripheral, administrative acts relating to such activity." Regardless of the situation or the test applied, the most important factor is: "the extent of the employer's right to control the 'means and manner' of the worker's performance . . ." If an employer can "control and direct the work of an individual, not only as to the result to be achieved, but also as to the details by which that result is achieved," an employer/employee relationship exists under the NLRA.

The rationale for argument that physicians are more like employees than independent contractors is based on the principle that an employer controls work and its instrumentalities and circumstances to a greater degree than does a hiring party in an independent-contractor relationship. Various aspects of the relationship between physicians and insurers suggest the relationship is more one of employee-employer than that of independent contractor and hirer.

Insurers control an ever-increasing degree of administrative details: pre-authorizations, concurrent utilization review, retroactive utilization review, credentialling, contract renewal, appellate procedures, requirement for referral to specialists, office inspections by the insurer for accreditation of a provider's practice, specificity of filing in order to receive reimbursement, review of coding, etc. Through such mechanisms, insurers control a physician's daily activities.

559 See Cilecek v. Inova Health Sys. Services, 115 F.3d 256 (4th Cir. 1997).
560 Robb v. United States, 80 F.3d 884, 889 (4th Cir. 1996) (citing Wood v. United States, 671 F.2d 825, 832 (4th Cir. 1982)).
562 Id: at 832.
563 See Cilecek v. Inova Health Sys. Services, 115 F.3d 256, 260 (4th Cir. 1997) (citing RESTATEMENT (SECOND) OF AGENCY §§ 2 & 220(2)).
Some primary care groups have quotas or limitations on the number of patients they must see, the number of new patients they must accept, details of office hours and availability of appointments to which they must conform. Physicians may decide whether to hire physician extenders; however, insurers decide whether or not they will reimburse physicians for the services physician extenders provide. Thus, insurers exert control or decision-making authority over how a physician will administer to a patient’s needs, i.e. through use of a nurse practitioner/physician assistant, or personally.

Insurers do not only control what tests are done, but also where they are done. Insurers restrict diagnostic studies to certain laboratories or hospitals. They restrict use of medications to certain formularies. Services are typically allowable only at certain treatment facilities and they also determine whether treatment is to be on an inpatient or outpatient basis.

Payment is usually determined also by insurers and usually physicians have no control over the fees paid. Usually fee schedules are not even provided to physicians. With capitation plans, doctors are more likely to be paid on a regular monthly basis a fixed rate per capita, rather than on a fee-for-service basis. Thus, reimbursements are more like wages than payments for a specified service.

Finally, although contracts may suggest an independent contractor status, such contracts are contracts of adhesion. Even if physicians consider themselves independent contractors, insurers clearly treat them more like employees, only without the benefits!

3. Historical Continuum Toward Collective Bargaining Rights of Physicians

Health care workers generally have collective bargaining rights including a right to strike.564 Nurses have been recognized for a long time as professional employees who have a right to collectively bargain.565 Resident physicians were long precluded from unionization because they were considered “students” under National Labor Relation Board (“NLRB”) rulings.566 On November 26, 1999, interns, residents, and fellows in private hospitals nationwide were recognized to have the right to organize and collectively bargain.567 The NLRB decided that housestaffs’ student status was irrelevant under the NLRA definition of employee.

Further reasons for their decision included that: the hospitals were statutory employers; residents received a stipend from which normal payroll deductions were taken; they received fringe benefits; and, they performed work in the sense of taking care of patients.568 Another large group of residents and fellows at a private hospital in Chicago sought collective bargaining rights under the new

564 See Jackson, A Striking Trend, supra note 490, at 17 (reporting on recent hospital strikes).
NLRB ruling.\textsuperscript{569} Nationwide, about fifty percent of residents at public hospitals are unionized.\textsuperscript{570} Unionization of residents in private hospitals continues to grow.\textsuperscript{571}

Traditionally, practicing private physicians have not been recognized as employees. In 1980, even attending staff physicians at universities, though recognized as professional employees, have been considered as supervisory employees precluded from collective bargaining.\textsuperscript{572} That precedent appears to have fallen as bargaining rights of staff physicians have recently been recognized.\textsuperscript{573} Practicing physicians employed by public hospitals in some areas of the country are also in unions.\textsuperscript{574} In May, 1999, eight hundred physicians joined the Union of American Physicians and Dentists.\textsuperscript{575}

The trend is clearly toward recognition of independent physicians' right to collectively bargain. Other professionals, e.g. nurses, have had such rights for years. With the recent ruling permitting residents, at both public and private hospitals, to bargain it seems inequitable (or even ludicrous) to take away that right when they step into the shoes of attending physicians. Furthermore, it seems even more ironic to permit staff physicians or attending physicians at medical schools to bargain collectively, yet refuse such rights to attendings who serve as voluntary faculty in the same institutions or at different private hospitals. Considering the fact that managed care permeates both public and private sectors, the need for collective bargaining is universal. Granting collective bargaining rights to all physicians is merely a continuation along a path of historical travel.

V. CONCLUSION

Over the past twenty to thirty years, the United States has undergone a paradigm shift in the health care delivery system. Fee-for-service plans have diminished in number and importance as managed care products have developed and expanded. The goals of managed care are cost containment, utilization review, and improvement in quality. Despite those laudable goals, current problems exist in the health care arena. New technology, new drug therapy, medical malpractice costs, and the use of health care as an investment market have resulted in continued high costs. The "fat" has been trimmed from the system to the point that further attempts to control cost by decreasing provider


\textsuperscript{570} Id.

\textsuperscript{571} See Jay Greene, \textit{PRN Files Petition for Union of Residents at Illinois Hospital}, \textit{AM. MED. NEWS}, Sep. 11, 2000, at 1.


\textsuperscript{574} See Nicholas Riccardi, L.A. County Doctors Vote Decisively to Unionize Labor: The 800 Employees are the Largest Group of U.S. Physicians to Organize in Nearly 20 Years. \textit{Health Agency Cutbacks Spurred the Effort, Which is Expected to Reverberate Nationwide}, \textit{LOS ANGELES TIMES}, May 29, 1999, at A1.

\textsuperscript{575} See \textit{id.}
reimbursements or shifting financial risk to the providers is resulting in loss of market participants such as IPAs and PHOs, groups of providers that have formed in response to the evolving market changes.

Physicians, feeling the frustration of lower reimbursements, higher demands, and onerous contract provisions are turning to physician unions as a viable means of dealing with relationships with overpowering insurers who refuse to negotiate. Patients feel frustration due to ever-rising costs of medical care, loss of ability to choose their doctors, and rationing of health care by insurers. The traditional patient-doctor relationship is deteriorating. The political and social response to managed care's problems has been an ineffective, costly, time-consuming piece-meal approach that has largely been initiated at the state level. Medical societies have shifted position in favor of physician unionization.

Physician unions could be a cost-effective, efficient, and successful means of dealing with problems of managed care. Physicians need the opportunity to negotiate on an equal basis with insurers in order to reestablish medical decision-making power into the doctors' realm for patient welfare. Physicians need to be able to negotiate onerous contracts on an equal basis—a process that could be much more effective and efficient than current attempts at legislative solutions on a piecemeal basis.

Traditional antitrust law poses significant barriers to collective bargaining by physicians. The courts have fluctuated in their use of the per se rule versus the rule of reason. The more recent cases, however, have generally shifted to a rule of reason, except in very few cases of facially evident price-fixing or boycott arrangements. Recognizing the unique and delicate nature of the health care industry, the antitrust enforcement agencies, i.e. the Department of Justice and the Federal Trade Commission, have formulated guidelines for activities of market participants in the health care arena. These guidelines, while in some ways at tension with case law, have largely recognized the rule of reason as the appropriate mode of analysis. Although such guidelines are a step in the right direction to providing antitrust relief for collective bargaining, they still do not go far enough.

There are basically four rationales for permitting physicians to collectively bargain. First, if evaluated under a rule of reason rather than a per se rule, physician unions can be procompetitive in the sense of providing significant benefits to consumers. Examples include increasing the number of options for patients by increasing the number of physicians on health panels, increasing access to health care, and improving quality of care by putting decision-making authority back into the hands of doctors.

Second, under a contract theory, current contracts between insurers and physicians are contracts of adhesion that are unconscionable. The result includes onerous contract provisions that are harmful, not only to physicians, but to their patients. Such evils of managed care are causing many doctors to leave the field of medicine and seek alternative careers, retire early, etc. Over time the result will be further deprivation of health care access to consumers. The solution is to provide equal power of negotiation to both insurers and physicians.

Third, judicial or statutory relief through antitrust exemption has a strong historical basis and is appropriate as a temporary or long-term solution. The rich
history of antitrust exemptions include labor, agricultural cooperatives, newspapers, fishing, insurance, and professional sports.

Finally, physician unions should be permitted under a labor theory. The National Labor Relations Act was intended to cover professional employees. Although independent physicians have typically been considered independent contractors, analysis of current working conditions including reimbursements, decision-making authority, and control of various aspects of a physician’s daily practice suggest the relationship of physicians to insurers is more akin to one of an employee than ever before. Recent historical trends in permitting other health care professionals, housestaff, and staff physicians to collectively bargain suggests a movement toward acceptance of physician unions.

The issue of physician unionization or collective bargaining is highly controversial. Nearly everyone can agree that the present managed care system has significant pitfalls. One solution worth trying is putting trust back into the patient-physician relationship. In the final analysis, if you have a serious health situation, who will you trust? Your doctor or your insurance company?
INTRODUCTION

One fateful August evening, a young woman approached an intersection in her 1992 automobile. A truck travelling in the opposite direction recklessly turned in front of her car, striking the car's front end. The car employed a passive or automatic belt restraint system consisting of a two-point motorized shoulder belt that automatically locked in place when the operator closed the door, a knee bolster designed to restrain an operator's lower torso, and a manual lap belt.

The young woman was not wearing her lap belt at the time of the accident and upon impact with the truck, slid forward in her seat as the shoulder belt tightened on her upper body. She suffered massive injuries including multiple rib fractures, lacerations to both lungs, and a tear to the left auricle of her heart. The young woman died due to lack of oxygen to her brain as a result of blood loss from the heart and lung lacerations.

The victim's estate filed suit against the manufacturer of the automobile in federal district court alleging, among other things, that the vehicle was defectively designed because it failed to contain an airbag. The defendant, manufacturer, filed a motion for summary judgment asserting that the plaintiff's claim was preempted by the National Traffic and Motor Vehicle Safety Act of 1966 ("Safety Act") and Federal Motor Vehicle Safety Standard 208 ("Standard

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1 Samuel Elswick is a third year student in the evening division of Salmon P. Chase College of Law and a staff member of the Northern Kentucky Law Review.


'[P]assive occupant restraint systems'--devices that do not depend for their effectiveness upon any action taken by the occupant except that necessary to operate the vehicle. Two types of automatic crash protection emerged: automatic seatbelts and airbags. The automatic seatbelt is a traditional safety belt, which when fastened to the interior of the door remains attached without impeding entry or exit from the vehicle, and deploys automatically without any action on the part of the passenger.

Id.

3 An airbag "is an inflatable device concealed in the dashboard and steering column. It automatically inflates when a sensor indicates that deceleration forces from an accident have exceeded a preset minimum, then rapidly deflates to dissipate those forces." Id. at 35.

208"). The district court agreed and granted the motion. The federal circuit court affirmed.

Claims against manufacturers based on the manufacturer’s failure to install airbags in its vehicles first appeared as a theory of liability in the mid-1980s, and such claims have been the fruit of litigation ever since. In order to understand the Supreme Court’s recent decision in Geier v. American Honda Motor Company, this note will first examine the legislative and judicial history of the Safety Act and Standard 208 as applied to “no-airbag” lawsuits. It will then conduct an analysis of the Geier decision, its holding and its future impact on both no-airbag lawsuits and the viability of manufacturers’ utilizing federal regulatory compliance as a defense to state common-law tort actions.

I. LEGISLATIVE BACKGROUND

A. The National Traffic and Motor Vehicle Safety Act of 1966

Over three decades ago, Congress confronted the “soaring rate of death and debilitation on the Nation’s highways” head-on by enacting the Safety Act. Congress’ express purpose for enacting the Safety Act was “to reduce traffic accidents and deaths and injuries to persons resulting from traffic accidents.” The Safety Act directed the Secretary of Transportation to promulgate Federal Motor Vehicle Safety Standards that “shall be practicable, shall meet the need for motor vehicle safety, and shall be stated in objective terms.” The Secretary’s general authority to promulgate safety standards under the Safety Act was eventually delegated to the Administrator of National Highway Traffic Safety Administration (“NHTSA”).

B. Federal Motor Vehicle Safety Standard 208

The NHTSA fulfilled its duty by promulgating Standard 208. Congress intended Standard 208 to address two distinct types of dangers: vehicle defects that result in accidents and vehicle defects that aggravate injuries to occupants involved in accidents. The second category of vehicle defect effects what is

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11 15. U.S.C. § 1392(a) (1988); see also State Farm, 463 U.S. at 33.
12 49 C.F.R. § 1.50(a) (1982); see also State Farm, 463 U.S. at 34 n.3.
sometimes labeled the “crashworthiness” of a vehicle.\textsuperscript{15} A subset of crashworthiness, the “second collision,” was specifically addressed by the Senate Committee when it stated that “[t]he 'second collision' -- the impact of the individual within the vehicle against the steering wheel, dashboard, windshield, etc. -- has been largely neglected.”\textsuperscript{16} The Senate Committee noted that certain preventative measures taken in designing the vehicle such as “[r]ecessed dashboard instruments and the use of seat belts can mean the difference between a bruised forehead and a fractured skull.”\textsuperscript{17} Several courts and commentators believe that this legislation “marked a dramatic shift from the historic definition of the automobile safety problem as one of avoiding accidents by modifying driver behavior to that of modifying vehicle design.”\textsuperscript{18}

As originally issued in 1967, Standard 208 merely required the installation of seatbelts in all automobiles,\textsuperscript{19} but it soon became apparent that most vehicle occupants would not use their seatbelts.\textsuperscript{20} The Department of Transportation ("DOT") then began to consider the practicability of mandating passive occupant restraint systems such as airbags and automatic seatbelts.\textsuperscript{21} The life-saving potential of these passive restraint systems was recognized, and after extensive field-testing of both devices, NHSTA established that passive restraint systems could possibly prevent approximately 12,000 deaths and 100,000 serious injuries annually.\textsuperscript{22}

In 1969, the DOT proposed a standard that required installation of passive restraint systems in new motor vehicles as soon as possible and not later than January 1, 1972.\textsuperscript{23} In response, automobile manufacturers filed suit to challenge this proposed requirement and were partly successful.\textsuperscript{24} In 1970, the DOT

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\textsuperscript{15} See \textit{Wood}, 865 F.2d at 397.
\textsuperscript{17} S. REP. NO. 89-1301, at 3 (1966), reprinted in 1966 U.S.C.C.A.N. 2709, 2711.
\textsuperscript{18} Chadwell, supra note 6, at 142. \textit{See Babb, supra note 14, at 1681. See generally Wood, 865 F.2d at 397; see also Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 33 (1983); S. REP. NO. 89-1301, at 3 (1966), reprinted in 1966 U.S.C.C.A.N. 2709, 2710-11} (stating that “[f]or too many years, the public’s proper concern over safe driving habits and capacity of the driver (the ‘nut behind the wheel’) was permitted to overshadow the role of the car itself.”).
\textsuperscript{21} \textit{See Geier}, 120 S. Ct. at 1922; \textit{See also State Farm}, 463 U.S. at 34-35.
\textsuperscript{22} \textit{See State Farm}, 463 U.S. at 35 (citing 42 Fed. Reg. 34,298 (1977)).
\textsuperscript{24} \textit{See Chadwell, supra note 6, at 145 n.30} (citing \textit{Chrysler Corp. v. Department of Transp.}, 472 F.2d 659 (6th Cir. 1972)) (rejecting the auto-makers challenge to NHTSA’s authority, but suspending the requirement due to an insufficiently objective standard for compliance). \textit{See also State Farm}, 463 U.S. at 36 n.5 (stating that the \textit{Chrysler} court held that the testing procedures of passive belts were not sufficiently objective to comply with the Safety Act).
revised Standard 208 to include some passive protection requirements, and in 1971, an express provision was added to Standard 208 allowing manufacturers to comply by utilizing non-detachable passive belts.

In 1972, NHTSA amended Standard 208 to require full passive protection for all front seat occupants for vehicles manufactured after August 15, 1975. Between August 1973 and August 1975, NHSTA gave manufacturers the option of installing a passive restraint system such as automatic seatbelts, or airbags or retaining manual seatbelts coupled with an ignition interlock device that would not allow the vehicle to start if the belts were not buckled.

Most car manufacturers chose the ignition interlock option, and in 1974, the DOT approved the use of detachable automatic seatbelts conditioned on such systems including an ignition interlock and a continuous warning buzzer to indicate that the safety belts were not connected. The interlock device and the continuous buzzer were extremely unpopular with consumers. Congress reacted to public disapproval of the devices by passing the Motor Vehicle and School Bus Safety Amendments of 1974, forbidding NHTSA from permitting or requiring manufacturer compliance by employing either of these devices. These amendments provided that any safety standard used in lieu of seatbelts must be presented to Congress, who may in turn, veto the standard by a concurrent resolution of both houses. The date for compulsory passive restraint systems was extended for one year, and became effective August 31, 1976. However, in June 1976, Department of Transportation Secretary William Coleman began a new rulemaking on the passive restraint initiations, and after hearings, he suspended the passive restraint requirements grounding his decision on potential public resistance to such devices. In lieu of the mandatory passive restraints,
the Secretary proposed a demonstration plan involving up to 500,000 automobiles installed with passive restraints.\textsuperscript{37}

However, in 1977, Secretary Coleman’s successor, Brock Adams terminated the demonstration project, and issued a mandatory passive restraint regulation: Modified Standard 208.\textsuperscript{38} This new safety standard required passive restraints, essentially either airbags or passive seatbelts, to be phased in starting with large cars in model year 1982 and extending to all automobiles by model year 1984.\textsuperscript{39}

During the intervening years, the automobile industry adapted its operations to comply with Modified Standard 208.\textsuperscript{40}

In 1981, Adam’s successor, Andrew Lewis, citing economic difficulties in the automobile industry and NHTSA doubts that passive restraint systems would produce significant safety benefits, rescinded the passive restraint requirement in Modified Standard 208.\textsuperscript{41} The Supreme Court in \textit{Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.},\textsuperscript{42} later held that the Secretary’s rescission of Modified Standard 208 was unlawful.\textsuperscript{43}

\textbf{C. Current Status of Federal Motor Vehicle Safety Standard 208}

In 1984, DOT Secretary Elizabeth Dole amended Standard 208 yet again.\textsuperscript{44} This version of Standard 208 required a gradual phase-in of passive restraints.\textsuperscript{45} This phase-in was to be completed in three annual stages.\textsuperscript{46} After this three-year phase-in, all new cars were required to have automatic occupant crash protection after September 1, 1989.\textsuperscript{47}

Standard 208 intentionally sought a “variety—a mix of several different passive restraint systems.”\textsuperscript{48} It attempted to acquire this mix by establishing a

\textsuperscript{37} Id. at 37.
\textsuperscript{38} Id.
\textsuperscript{39} Id. (citing Modified Standard 208, 42 Fed. Reg. 34,289 (1977) codified at 49 C.F.R. § 571.208 (1978)).
\textsuperscript{40} See \textit{State Farm}, 463 U.S. at 37.
\textsuperscript{43} See id. at 46.
\textsuperscript{45} See 49 Fed. Reg. 28,962, 28,999-29,000; \textit{Geier}, 120 S. Ct. at 1924.
\textsuperscript{46} 49 Fed. Reg. at 28,999 stated:

The Phase-In

The rule requires the manufacturers to follow a phase-in schedule for compliance with the automatic occupant protection requirements. A minimum of 10 percent of all cars manufactured after September 1, 1986, must have automatic occupant crash protection. After September 1, 1987, the percentage is raised to 25 percent; after September 1, 1988, it is raised to 40 percent; and after September 1, 1989, all new cars must have automatic occupant crash protection.

\textit{Id.}

\textsuperscript{47} See id.
\textsuperscript{48} \textit{Geier}, 120 S. Ct. at 1924.
performance standard for passive restraint systems and by giving manufacturers several options or types of passive restraint systems to utilize including airbags, automatic belts, or other passive restraint technologies.49

The Department of Transportation issued this performance standard instead of mandating the use of a single device such as an airbag for several reasons which included:50 (1) the possible negative public perception of airbags, their relative safety, and the potential for backlash if airbags were the only alternative;51 (2) the possibility that a mix of passive restraint systems could provide data on the comparative effectiveness of different systems;52 (3) the belief that a mix would allow the industry to address safety concerns and reduce the high production costs of airbags;53 (4) the potential that a mix of systems would spur growth of alternative, more cost-efficient, and safer devices;54 and (5) the hope that a mix would nurture public confidence.55

Standard 208 provided a form of extra credit during the phase-in period if manufacturers utilized "airbags, passive interiors, or other systems that meet the test requirements of the rule."56 Under this extra credit provision, manufacturers received credit for an extra one-half automobile toward their required percentage during the phase-in period for the use of any of the previously cited non-belt technologies.57

Standard 208 as promulgated required rescission of the automatic occupant protection requirement if, by September 1, 1989, two-thirds of the population of the United States were residents of states that had passed mandatory use laws (MUL's) meeting the requirements of Standard 208.58 This provision reflected DOT's belief that ordinary lap and shoulder belts would produce essentially the same amount of safety as automatic occupant systems, at substantially lower costs if automobile occupants would utilize their safety belts.59

Presently, federal law requires that all passenger cars "manufactured on or after September 1, 1997 must have an airbag at the driver's and right front passenger's position."60 Passenger cars automatically meet applicable frontal crash protection requirements of Standard 208 if they have airbags at the driver's and right front passenger's position.61

50 See Geier, 120 S. Ct. at 1924 (citing 49 Fed. Reg. 28,962, 28,997 (1984)).
51 Id. at 1924 (citing 49 Fed. Reg. 28,962, 29,001 (1984)).
54 See Geier, 120 S. Ct. at 1924 (citing 49 Fed. Reg. 28,962, 29,001-02 (1984)).
55 Id.
57 See id.
58 Id. at 28,997.
59 See generally id. at 28,997-99. See also Geier, 120 S. Ct. at 1925 (stating that the Secretary believed that state enforced MUL's would nullify any intervening increases in safety expected from passive restraint systems) (citations omitted).
61 See id. at S.1.5.4.
II. THE DOCTRINE OF FEDERAL PREEMPTION

The Supremacy Clause of the United States Constitution provides that "the Laws of the United States . . . shall be the supreme Law of the Land; . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." If a conflict exists between a State law and a Federal law, the former is "without effect." The doctrine of federal preemption is grounded in the Supremacy Clause of the United States Constitution, which states that "the Laws of the United States... shall be the supreme Law of the Land;... any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." If a conflict exists between a State law and a Federal law, the former is "without effect." The Supreme Court's analysis of the pre-emptive scope of a statute begins with the statute's text, but its interpretation of the statute's language does not take place in a "contextual vacuum." Instead, the Court's interpretation is governed by two basic presumptions concerning the nature of preemption. First, States are independent sovereigns in our federal system, and the Court presumes that "Congress does not cavalierly pre-empt state-law causes of action." Second, "[t]he purpose of Congress is the ultimate touchstone" in each preemption case.

The Supreme Court's preemption analysis can be divided into three categories: express preemption, implied field preemption, and implied conflict preemption. Express preemption exists when Congress' intent is "explicitly stated in the statute's language," expressly commanding that the state law be preempted if it is in actual conflict with the federal law. Implied field preemption exists if federal law "so thoroughly occupies a legislative field as to make reasonable the inference that Congress left no room for the States to supplement it." In addition to express preemption and implied field preemption, a state law may also be preempted if it "actually conflicts with a . . . federal statute." An actual conflict between a state law and a federal statute will exist when the state law "stands as an obstacle to the accomplishment and

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62 U.S. CONST. art. VI.
65 See Medtronic, 518 U.S. at 485.
66 Id.
67 Id. (quoting Hillsborough County v. Automated Medical Laboratories, Inc., 471 U.S. 707, 715 (1985)).
68 Medtronic, 518 U.S. at 485 (quoting Retail Clerks v. Schermerhorn, 375 U.S. 96, 103 (1963)) (citations omitted).
execution of the full purposes and objectives of Congress.'" Additionally, regulations promulgated by federal agencies acting non-arbitrarily within their statutory authority may also be given pre-emptive force.74

In cases involving Standard 208, the plaintiff generally asserts that the defendant auto manufacturer, who otherwise fully complied with Standard 208, nonetheless had a duty to equip the automobile with airbags.75 Almost invariably, the defendant auto manufacturer asserts that the Safety Act's preemption provision76 either expressly or impliedly preempts the State common-law tort action.77 Finally, the plaintiff counter argues that the Safety Act's savings clause78 preserves all state common-law tort claims including those sounding in defective design.79

A. Preemption Analysis in the Federal Circuit Courts

Several Federal Circuit Court decisions are instructive on how this scenario unfolds in the context of Standard 208 litigation. In Pokorny v. Ford Motor


Federal regulations have no less pre-emptive effect than federal statutes. Where Congress has directed an administrator to exercise his discretion, his judgements are subject to judicial review only to determine whether he has exceeded his statutory authority or acted arbitrarily. When the administrator promulgates regulations intended to pre-empt state law, the court's inquiry is similarly limited ...

Id. (internal citations omitted).

75 See generally Geier, 120 S. Ct. at 1916-17 (asking whether a defendant who is in compliance with FMVSS 208, which did not require the installation of airbags, nonetheless had a common-law duty to install airbags).


Whenever a Federal motor vehicle safety standard established under this subchapter is in effect, no State or political subdivision of a State shall have any authority either to establish, or to continue in effect, with respect to any motor vehicle or item of motor vehicle equipment any safety standard applicable to the same aspect of performance of such vehicle or item of equipment which is not identical to the Federal standard. Nothing in this section shall be construed to prevent the Federal Government or the government of any State or political subdivision thereof from establishing a safety requirement applicable to motor vehicles or motor vehicle equipment procured for its own use if such requirement imposes a higher standard of performance than that required to comply with the otherwise applicable federal standard. (15 U.S.C. § 1392(d) is now codified without substantive change at 49 U.S.C. § 30,103(b) (1994)).

Id.

77 See Geier, 120 S. Ct. at 1917.


Compliance with any Federal motor vehicle safety standard issued under this subchapter does not exempt any person from any liability under common law. (15 U.S.C. § 1397(k) is now codified without substantive change at 49 U.S.C. § 30,103(e) (1994)).

Id.

79 See Geier, 120 S. Ct. at 1919 (stating that petitioners argue that a savings clause has the effect of foreclosing any possibility of implied conflict preemption between the state common-law action and the federal standard) (citations omitted).
Co.,\textsuperscript{80} the administratrix of a man killed while a passenger in a 1981 Ford van sued Ford contending that the van was defectively designed.\textsuperscript{81} The plaintiff alleged that the van should have been equipped with: (a) airbags; (b) automatic seatbelts; or (c) protective netting on the windows.\textsuperscript{82} The court held that the airbag and automatic seatbelt claims were impliedly preempted because they presented an actual conflict with the Safety Act and Standard 208 and frustrated the goals of providing auto manufacturers a choice among several options regarding passive restraints.\textsuperscript{83} However, the claim that the van was defectively designed because it lacked protective netting was not preempted.\textsuperscript{84} Liability for this type of automatic restraint presents "no direct, actual conflict with Standard 208's regulatory framework. It does not take away the flexibility established by the federal scheme, and it does not have the effect of prohibiting an option granted by Congress or the Department of Transportation."\textsuperscript{85}

In Taylor v. General Motors Corp.,\textsuperscript{86} Charles Taylor and Paula Evans were killed in separate front-end collisions while operating automobiles manufactured by General Motors Corporation and American Honda Motor Company.\textsuperscript{87} The personal representatives of the decedents' estates filed claims against the automobile manufacturers under Florida tort law claiming that the vehicles were defectively designed because they were not equipped with airbags.\textsuperscript{88} The court held that the language of the Safety Act did not expressly preempt State law tort claims.\textsuperscript{89} However, the court concluded that the appellants strict liability claim would take away the flexibility provided by Standard 208 by prohibiting the exercise of a federally granted choice, thereby "frustrat[ing] the federal regulatory scheme."\textsuperscript{90} Therefore, the claim was impliedly preempted by Standard 208 and the Safety Act.\textsuperscript{91}

In Harris v. Ford Motor Co.,\textsuperscript{92} the plaintiff was seriously injured when she lost control of her 1992 Mercury Topaz and struck a tree.\textsuperscript{93} Harris sued Ford in a California state court contending that the car was defectively designed because Ford had not equipped it with a driver side airbag.\textsuperscript{94} The three-judge panel

\begin{footnotesize}
\begin{enumerate}
\item Pokorny v. Ford Motor Co., 902 F.2d 1116 (3rd Cir. 1990).
\item See id. at 1117.
\item Id.
\item Id. at 1123, 1126.
\item Id. at 1125-26.
\item Id. at 1126 (citing Fidelity Fed. Sav. & Loan Ass'n v. De la Cuesta, 458 U.S. 141, 154-56 (1982)).
\item Taylor v. General Motors Corp., 875 F.2d 816 (11th Cir. 1989).
\item See id. at 817.
\item Id.
\item Id. at 825.
\item Id. at 827.
\item Id.
\item Harris v. Ford Motor Co., 110 F.3d 1410 (9th Cir. 1997).
\item See id. at 1411.
\item Id.
\end{enumerate}
\end{footnotesize}
concluded that a judgment for the plaintiff based on a common-law cause of action for failure to install airbags "would have an effect on Ford identical to a state statute or regulation requiring airbags in all vehicles." The court concluded that this type of common-law recovery would set a safety standard for vehicle performance or equipment. Thus, the court held that that the Safety Act expressly preempts state tort law causes of action for failure to install airbags.

B. Preemption Analysis in the Supreme Court

*Cipollone v. Ligget Group, Inc.* and its progeny "provided the impetus for a shift in the interpretations of federal preemption of state products liability claims." In *Cipollone*, the plaintiff brought an action against Ligget Group, Inc., contending that Rose Cipollone developed lung cancer from smoking cigarettes manufactured by the defendants. The plaintiff's complaint prayed for several different types of recovery relying on theories of strict liability, negligence, express warranty, and fraudulent misrepresentation.

The defendants asserted that the preemption provision of the Federal Cigarette Labeling and Advertising Act of 1965 and its successor, the Public Health Cigarette Smoking Act of 1969 shielded them from all liability after 1965, and preempted the plaintiff's common law claims. The Court read the

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95 Id. at 1415.
96 Id. (citations omitted).
97 Id.
100 See Cipollone, 505 U.S. at 508.
101 Id. at 509.
102 15 U.S.C. § 1334 (Supp. III 1968) stated:
   Preemption.
   (a) Additional statements on packages.
   No statement relating to smoking and health, other than the statement required by section 1333 of this title, shall be required on any cigarette package.
   (b) Advertising statements.
   No statement relating to smoking and health shall be required in the advertising of cigarettes the packages of which are labeled in conformity with the provisions of this chapter.

Id.
   Preemption.
   (a) No statement relating to smoking and health, other than the statement required by section 1333 of this title, shall be required on any cigarette package.
   (b) No requirement or prohibition based on smoking and health shall be imposed under State law with respect to advertising or promotion of any cigarettes the packages of which are labeled in conformity with the provisions of this chapter.

Id.
104 See Cipollone, 505 U.S. at 510.
1965 Act’s preemption provision narrowly, citing the policy of a “presumption against preemption” of state laws. The Supreme Court held that the 1965 Act’s preemption clause merely precluded state and federal rulemaking bodies from requiring warning statements on cigarette labels or in cigarette advertisements. Under the Court’s holding, only positive enactments by legislative or administrative bodies that require specific warning labels are preempted by the Act, not state common-law damage actions.

The preemption provision of the Public Health Cigarette Smoking Act of 1969 was interpreted as being much broader textually, because it barred not only statements but also requirements or prohibitions imposed under state law. The Court held that the 1969 Act preempted the plaintiff’s claims based on failure to warn and neutralization of federally required warnings as far as they relied upon “omissions or inclusions” in the cigarette company’s advertising or promotions. However, the Court concluded that the 1969 Act did not preempt the plaintiff’s express warranty, intentional fraud, conspiracy or misrepresentation claims.

One particular portion of the Cipollone opinion created confusion and doubt regarding whether Congress’ inclusion of an express preemption clause in a federal statute forecloses a court’s use of implied preemption. Under this view of Cipollone, once a court finds that a preemption provision in a federal statute provides a reliable indicia of Congressional intent concerning state authority, then preemption analysis stops at that moment and there is no need to infer Congressional intent to preempt. Several courts interpreted Cipollone for the proposition that when a federal statute contains an express preemption

105 Id. at 518.
106 Id.
107 Id. at 519-20.
109 See Cipollone, 505 U.S. at 520.
110 Id. at 530-31.
111 Id. at 531.
112 Cipollone, 505 U.S. at 517 stated:

When Congress has considered the issue of pre-emption and has included in the [statute] a provision explicitly addressing that issue, and when that provision provides a ‘reliable indicium of congressional intent with respect to state authority,’ ‘there is no need to infer congressional intent to pre-empt state laws from the substantive provisions’ of the legislation. ... Congress’ enactment of a provision defining the pre-emptive reach of a statute implies that matters beyond that reach are not pre-empted.

Id. (alteration in original) (internal citations omitted).
113 See Freightliner Corp. v. Myrick, 514 U.S. 280, 287-88 (1995). See Chadwell, supra note 6, at 173 (arguing that “seven justices apparently ruled that all doctrines of implied preemption, both ‘conflict’ and ‘occupation-of-the-field’ varieties, are eliminated once Congress enacts a provision that, to some degree, expressly preempts state law”).
114 See Freightliner, 514 U.S. at 287-88.
clause, there should be no implied preemption analysis. This led to inconsistent results. For example, in *Myrick v. Freuhauf Corp.*, the Court of Appeals for the Eleventh Circuit followed the literal language of the *Cipollone* decision. The court held that Standard 208 did not expressly preempt state common-law claims, and that the preemption provision of the Safety Act, which included a savings clause provided a "reliable indicia" of Congressional intent not to apply implied preemption analysis.

In 1995, the Supreme Court granted certiorari to the defendants in *Myrick v. Freuhauf Corp.* in the case of *Freightliner Corp. v. Myrick.* This case involved two separate but similar accidents. In both crashes, 18-wheel tractor-trailers jammed their brakes suddenly and jack-knifed into oncoming traffic. Neither truck had an anti-lock breaking system ("ABS"). One individual suffered brain damage and permanent paralysis, and the other accident victim was killed. Plaintiffs sued alleging that failure to install ABS was negligence and resulted in a design defect. The Court held that this action was not expressly preempted under the Safety Act. The Court then cured any uncertainty resulting from the *Cipollone* decision by expressly stating that implied preemption can exist even when Congress has included an express preemption provision in a federal statute. The Court further held that the plaintiff's common law cause of action did not conflict with federal law because nothing in the Standard 208 currently regulates ABS brakes, and thus "it is not impossible . . . to comply with both Federal and State Law."

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115 See Babb, supra note 14, at 1694 (stating that many courts believed that when an express preemption clause was included in a federal statute, *Cipollone* mandated abandoning any implied preemption analysis).

116 *Id.* (citing six cases interpreting *Cipollone* as mandating a finding of either express preemption or no preemption).

117 13 F.3d 1516 (11th Cir. 1994).

118 See *id.* at 1526-27.

119 13 F.3d 1516 (11th Cir. 1994).


121 See *id.* at 282.

122 *Id.*

123 *Id.*

124 *Id.*

125 *Id.* at 283.

126 *Freightliner*, 514 U.S. at 286.

127 See *id.* at 287-88.

128 *Id.* at 289 (stating further that the plaintiff's lawsuit did not frustrate the "accomplishment and execution of the full purposes and objectives of Congress" because the Act did not address the need for ABS devices) (citations omitted).
III. THE FACTS OF GEIER V. AMERICAN HONDA MOTOR CO., INC.\(^{129}\)

In 1992, Alexis Geier was seriously injured when the 1987 Honda Accord she was driving collided with a tree.\(^{130}\) The Accord was equipped with manual shoulder and lap belts that Geier was wearing at the time of the accident.\(^{131}\) However, the Accord was not equipped with airbags or any other type of passive restraint system.\(^{132}\)

Geier and her parents brought suit against the manufacturer of the Accord, American Honda Motor Co., under District of Columbia tort law.\(^{133}\) The plaintiffs' complaint alleged, inter alia, that "American Honda had designed its car negligently and defectively because it lacked a driver's side airbag."\(^{134}\) The District Court dismissed Geier's lawsuit.\(^{135}\) The District Court concluded that the plaintiff's lawsuit was expressly preempted by Standard 208 because requiring an airbag would set a "safety standard" that is not identical to the federal standard governing the same feature of performance.\(^{136}\)

The United States Court of Appeals for the District of Columbia subsequently affirmed the district court's decision but on different grounds.\(^{137}\) The Court of Appeals concluded that the presence of the savings clause\(^{138}\) in the Safety Act\(^{139}\) makes it doubtful that the plaintiffs' lawsuit establishes the type of safety standard that the Act's preemption provision relates.\(^{140}\) Nonetheless, the Court held that the plaintiffs' common-law claims would create an obstacle to the accomplishment of Standard 208's objectives and that those claims actually conflicted with Standard 208.\(^{141}\) Thus, applying ordinary preemption principles, the Court of Appeals held that the Act preempted the plaintiffs' lawsuit.\(^{142}\)

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\(^{130}\) See id. at 1917.

\(^{131}\) Id.

\(^{132}\) Id.

\(^{133}\) Id.

\(^{134}\) Id.

\(^{135}\) See Geier, 120 S. Ct. at 1917.

\(^{136}\) Id. (citing Geier v. American Honda Motor Co., Inc., Civ. No. 95-CV-0064 (D.D.C. Dec. 9, 1997)).

\(^{137}\) See Geier, 120 S. Ct. at 1917.


\(^{140}\) See Geier, 120 S. Ct. at 1917 (citing Geier v. American Honda Motor Co., Inc., 166 F.3d 1236, 1238-43 (D.C. Cir. 1999)).

\(^{141}\) Id.

\(^{142}\) Id.
IV. THE COURT'S REASONING IN GEIER V. AMERICAN HONDA MOTOR CO., INC. \(^{143}\)

A. The Majority Opinion


First, the Supreme Court held that the Safety Act's express preemption clause did not preempt the plaintiffs' state common law tort actions for negligence and defective design. Second, the Court held that ordinary preemption principles nevertheless apply. Finally, the Court held that the plaintiffs' common-law tort action, based on the defendant's failure to install airbags in its vehicles, actually conflicted with Standard 208, and the Safety Act itself, and would stand as an obstacle to the accomplishment of Standard 208's objectives and was thus preempted by the Safety Act.

1. The Majority's Express Preemption Analysis

The Court first asked whether the Safety Act's express preemption clause pre-empted Geier's common law negligence and design defect claims. The majority addressed Honda's argument that in *Medtronic Inc., v. Lohr*, a majority of the Court held that the Safety Act's express preemption clause could expressly preempt state tort actions alleging negligence by the manufacturer due to failure to install airbags in its vehicles. The previously cited cases abrogated by the *Geier* decision were all state supreme court decisions holding that neither the Safety Act's express preemption provision nor Standard 208 preempts a state common-law tort action alleging negligence by the manufacturer due to failure to install airbags in its vehicles. See *Geier*, 120 S. Ct. at 1917, 1928.

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\(^{144}\) *Id.*

\(^{145}\) *Id.* at 1917-18.


\(^{147}\) See *Geier*, 120 S. Ct. at 1917-18.

\(^{148}\) *Id.* at 1918.

\(^{149}\) *Id.*


\(^{151}\) See *Geier*, 120 S. Ct. at 1918.

\(^{152}\) *Id.*

\(^{153}\) *Id.*


\(^{155}\) 15 U.S.C. § 1392(d), see supra note 76.

\(^{156}\) See *Geier*, 120 S. Ct. at 1918.

However, the Court declined to address the significance of the distinction between a "standard" and a "requirement," finding that the Safety Act's savings clause resolved the express preemption issue.

The Court reasoned that the federal statute merely creates a "floor" or a minimum safety standard, leaving room for state common law to operate. Moreover, the majority noted that it is possible to read the preemption provision, by itself, as applicable to standards set in state common law actions, as well as those contained in state regulations or legislation. Additionally, a broad reading of the preemption provision, absent a savings clause, could arguably preempt all non-identical state standards established in common law tort actions concerning the same performance feature as its counterpart federal standard, even if the federal standard had been intended only to establish a "floor."

Thus, the Court held that the presence of the savings clause permits a narrow reading of the preemption provision and removes common law tort actions from the reach of the Safety Act's express preemption provision.

2. The Majority's Implied Preemption Analysis

The Court then proceeded to answer the question of whether the savings clause "foreclos[es] or limit[s] the operation of ordinary pre-emption principles . . . [that] instruct us to read statutes as pre-empting state laws (including common-law rules) that 'actually conflict' with the statute or federal standards promulgated thereunder." The majority recognized that it had previously left this question open in *Freightliner Corp., v. Myrick,* but concluded that the Safety Act's "saving[s] clause, (like the express pre-emption

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158 See *Geier*, 120 S. Ct. at 1918 (citing *Medtronic*, 518 U.S. at 502-04). See also *Medtronic*, 518 U.S. at 502 (stating that "[t]hese state requirements therefore escape pre-emption, not because their source of the duty is a judge-made common-law rule, but because their generality leaves them outside the category of requirements that [the federal statute] envisioned . . . ."); id. at 504-05 (Breyer, J., concurring in part and concurring in judgement) (stating that a federal statute would pre-empt a requirement in the form of a standard of care or behavior set forth by a state common-law tort action); id. at 509 (O'Connor, J., concurring in part and dissenting in part) (stating that state common-law tort actions do impose "requirements" and are thus pre-empted where those requirements differ from those imposed by federal statutory requirements).


Compliance with any Federal motor vehicle safety standard issued under this subchapter does not exempt any person from any liability under common law.

Id.

160 See *Geier*, 120 S. Ct. at 1918.

161 Id.

162 Id.

163 Id.

164 Id.

165 Id.

166 *Geier*, 120 S. Ct. at 1919 (citations omitted).

167 Id. (citing *Freightliner Corp., v. Myrick*, 514 U.S. 280, 287 n. 3 (1995)).
provision) does not bar the ordinary working of [implied] conflict pre-emption principles." 168

The Court stated that nothing in the text of the savings clause reflected Congress' intent to save common law tort suits that actually conflict with Standard 208. 169 The majority concluded that it could perceive of no rational basis for Congress requiring that manufacturers comply with Standard 208 as a precondition to the provision's applicability had it wanted the Act to "save" all state common-law tort actions, regardless of their actual conflict with the objectives of Standard 208. 170

The Court stated that its interpretation of the savings clause neither conflicted with its primary purpose nor eviscerated the clause from the Safety Act, 171 stating that the Court has repeatedly "decline[d] to give broad effect to a saving clauses where doing so would upset the careful regulatory scheme established by federal law." 172 Finally, the majority concluded: "the saving clause foreseees—it does not foreclose—the possibility that a federal safety standard will pre-empt a state common-law tort action with which it conflicts." 173

The Supreme Court then addressed the dissent's argument that the preemption provision, 174 the savings clause, 175 or both taken together, create a kind of "special burden" disfavoring ordinary preemption principles, which a court must impose on a party claiming conflict preemption under these principles. 176 Rejecting this interpretation, the majority concluded that the two provisions when read together express a "neutral policy, not a specially favorable or unfavorable policy, towards the application of ordinary conflict pre-emption principles." 177 In fact, the majority argued that the preemption provision demonstrates that the government sought to subject the auto industry to a "single, uniform set of federal safety standards." 178 The Court concluded that

168 Geier, 120 S. Ct. at 1919.
169 Id. (asserting that the words "compliance" and "does not exempt" in 15 U.S.C. § 1397(k) (1988) simply bar the defendant from arguing that compliance with Standard 208 automatically exempts it from state common law tort actions regardless of whether the Federal Government meant the standard to be an absolute requirement or merely a "floor" or minimum one), citing RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 4(b), Comment e (1997) (contrasting state law compliance defenses versus a federal claim of preemption).
170 See Geier, 120 S. Ct. at 1919.
171 Id. (reasoning that the savings clause still operated to remove state common law tort actions from the scope of the express preemption clause, thereby "preserv[ing] those actions that seek to establish greater safety than the minimum safety achieved by a federal regulation intended to provide a floor.").
173 Geier, 120 S. Ct. at 1920.
176 See Geier, 120 S. Ct. at 1920.
177 Id.
178 Id., citing H.R. REP. NO. 89-1776, at 17 (1966). "Basically, this preemption subsection is intended to result in uniformity of standards so that the public as well as industry will be guided by one set of criteria rather than by a multiplicity of diverse standards." Id.
this policy favors preemption of state common-law tort actions, because the laws that judges and juries make or apply could themselves "create uncertainty and even conflict . . . when different juries in different States reach different decisions on similar facts."179

The Court stated that there is nothing in either the Safety Act's text or in Supreme Court precedents that refers to a "special burden."180 The majority then rejected the argument that this "special burden" was reflected in a statement made by the Court in Freightliner Corp. v. Myrick,181 that "'at best' there is an 'inference that an express preemption clause forecloses implied preemption.'"182 The Court distinguished this statement by explaining that the statement was made in rejecting the absolute argument that an express preemption clause entirely bars the possibility of implied conflict preemption.183

The Court framed the final and fundamental question to be answered as "whether a common-law 'no airbag' action like the one before us actually conflicts with FMVSS [Standard] 208?"184 In answering this question, the majority closely examined the legislative and administrative history of Standard 208 up to the 1984 version promulgated under then Transportation Secretary Elizabeth Dole.185

The Court believed that under Secretary Dole, the 1984 version of Standard 208 reflected six significant considerations.186 The majority stated that these six considerations taken together reflected DOT's primary objective of obtaining a "variety--a mix of several different passive restraint systems."187 The DOT sought to accomplish this by setting a performance requirement for passive restraint systems and allowing devices such as airbags, automatic belts, or other automatic restraint systems.188

The Court stated that the DOT intentionally rejected a proposed "all airbag" requirement for Standard 208 and did so for several reasons.189 The 1984 version

179 See Geier, 120 S. Ct. at 1920.
180 See id. at 1920-21.
182 Geier, 120 S. Ct. at 1921 (quoting Freightliner, 514 U.S. at 289).
183 See Geier, 120 S. Ct. at 1921.
184 Id. at 1922.
185 Id. at 1922-24.
186 Id. at 1923-24 (citing 49 Fed. Reg. 28,983-29,003 (1984)). According to the Court in Geier, these considerations included: (1) buckled up seatbelts are a vital ingredient of automobile safety and if properly used would save thousands of lives; (2) in spite of the enormous risks, more than 80 percent of front seat occupants would not buckle their safety belts; (3) airbags could decrease the dangers from not buckling seat belts, but not entirely; (4) passive restraints have disadvantages such as intrusiveness and public dislike; (5) airbags pose special risks to out-of-position occupants such as children and small women in small cars; and (6) airbags are substantially more expensive than other automatic restraint systems. See Geier, 120 S. Ct. at 1923-24.
187 Geier, 120 S. Ct. at 1924.
188 See Geier, 120 S. Ct. at 1924 (citing 49 Fed. Reg. 28,996 (1984)).
189 See Geier, 120 S. Ct. at 1924 (citing 49 Fed. Reg. 29,001-002 (1984)). DOT rejected an "all airbag" standard because of safety concerns associated with airbags, and a fear that an all airbag standard would create a "backlash" that could be decreased if other alternatives were available; a
of Standard 208 purposefully sought to gradually phase-in passive restraint systems.190 This gradual "phase-in" was enforced in three annual stages.191 Ultimately, the DOT believed that the 1984 version of Standard 208 "embodied" the Secretary's policy judgment that safety would best be promoted if the manufacturers installed alternative protection systems in their fleets rather than one particular system in every car.192

The majority stated that to allow the petitioners' common-law tort action to succeed would be equivalent to finding that American Honda Motor Co. had a duty to the petitioner to install an airbag in the 1987 Honda Accord when they built it.193 This finding would have the effect of allowing a state to create law requiring manufacturers of "all similar cars to install airbags rather than other passive restraint systems, such as automatic belts or passive interiors."194 The Court found that the existence of such common-law causes of action would present an obstacle to the variety and mix of passive restraint systems that Standard 208 sought to employ.195

The Court stated that if this state common-law action was allowed to succeed, it would have required all District-of-Columbia manufacturers to install airbags in all of their model year 1987 new cars or face potential tort liability, while Standard 208 merely required ten percent be equipped with some type of passive restraint system.196 The majority held that the objective of Standard 208 was the development of a mix of alternative passive restraint devices, and the rule of state tort law would stand as an obstacle to the accomplishment of that objective.197 Since the Court had already held that the statute foresees the application of ordinary principles of preemption in cases of actual conflict, the Court held that the state common-law tort action was preempted.198

Id.

190 See Geier, 120 S. Ct. at 1924 (citing 49 Fed. Reg. 28,999-29,000 (1984)).
191 49 Fed. Reg. 28,962, 28,999 (1984). The 1984 version of FMVSS 208 required the "phase-in" to be completed in three annual stages as follows:

- A minimum of 10 percent of all cars manufactured after September 1, 1986, must have automatic crash protection. After September 1, 1987, the percentage is raised to 25 percent, and after September 1, 1988 it is raised to 40 percent; and after September 1, 1989 all new cars must have automatic crash protection.

193 See Geier, 120 S. Ct. at 1925.
194 Id.
195 Id.
196 Id.
197 Id.
198 See Geier, 120 S. Ct. at 1925, 1928.
B. The Dissenting Opinion

Justice Stevens, writing for the four Justice dissent, criticized the majority's holding, and "especially . . . the Court's unprecedented extension of the doctrine of pre-emption." The dissent framed the Court's holding as standing for the proposition that an interim regulation motivated by the Secretary of Transportation's desire to promote development of a variety of passive restraint devices prohibited state courts from deciding whether a manufacturer's failure to install an airbag in its vehicles created common-law liability under theories of negligence or defective design.

Justice Stevens stated that "[t]his case is about federalism," meaning respect for "the Constitutional role of the States as sovereign entities." The dissent characterized the Court's holding as creating a judge-made rule that was both unique and imprecise which could not be found in either a Congressional enactment or an Executive Order. Instead, Justice Stevens concluded that this new rule "has a unique origin: it is the product of the Court's interpretation of the final commentary accompanying an interim administrative regulation and the history of airbag regulation generally."

The dissent concluded that the objectives sought by Secretary Dole in adopting Standard 208 would not be frustrated by allowing state courts to decide whether in 1987 the life-saving benefits of airbags were sufficiently obvious that failure to install them in some cars might amount to a design defect. Justice Stevens criticized the majority's characterization of its rejection of the "presumption against pre-emption" and its reliance on regulatory history and commentary rather than either statutory or regulatory text as ordinary principles of conflict pre-emption.

The dissent framed the question presented as whether the Safety Act or Standard 208 promulgated by Secretary Dole in 1984 preempts common-law tort actions claiming that an automobile built in 1987 was "negligently and defectively designed because it lacked 'an effective and safe passive restraint system, including but not limited, to airbags.'" The dissent wrote that by

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199 Id. at 1928 (Stevens, J., dissenting).
200 Id.
201 Id. (quoting Coleman v. Thompson, 501 U.S. 722, 726 (1991)).
202 Geier, 120 S. Ct. at 1928 (Stevens, J., dissenting) (quoting Alden v. Maine, 527 U.S. 706, 713 (1999)).
203 See Geier, 120 S. Ct. at 1928 (Stevens, J., dissenting).
204 Id.
205 Id. at 1929.
206 Id. (citing Geier, 120 S. Ct. at 1922).
208 See Geier, 120 S. Ct. at 1929 (Stevens, J., dissenting) (citing 49 C.F.R. §§ 571.208, S4.1.3-S 4.1.4 (1998)).
enacting the Safety Act, Congress’ stated purpose was to “reduce traffic accidents and deaths and injuries to persons resulting from traffic accidents.”

The dissent then recounted the “complex and convoluted” legislative and administrative history of Standard 208.

Before beginning the dissent’s preemption analysis, Justice Stevens stated that he expressed no opinion on the merit or lack thereof of the petitioners’ claims but that he did believe that Honda’s good faith compliance with Standard 208 would not completely immunize it from liability. However, the dissent stated that such good faith compliance could be admissible to disprove claims of negligence and defective design, and may be used as evidence to foreclose the award of punitive damages.

1. The Dissent’s Express Preemption Analysis

Justice Stevens began the dissent’s express preemption analysis by stating that the “Supremacy Clause does not give unelected federal judges carte blanche to use federal law as a means of imposing their own ideas of tort reform on the states.” Under this view, the states as separate sovereigns within our federal system can create law providing tort remedies to victims of personal injury under their traditional police powers and such laws “are not to be pre-empted . . . unless it is the clear and manifest purpose of Congress to do so.”

The dissent found no express preemption of state common-law actions by Standard 208 and cited two specific grounds for this decision. First, unlike the broad preemption provisions examined in three other Supreme Court decisions, the Safety Act’s preemption provision contained the term “safety

212 See Geier, 120 S. Ct. at 1929-31 (Stevens, J., dissenting).
213 Id. at 1931.
214 See Geier, 120 S. Ct. at 1931 n.6 (Stevens, J., dissenting) (citing Wood v. General Motors Corp., 865 F.2d 395, 417 (1st Cir. 1988); RESTATEMENT (THIRD) OF TORTS; GENERAL PRINCIPLES § 14(b), and Comment g (Discussion Draft, April 5, 1999); Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 142-43 (1963)).
215 See Geier, 120 S. Ct. at 1931 (Stevens, J., dissenting).
216 Id. at 1931-32 (quoting Silkwood v. Kerr-McGee Corp., 485 F. Supp. 566, 583-84 (W.D. Okla. 1979) (“good faith belief in, and efforts to comply with, all government regulations would be evidence of conduct inconsistent with the mental state requisite for punitive damages’ under state law.”).
217 Geier, 120 S. Ct. at 1932 (Stevens, J., dissenting).
219 See Geier, 120 S. Ct. at 1932-34 (Stevens, J., dissenting).
220 Id. at 1933-34 (Stevens, J., dissenting) (citing Cipollone v. Liggett Group, Inc., 505 U.S. 504, 548-49 (1992)) (concluding that “[n]o requirement or prohibition . . . shall be imposed under State law” included common-law claims); CSX Transp., Inc. v. Easterwood, 507 U.S. 658, 664 (1993) (holding that an express statement in the Federal Railroad Safety Act of 1970 expressing an intent to preempt any conflicting state law, rule, regulation, order or standard relating to railroad safety
Justice Stevens viewed the ordinary meaning of this term to consist of positive enactments prescribed by legislatures or administrative agencies, and not judge or jury decisions in common-law tort suits.\textsuperscript{223}

Second, the dissent pointed out that the Safety Act, unlike the acts examined in the three previously cited cases, contains a savings clause\textsuperscript{224} expressly saving common-law tort actions.\textsuperscript{225} The dissent reasoned that by inserting the savings clause in the Safety Act, Congress unambiguously expressed a policy that conformity with a federal safety standard should not immunize a manufacturer from common-law liability.\textsuperscript{226} According to Justice Stevens, if Congress had intended such a result, it would have inserted a similar reference in the preemption provision.\textsuperscript{227} The dissent concluded that the Safety Act's preemption provision does not preempt state common-law tort actions.\textsuperscript{228}

\textbf{2. The Dissent's Implied Preemption Analysis}

The dissent gave three reasons for rejecting Honda's claim that imposing common-law liability for failure to install an airbag would frustrate the purposes and objectives of Standard 208.\textsuperscript{229} First, the text of the Safety Act contains a savings clause that "arguably denies the Secretary the authority to promulgate standards that would pre-empt common-law remedies."\textsuperscript{230} Second, the text of Standard 208 contains nothing about preempting state common-law causes of action.\textsuperscript{231} Third, the presumption against preemption assumes that "the historic police powers of the States [should] not... be superseded by the Federal Act unless that was the clear and manifest purpose of Congress."\textsuperscript{232}

First, the dissent again made reference to the savings clause in the Safety Act which "arguably denies the Secretary the authority to promulgate standards that

\begin{itemize}
  \item \textsuperscript{221} 15 U.S.C. § 1392(d) (1988).  
  \item \textsuperscript{222} See Geier, 120 S. Ct. at 1934 (Stevens, J., dissenting).  
  \item \textsuperscript{223} Id.  
  \item \textsuperscript{225} Geier, 120 S. Ct. at 1934 (Stevens, J., dissenting).  
  \item \textsuperscript{226} See id.  
  \item \textsuperscript{227} Id. (citing Chicago v. Environmental Defense Fund, 511 U.S. 328, 338 (1994)) (noting the presumption that Congress acts intentionally by including particular language in one portion of a statute but omitting it in another).  
  \item \textsuperscript{228} See Geier, 120 S. Ct. at 1934 (Stevens, J., dissenting).  
  \item \textsuperscript{229} Id. at 1935.  
  \item \textsuperscript{230} Id.  
  \item \textsuperscript{231} Id.  
  \item \textsuperscript{232} Id. at 1939 (quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)).
\end{itemize}
would pre-empt common-law remedies." The dissent then moved to the textual argument of Standard 208.

The dissent rejected Honda’s argument that allowing manufacturers to incur the risk of common-law liability for negligence and defective design in failure to install airbag cases would frustrate the Secretary’s policy in enacting Standard 208. According to Honda, the Secretary sought to promote safety by gradually phasing-in a passive restraint requirement and allowing manufacturers a choice of several alternatives instead of requiring the use of one specific system such as airbags. The United States, in an Amicus brief, argued that if manufacturers had known in 1984 that they might later be liable for common-law claims for defective design in failure to install cases, they probably would have installed airbags in all their cars, and this result would frustrate the Secretary’s safety objectives and the procedures established to meet them.

The dissent found three errors in this line of reasoning. First, the pre-1984 risk of liability failed to lead to pervasive airbag installation by manufacturers. Second, Standard 208’s phase-in period would have ended prior to the time when “its purposes could have been frustrated by the specter of tort liability.” Third, all of the standards set by the Safety Act establish a minimum requirement, not a maximum.

Additionally, Justice Steven’s stated that even if allowing a choice to manufacturers and the implementation of a gradual phase-in were key considerations of the Secretary in promulgating Standard 208, “there is nothing in the Standard, the accompanying commentary, or the history of airbag regulation to support the notion that the Secretary intended to advance those purposes at all costs . . . .” The dissent concluded that Honda failed to cross the “high threshold” required to preempt state laws that purportedly frustrate the federal law’s purpose. The dissent stated that Honda failed to show that allowing a “failure to install” lawsuit would impose a requirement on manufacturers that “directly and irreconcilably contradicts any primary objective that the Secretary set forth with clarity in Standard 208.”

Justice Stevens carefully noted that Standard 208 contains no expression of an intent to preempt state law, and this silence bolsters the conclusion that the

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233 See Geier, 120 S. Ct. at 1935 (Stevens, J., dissenting).
234 Id.
235 Id. at 1936.
236 Id.
237 Id. (citing Brief for United States as Amicus Curiae at 25, Geier v. American Honda Motor Co., Inc., 120 S. Ct. 1913 (2000)).
238 See Geier, 120 S. Ct. at 1936 (Stevens, J., dissenting).
239 Id.
240 Id.
241 Id. at 1937.
243 See Geier, 120 S. Ct. at 1938 (Stevens, J., dissenting).
244 Id.
continued existence of common-law liability in this type of case "poses no
danger of frustrating any of the Secretary's primary purposes in promulgating
Standard 208."245

Justice Stevens stated that the majority failed to apply the traditional
presumption against preemption in analyzing conflict preemption.246 To the
dissent, this presumption is "rooted in the concept of federalism," and "start[s] with the assumption that the historic police powers of the States [should] not ... be superseded by the Federal Act unless that was the clear and manifest purpose of Congress."247

The dissent believed that this presumption against preemption places the
power of preemption in Congress.248 Justice Stevens believes that the legislative
branch is better suited to achieve the appropriate balance between the states and
the federal government, especially in areas where the states have historically
regulated.249 Thus, the checks and balances intrinsic in the legislative process
would prevent the encroachment of the federal government on vital state
interests.250

Justice Stevens stated that administrative agencies, like the NHTSA, are ill
equipped to represent the state's interests, yet they still promulgate
comprehensive regulations with broad preemptive consequences for the states.251
In the dissent's view, in situations where implied regulatory preemption is at
issue the Court "expect[s] an administrative regulation to declare any intention
to preempt state law with some specificity."252 Moreover, Justice Stevens stated
that "because agencies normally address problems in a detailed manner and can
speak through a variety of means...we can expect that they will make their
intentions clear if they intend for their regulations to be exclusive."253

The dissent stated that the typical agency rulemaking process provides
affected states notice and an opportunity to take an active part in the
proceedings, especially proceedings concerning preemption decisions.254 Justice
Stevens found that Honda had failed to overcome the presumption against
preemption because "[n]either Standard 208 nor its accompanying commentary include[d] the slightest specific indication of an intent to pre-empt common-law no-airbag suits."255

245 Id. at 1938-39.
246 Id. at 1939.
247 Id. (quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)).
248 See Geier, 120 S. Ct. at 1939 (Stevens, J., dissenting).
249 Id.
250 Id. (citing Garcia v. San Antonio Metro. Transit Auth., 469 U.S. 528, 552 (1985)) (citations
omitted).
251 See Geier, 120 S. Ct. at 1940 (Stevens, J., dissenting).
252 Id. (citing California Coastal Comm'n v. Granite Rock Co., 480 U.S. 572, 583 (1987));
Hillsborough County v. Automated Medical Laboratories, Inc., 471, U.S. 707, 717-18 (1985)).
253 Geier, 120 S. Ct. at 1940 (Stevens, J., dissenting) (quoting Fidelity Fed. Sav. & Loan Ass'n v.
De la Cuesta, 458 U.S. 141, 154 (1982)).
254 See Geier, 120 S. Ct. at 1940-41 (Stevens, J., dissenting).
255 Id. at 1941.
Justice Stevens criticized the majority’s “unprecedented use of inferences from regulatory history and commentary as a basis for implied preemption.” He concluded his dissent by observing that neither the text of the Safety Act nor Standard 208 contained any intent to preempt state common-law causes of action, and that he was convinced that the defendants had not overcome the presumption against preemption.

V. ANALYSIS OF GEIER V. AMERICAN HONDA MOTOR CO., INC.


The Supreme Court correctly held that the Safety Act’s express preemption provision did not preempt state common-law tort actions. This decision is neither surprising nor monumental considering that with the exception of one decision, the Supreme Court and every Federal Circuit Court to consider this issue has held that the Safety Act’s express preemption provision does not preempt state common-law tort actions.

In Geier, the Supreme Court wisely provided lower courts with a judicious method of analyzing whether the preemption provision of the Safety Act expressly preempts state common-law causes of action. In its new analysis,
courts no longer need to determine the exact meaning of the word "standard," as opposed to "requirement." Under this view, the Safety Act's savings clause demonstrates that Congress intended to preserve a substantial number of common-law tort actions. Thus, the Act's express preemption provision should be read narrowly to exclude common-law tort actions in order to carry out Congress' purposes and objectives. Read as such, the Safety Act should be seen as merely creating a "floor" or minimum standard, allowing room for state common-law tort actions to operate.

In three prior instances, the Court concluded that a broadly worded preemptive provision in a statute could be read as including state common-law tort actions. In the absence of a savings clause, it is possible that a court could read the Safety Act's express preemption provision, standing by itself, as applicable to state common-law actions, in addition to state legislative enactments and regulations.

Moreover, a broad reading of the preemption provision, absent a savings clause, could possibly preempt all non-identical state "standards" established in common law tort actions concerning the same performance feature as its counterpart federal standard, even if the federal standard merely established a "floor." However, the Court correctly held that the presence of the savings clause in the Safety Act mandates a narrow reading of the preemption provision and removes common law tort actions from the reach of the express preemption provision.

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265 Id. (concluding that the presence of a savings clause in the act resolves the disagreement).
267 See Geier, 120 S. Ct. at 1918 (stating that the presence of the savings clause assumes that there are many common-law claims to save). See also id. at 1934 (Stevens, J., dissenting) (stating that the presence of the savings clause in the Act "unambiguously expresses a decision by Congress that compliance with a federal safety standard does not exempt a manufacturer from any common-law liability.").
268 See Geier, 120 S. Ct. at 1918. See Cipollone v. Liggett Group, Inc., 505 U.S. 504, 518, 519 (1992) (concluding that the Court's "presumption against preemption" of state laws required that only positive enactments by legislative or administrative bodies are preempted by the Federal Cigarette Labeling and Advertising Act of 1965, not state common-law damage actions).
269 See Geier, 120 S. Ct. at 1918 (citing Brief for United States as Amicus Curiae at 21, Geier v. American Honda Motor Co., Inc., 120 S. Ct. 1913, 1918 (2000) (No. 98-1811) (stating that a state tort action for defective design based on a vehicle's lack of antilock brakes would not be preempted by FMVSS 208)).
270 See Geier, 120 S. Ct. at 1933-34 (Stevens, J., dissenting) (citing Cipollone, 505 U.S. at 548-49) (concluding that "[n]o requirement or prohibition . . . shall be imposed under State law . . . " included common-law claims); CSX Transp., Inc. v. Easterwood, 507 U.S. 658, 664 (1993) (holding that an express statement in the Federal Railroad Safety Act of 1970 expressing an intent to preempt any conflicting state law, rule, regulation, order or standard relating to railroad safety required express preemption of a state common-law claim that a train speed under the Act's maximum was excessive) (citations omitted). See also Medtronic, Inc. v. Lohr, 518 U.S. 470, 502-03 (1996) (plurality opinion) (holding that any requirement imposed by a State or its political subdivisions may include common-law duties) (citations omitted).
271 See Geier, 120 S. Ct. at 1918.
272 Id.
273 Id.
The Safety Act's express preemption provision prohibits a state or political subdivision of the state from promulgating legislation or regulations governing safety standards that are not identical to the federal standard. However, it does not bar a state court from entering a common-law tort judgement for defective design.

B. Standard 208 Impliedly Preempts State Design Defect Claims for Failure to Install Airbags

1. The Effect of the Safety Act's Savings Clause

The Supreme Court appropriately held that the Safety Act's savings clause does not foreclose or limit the possibility of ordinary implied conflict preemption. Additionally, the Court reaffirmed its prior decision in *Freightliner Corp. v. Myrick* that the presence of an express preemption provision in the Safety Act does not foreclose the possibility of implied conflict preemption.

The savings clause states that "[c]ompliance with any Federal motor vehicle safety standard issued under this subchapter does not exempt any person from any liability under common law." The actual text of the savings clause unambiguously demonstrates congress' intent to preserve common-law liability. However, nothing in the text of the savings clause discloses a congressional intent to save state common-law tort actions that actually conflict with federal regulations. In fact, many circuit courts have held that the

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274 *See also* Brief for United States as Amicus Curiae at 14, 15, *Geier v. American Honda Motor Co., Inc.*, 120 S. Ct. 1913, 1918 (2000) (No. 98-1811) (concluding that the Safety Act bars state legislatures and administrative bodies from enacting safety standards that are different from the federal standard concerning the same aspect of performance, but it does not bar state courts from finding that a vehicle was defectively designed with respect to that feature).


277 *See Geier*, 120 S. Ct at 1919.


280 *See Geier*, 120 S. Ct. at 1919 (citing *Freightliner*, 514 U.S. at 288) (concluding that even though a statute contains an express preemption provision supports an inference that Congress did not intend to preempt additional matters, it does not mean that the presence of that express preemption provision completely bars any chance of implied preemption).


283 *Id.* at 1265 (concurring with other circuits that the savings clause does not preserve state tort actions that actually conflict with or subvert the purposes and methods of the federal design) (quoting *Pokorny v. Ford Motor Co.*, 902 F.2d 1116, 1125 (3rd Cir. 1990) ("it is well established that a savings clause like § 1397(k) does not 'save' common law actions that would subvert a federal statutory or regulatory scheme); *Taylor v. General Motors Corp.*, 875 F.2d 816, 827-28
"imposition of common-law liability for the 'defect' urged by...plaintiffs would have a regulatory effect not unlike that of any state law or regulation...that...would [in effect] create an actual conflict with the federal scheme."284

Reading the Safety Act's savings clause to foreclose or limit the operation of ordinary implied preemption principles would, in effect, allow a jury to impose a safety standard that actually conflicts with federal objectives.285 Such an interpretation of the savings clause would presume that this federal legislative act tolerates an actual conflict with state common-law, and permits a judge or jury to defeat the objectives of a federal regulatory scheme.286 As the Court has aptly stated, this would in effect, allow the act to "destroy itself."287 This could not have been Congress' intent in inserting the savings clause into the Safety Act.288

The Geier Court appropriately refused to interpret a savings clause broadly when doing so would disturb the closely guarded regulatory scheme established by the Safety Act.289 Thus, upon examination of prior federal circuit court precedent, and the traditional Supreme Court approach of narrowly construing savings clauses, the Court properly concluded that "the savings clause foresees--it does not foreclose--the possibility that a federal safety standard will pre-empt a state common-law tort action with which it conflicts."290

2. A State Common Law Action for Failure to Install Airbags Actually Conflicts With Standard 208 and Is Impliedly Preempted

A state law is impliedly preempted if it "actually conflicts with a . . . federal statute."291 An actual conflict between a state law and a federal statute exists when the state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."292

n.20 (11th Cir. 1989) ("a 'general' savings clause, such as that contained in the Safety Act, does not preclude the finding of implied preemption"); Wood v. General Motors Corp., 865 F.2d 395, 415-16 (1st Cir. 1988) (discussing a "general reluctance . . . to follow a savings clause if state law will actually conflict with a federal regulatory scheme"). See also Geier, 120 S. Ct. at 1919 (stating that textually, nothing in the savings clause's text discloses a Congressional intent to save state common-law causes of action that actually conflict with federal regulations).

284 Perry, 957 F.2d at 1265 (concluding that state common-law damage awards can have the effect of a regulation).
286 Id. at 1920.
287 Id. (citations omitted).
288 Id.
289 See Geier, 120 S. Ct. at 1919-20 (quoting United States v. Locke, 120 S. Ct. 1135, 1147 (2000)). See also American Telephone & Telegraph Co. v. Central Office Telephone, Inc., 524 U.S. 214, 227-28 (1998) (refusing to construe a savings clause as continuing a common-law action that is utterly inconsistent with the provisions of the statute causing the act to "destroy itself").
290 Geier, 120 S. Ct. at 1919.
292 International Paper, 479 U.S. at 492 (citations omitted).
A state common-law action alleging that a manufacturer's failure to install an airbag in a 1987 model automobile, when Standard 208 required only ten percent of the manufacturer's fleet nationwide to be equipped with any passive restraint devices, would stand as an obstacle to the gradual phase-in of passive restraints that Standard 208 deliberately imposed. Such a cause of action therefore should be impliedly preempted, because Standard 208 purposely sought to allow automobile manufacturers a choice among several passive restraint devices to use in their automobiles.

The DOT sought to gradually phase-in a variety or mix of these passive restraint devices rather than impose an “all-airbag” standard for several compelling reasons, and therefore allowed manufacturers a choice among several different passive restraint systems. A manufacturer was deemed “in compliance” with Standard 208 if it installed one of the types of passive restraint devices required by DOT in the percentage of its vehicles called for under the Standard.

In the Geier case, the phase-in required American Honda Motor Co. to install some type of passive restraint device in ten percent of the automobiles that it manufactured in model year 1987. American Honda complied with this requirement and installed passive restraint devices in ten percent of its 1987 model year vehicles.

This state common-law design defect action would stand “as an obstacle to the accomplishment and execution of” Standard 208’s objective of allowing manufacturers a variety or choice of passive restraints to install in their vehicles.

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293 See Geier, 120 S. Ct. at 1925.
294 Id.
295 Id. at 1922.
296 Id. at 1922 (citing 49 Fed. Reg. 28,962 (1984)) noting that:
DOT’s comments, which accompanied the promulgation of FMVSS 208, make clear that the standard deliberately provided the manufacturer with a range of choices among different passive restraint devices. Those choices would bring about a mix of different devices introduced gradually over time . . . [which] would thereby lower costs, overcome technical safety problems, encourage technological development, and win widespread consumer acceptance—all of which would promote FMVSS 208’s safety objectives.
Id. See also supra note 191.
297 See 49 Fed. Reg. 28,962, 28,996 (1984) (codified at 49 C.F.R § 571.208 (1984) (stating that this requirement may be complied with by “using automatic detachable or non-detachable belts, airbags, passive interiors, or other systems that will provide the necessary level of protection”).
298 Id. at 28,999 stated:
The Phase-In
The rule requires the manufacturers to follow a phase-in schedule for compliance with the automatic occupant protection requirements. A minimum of 10 percent of all cars manufactured after September 1, 1986, must have automatic occupant crash protection. After September 1, 1987, the percentage is raised to 25 percent; after September 1, 1988, it is raised to 40 percent; and after September 1, 1989, all new cars must have automatic occupant crash protection.
Id.
299 See Geier, 120 S. Ct. at 1925.
300 Id. at 1916, 1917.
and thus was impliedly preempted. Standard 208 sought a gradually phased-in variety of alternative passive restraint systems. If allowed to succeed, the state common-law action would have the effect of requiring auto manufacturers to install airbags in all their vehicles or face recurring product liability suits in state courts. Moreover, these common-law suits would have the effect of defining the standard retroactively: lawsuits filed in 2000 would set safety standards for vehicles built in model year 1987. This would be the functional equivalent of setting a safety standard in contravention of Standard 208. It is evident that the existence of a cause of action which imposes liability based solely on a manufacturer's failure to install airbags would stand as an obstacle to Standard 208's objectives which included allowing manufacturers flexibility and fostering a diversity of approaches during the gradual passive restraint phase-in period.

In promulgating Standard 208, the agency sought to bring about a gradual phase-in of a variety of passive restraint systems. It was the belief of the agency at the time that this would be the most effective way to foster the development of "crashworthy vehicles." The Court in *Geier* correctly interpreted the Safety Act's savings clause, and its ultimate holding is reinforced by numerous federal circuit court decisions that arrived at the same result by applying an implied preemption analysis to failure to install cases.

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301 *Id.* at 1925, 1926 (citing *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941); *International Paper Co. v. Ouellette*, 479 U.S. 481, 493 (1987); *Fidelity Federal Sav. & Loan Ass'n v. De la Cuesta*, 458 U.S. 141, 156 (1982). *See also Geier v. American Honda Motor Co., Inc.*, 166 F.3d 1236, 1243 (D.C. Cir. 1999) (concluding that allowing state tort claims asserting defective design for failure to install an airbag would interfere with the regulatory scheme chosen by the DOT to achieve the goals of the Safety Act, the common-law action is preempted).

302 *Id.* at 1925.

303 *See generally id.*

304 *Id.* at 1920 (stating that the Court can find nothing in either the preemption provision or the savings clause that "favor [s] one set of policies over the other where a jury imposed safety standard actually conflicts with a federal safety standard" (emphasis added)).

305 *See Geier*, 120 S. Ct. at 1925.

306 *Id.* at 1928.

307 *See generally id.*

308 *Id.* concluding that:

FMVSS 208 sought a gradually developing mix of alternative passive restraint devices for safety-related reasons. The rule of state tort law for which petitioners argue [that a vehicle that lacks an airbag is defectively designed] would stand as an "obstacle" to the accomplishment of that objective. And the statute foresees the application of ordinary principles of pre-emption in cases of actual conflict. Hence, the tort action is pre-empted.

310 *Id.*
3. The Geier Court’s Interpretation of the Savings Clause and Its Potential Impact on Future Design Defect Claims

The Supreme Court in *Geier* correctly interpreted the Safety Act’s savings clause as precluding the use of “compliance with Standard 208” as a defense that would immunize defendant automobile manufacturers from common-law tort liability.\(^{311}\) This conclusion is significant because it interprets the savings clause as creating only a minimum requirement.\(^{312}\) Evidence of compliance may still be relevant to this determination.\(^{313}\) Under this view, common-law product liability actions are preserved, but the plaintiff must prove that the vehicle is otherwise defective despite evidence of the manufacturer’s compliance with the minimum standard imposed under FMVSS 208.\(^{314}\)

The Geier Court’s recent interpretation of the savings clause does not eviscerate it from the Safety Act.\(^{315}\) Quite the opposite, under this view, the savings clause has a dual purpose: first, it establishes that the express preemption provision does not preempt state common-law tort actions; and second, it preserves those state common-law claims that that create a higher safety standard than the minimum required under Standard 208.\(^{316}\)

This decision will provide a significant advantage to future tort victims. In fact, both the majority and the dissent expressly stated that the savings clause preserves common-law actions that establish that a greater safety design was possible.\(^{317}\) Thus, a manufacturer may not be held liable for the simple failure to install airbags in all its vehicles.\(^{318}\) However, once the manufacturer makes the decision and installs a particular passive restraint system, such as an air bag, it may be subject to state common-law tort liability for defective design of that state tort claims asserting defective design for failure to install an airbag would interfere with the regulatory scheme chosen by the DOT to achieve the goals of the Safety Act, the common-law action is preempted).

311 See *Geier*, 120 S. Ct. at 1919 (The words 'compliance' and 'does not exempt,' 15 U.S.C. § 1397(k) (1988), sound as if they simply bar a special kind of defense, namely, a defense that compliance with a federal standard automatically exempts a defendant from state law, whether the Federal Government meant the standard to be an absolute requirement or only a minimum one) (citing RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 4(b) Comment (e) (1997)) (distinguishing 'state-law compliance defense and a federal claim of preemption'); Perry v. Mercedes Benz of North America, Inc, 957 F.2d 1257, 1265 (5th Cir. 1992) (concluding that once a manufacturer chooses an available option, Standard 208 simply establishes minimum performance requirements for the device; it does not remove common-law tort liability which the savings clause preserves).

312 See *Geier*, 120 S. Ct. at 1919 (stating that the savings clause preserves those common-law actions seeking to create greater safety than the minimum achieved by a federal standard intended to provide only a floor).

313 See *Geier*, 120 S. Ct. at 1931 (Stevens, J., dissenting) (stating that good faith compliance with Standard 208 would not provide a manufacturer with an absolute defense, but would be admissible to disprove charges of negligent and defective design).

314 Id.

315 See *Geier*, 120 S. Ct. at 1919.

316 Id.

317 Id.; see also id. at 1931 (Stevens, J., dissenting).

318 Id. at 1922, 1927.
device. Under this interpretation of the savings clause, compliance with Standard 208's minimum requirements does not immunize a manufacturer from liability in all classes of state common-law design defect cases. It merely eliminates the claim that the lack of a particular passive restraint device such as an airbag makes a vehicle per se defective, while preserving "those actions that seek to establish greater safety than the minimum achieved by a federal regulation intended to provide a floor." Standard 208 merely provides a "minimum standard for motor vehicle performance, or motor vehicle equipment performance." The Safety Act's savings clause provides that compliance with Standard 208 does not immunize any person from liability under common law and "contemplates that manufacturers may be held liable for failure to exceed these minimum standards when their decisions were unreasonable.

In Geier, the Supreme Court concluded that Standard 208 merely establishes a minimum standard or "floor" for automobile safety. This proposition was not novel at the time of the decision. In 1992, a forward thinking federal circuit court applied this "minimal" approach to interpreting Standard 208. In Perry v. Mercedes Benz of North America, Inc., the plaintiff was injured when her vehicle's airbag failed to inflate upon impact in an automobile accident. She asserted that her car's airbag had an unreasonably dangerous "deceleration velocity deployment threshold" even though it met the "minimum requirements" of Standard 208. The plaintiff did not dispute the manufacturer's decision or choice to install airbags in its cars, but instead argued that the airbag should have been designed in a manner that was safer even though such a design would exceed the minimum required under federal law.

The Perry court held that allowing state tort liability for the manufacturer's failure to design its airbags to perform in a manner that effectively exceeds the

320 See Geier, 120 S. Ct. at 1919.
321 Id.
322 15 U.S.C. § 1391(2) (1988) ("Motor vehicle safety standards" means a minimum standard for motor vehicle performance, or motor vehicle equipment performance, which is practicable, which meets the need for motor vehicle safety and which provides objective criteria).
325 See Geier, 120 S. Ct. at 1919.
327 Id.
328 Id. at 1259.
329 Id. at 1259 n.1 ("The airbag system's 'deceleration velocity deployment threshold' determines the force that must be caused by the vehicle's sudden deceleration to trigger inflation of the airbag. [Mercedes Benz] . . . designed the system in Perry's vehicle with a minimum threshold of twelve miles per hour against a rigid barrier.").
330 Id. at 1259, 1260.
331 Id.
The federal minimum standards would not stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Standard 208. The Perry court based its holding on the effect of the Safety Act's savings clause which preserves common-law tort liability under the theory that Standard 208 merely creates a minimum safety standard or "floor."

Two recent federal circuit court decisions exemplify the disparate results that the circuits have produced when ruling on similar factual scenarios. Liability in these cases often turns on whether the court interprets the savings clause in a manner that preserves common-law tort actions that seek to establish a greater safety standard than the minimum required under Standard 208. In James v. Mazda Motor Corp., the plaintiff was killed when her 1994 Mazda Protege was forced off the road and crashed into the highway median. The plaintiff's automobile employed a passive restraint system consisting of an automatic two-point shoulder belt, and a manual lap belt that the plaintiff was not wearing at the time of the accident. In the wrongful death action which followed, the plaintiff's complaint alleged that the automobile's manual lap belt had been defectively designed and that Mazda had negligently failed to warn consumers that the Protege was dangerous unless the lap belt was utilized.

The court affirmed the district court's grant of summary judgment to the defendant in a perfunctory five page opinion, devoid of meaningful analysis, citing a prior Eleventh Circuit case and the Supreme Court's recent opinion in

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332 See Perry, 957 F.2d at 1264.
333 Perry, 957 F.2d at 1265-66 states:

Once the manufacturer chooses an option that includes an air bag system, Standard 208 merely set[s] forth minimum performance requirements for that system. To allow tort liability for the design of that system would not remove or require any particular choice, or otherwise frustrate "flexibility" that the federal scheme provides. We recognize that the manufacturer who chooses to meet only the bare minimum performance requirements will be burdened with the potential for tort liability, but this is the exact burden that Congress preserved in the Savings Clause, when it stated that "[c]ompliance with any Federal motor vehicle safety standard . . . does not exempt any person from liability under common law." Congress sought to meet its goal of minimizing the number of deaths and injuries caused by auto accidents by setting forth minimum standards and leaving common law liability in place.

Id.
335 James v. Mazda Motor Corp., 222 F.3d 1323 (11th Cir. 2000).
336 See James, 222 F.3d at 1323, 1324.
337 Id. at 1324.
338 Id.
339 See James, 222 F.3d at 1326-27.
340 See id. at 1325 (quoting Irving v. Mazda Motor Corp., 136 F.3d 764 (11th Cir. 1998)) (holding that "(1) Irving's common law 'defective design claim is not expressly preempted by [FMVSS 208]' (2) Irving's 'suit against Defendants for their exercise of an option provided to Defendants by FMVSS 208 conflicts with federal law and, thus, is [impliedly] preempted,' and (3) Irving's 'failure-to-warn claim--which is, in this case, dependent on the preempted defective-design claim--was properly dismissed [because it was also preempted]"") (internal citations omitted).
The court stated that "[t]he Supreme Court made clear that, despite a savings clause in the National Traffic and Motor Vehicle Safety Act, . . . courts should apply normal implied preemption principles to determine if a state common law action 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." In criticizing the plaintiffs' complaint, the court stated "[w]e are not sure that the plaintiffs read the same Geier opinion that we have read." Upon examination of the Eleventh Circuit's terse opinion in James, one would wonder what version of the Geier opinion that the Eleventh Circuit read.

The court stated that "[a]s an initial matter, we find no error in the [district] court's conclusion that the passive two-point shoulder belt and manual lap belt complied with FMVSS [Standard] 208." The Eleventh Circuit clearly misapprehended the Supreme Court's decision in Geier.

The Geier opinion stands for three simple propositions. First, given the presence of the savings clause, the Safety Act's express preemption provision must be read narrowly to exclude all common-law actions. Second, common-law tort actions which attempt to impose liability based upon a manufacturer's decision concerning the type of passive restraint system to install among alternatives available under Standard 208 at the time the vehicle was manufactured would "stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress and are thus impliedly preempted." Third, both the majority and the dissent declared that once a manufacturer chooses the type of passive restraint system to install, Standard 208 merely creates a "floor" or a minimum standard. Thus "[t]o allow tort liability for the design of that system would not remove or require any particular

341 Geier, 120 S. Ct. at 1913.
342 James, 222 F.3d at 1326 (quoting Geier, 120 S. Ct. at 1921).
343 Id. at 1326.
344 Id. at 1325 (emphasis added).
345 See Geier, 120 S. Ct. at 1918.
346 Id. at 1919.
347 Id. at 1919 states that:
Nothing in the language of the savings clause suggests an intent to save state-law tort actions that conflict with federal regulations. The words '[c]ompliance' and 'does not exempt,' sound as if they simply bar a special kind of defense, namely, a defense that compliance with a federal standard automatically exempts a defendant from state law, whether the Federal Government meant that standard to be an absolute requirement or only a minimum one . . . [The savings clause] preserves those actions that seek to establish greater safety than the minimum safety achieved by a federal regulation intended to provide a floor.

Id. (internal citations omitted) (alteration in the original).
348 Id. at 1931 (Stevens, J., dissenting) states:
I express no opinion on the possible merit, or lack of merit, of those claims. I do observe, however, that even though good-faith compliance with the minimum requirements of Standard 208 would not provide Honda with a complete defense on the merits, I assume that such compliance would be admissible evidence tending to negate charges of negligent and defective design.

Id. (internal citations omitted).
choice, or otherwise frustrate ‘flexibility’ that the federal scheme provides.”

State common-law tort actions that merely allow a jury to determine whether a manufacturer’s compliance with Standard 208 was sufficient to provide a reasonably safe design or whether a safer design was necessary are not impliedly preempted by Standard 208.

The introduction to this note refers to the case of King v. Ford Motor Company. Factually, King is tragically on all-fours with the James case. In King, the driver of a 1992 Ford Escort was killed when she executed a defensive maneuver to avoid colliding with a vehicle that made an improper left turn. The Escort employed an automatic two-point shoulder belt, a knee bolster, and a manual lap belt.

The driver suffered catastrophic injuries and ultimately died as a result of the accident. Her estate sued Ford Motor Company and Mazda Motor Corporation collectively in federal district court alleging theories including: failure to install an airbag, a defective and unreasonably dangerous automatic seat belt restraint system, and failure to warn of the dangers of the automatic restraint system.

The district court dismissed the claim for failure to install an airbag on summary judgment due to its implied conflict with Standard 208, and the Sixth Circuit did not challenge this ruling. However, the district court denied the defendant’s motion to dismiss the claims of defective design and failure to warn allowing them to proceed to the jury who returned a verdict for the plaintiff on both claims. Ford appealed, arguing that the plaintiff’s common-law tort action alleging that two-point, automatic seatbelts with manual lap belts are inherently defective would limit the manufacturer’s flexibility in choosing a passive restraint system and was thus impliedly preempted by Standard 208.

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350 Id.
352 See id. at 890.
353 Id., n.1 (stating that a knee bolster is a large pad in the lower portion of the instrument panel intended to restrain the body’s lower torso when it slides forward in a frontal collision by allowing the occupant’s knees to strike the pad and absorb the energy of the lower torso).
354 Id.
355 Id.
356 Id.
357 See King, 209 F.3d at 890, 891.
358 Id.
359 Id. at 891.
360 Id at 892 citing 49 C.F.R. § 571.208, S4.1.4-S4.1.4.2.2 stating that:

Standard 208 . . . requires passenger cars manufactured after September 1, 1989 but before September 1, 1993, . . . to comply with one of three front-seat occupant crash protection options: (1) a complete passive restraint system; (2) a passive system (automatic seat belts or air bags) for frontal crash protection, manual belts for lateral crashes and rollovers, and a warning system; or (3) manual front seat belts with a warning system.
The Sixth Circuit, without the benefit of the Geier opinion, nonetheless correctly applied the analysis first developed in Perry. This analysis delivered a result consistent with the Supreme Court’s reasoning in Geier.

The Sixth Circuit wisely held that the plaintiff’s defective design claim was not impliedly preempted by Standard 208. The court concluded that the plaintiff’s claim did not assert that the design choice made by the manufacturer to install an automatic shoulder belt and a knee bolster was inherently defective. On the contrary, the Sixth Circuit concluded that the plaintiff’s merely asserted that “the specific design was defective due to failure to use load limiters, and/or change the location of the knee bolster and/or change the location of the belt anchor.” The Sixth Circuit also held that the plaintiff’s failure to warn claim which alleged that defendant failed to adequately warn the decedent that failing to wear the lap belt could lead to lethal injuries caused by the shoulder restraints was not impliedly preempted by Standard 208.

In arriving at this decision, the court analyzed Standard 208 as merely providing the “minimum standard[s] for motor vehicle[s] or motor vehicle equipment performance.” The court concluded that the Safety Act’s savings clause establishes that compliance with Standard 208 does not immunize a manufacturer from common-law liability, but instead “contemplates that manufacturers may be held liable for failure to exceed these minimum standards when their decisions were unreasonable.”

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361 See King, 209 F.3d at 892 (citing Irving v. Mazda Motor Corp., 136 F.3d 764, 768-69 (11th Cir. 1998) (holding that such a common law claim is preempted by Standard 208).
363 See King, 209 F.3d at 892.
364 Id.
365 See 49 C.F.R. § 571.209 (2000) (stating that a “[l]oad-limiter means a seat belt assembly component or feature that controls tension on the seat belt to modulate the forces that are imparted to occupants restrained by the belt assembly during a crash”). See also King, 209 F.3d at 894 (discussing excessive belt loads or tension levels on seat belts that exceed human tolerance levels).
366 King, 209 F.3d at 892.
367 Id. at 894 (discussing whether the warning on the vehicle’s visor was adequate, the court stated that the decedent may have known that not wearing a lap belt would decrease the effectiveness of the shoulder belt system and result in injuries caused by colliding with the car’s interior, but “she was not aware that the failure to wear the [lap] belt could lead to deadly injuries caused by the [tension of] the shoulder harness even in a relatively minor accident.”).
368 Id. at 894-95.
370 King, 209 F.3d at 892-93 (quoting Perry v. Mercedes Benz of North America, Inc., 957 F.2d 1257, 1265-66 (5th Cir. 1992)).

Once a manufacturer chooses an option that includes an airbag system, Standard 208 merely sets forth minimum performance requirements for that system. To allow tort liability for the design of that system would not remove or require any particular choice, or otherwise frustrate ‘flexibility’ that the federal scheme provides. We recognize that the manufacturer that chooses to meet only the bare minimum requirements will be burdened with the potential for tort liability, but this is the exact burden that Congress preserved in the Savings Clause when it stated that “[c]ompliance with any federal motor vehicle safety standard . . . does not exempt any person from liability under common law.
The court appropriately determined that the plaintiff’s claims did not challenge the choice that the defendants made in installing the two-point automatic passive restraint system, but instead challenged the manufacturer’s decision to comply with the bare minimum performance requirements of Standard 208. Thus, the Sixth Circuit, in complete harmony with the Supreme Court’s forthcoming decision in Geier, prophetically held that the plaintiff’s common-law claims were not impliedly preempted by Standard 208.

CONCLUSION

The history of Federal Motor Vehicle Safety Standard 208 has been “complex and convoluted.” However, the Supreme Court’s recent decision in Geier established three guiding principles governing any future preemption analysis.

First, due to the presence of the savings clause, the Safety Act’s express preemption provision must be read narrowly to include only state legislative acts or administrative regulations and to exclude state common-law tort actions. Second, tort actions that challenge a manufacturer’s choice of passive restraint systems among possible alternatives granted by Standard 208 would stand as an obstacle to the objectives of Standard 208 of allowing manufacturers a choice of systems to install. Such causes of action are thus impliedly preempted.

Finally and most significantly to both tort victims and automobile manufacturers, both the majority and the dissent in Geier concluded that once a manufacturer chooses the type of passive restraint system to install, Standard 208 merely creates a minimum standard or “floor.” The Safety Act’s savings clause preserves common-law tort actions although they may seek to establish liability for a manufacturer’s failure to exceed Standard 208’s

Id. See also Geier v. American Honda Motor Co., Inc., 120 S. Ct. 1913, 1919 (2000) (stating that the “[savings clause] preserves those actions that seek to establish greater safety than the minimum safety achieved by a federal regulation intended to provide a floor”).

371 See King, 209 F.3d at 892.

In the case at bar . . . plaintiff’s position was not that the design choice made by defendants for protecting against frontal collisions—an automatic shoulder belt and knee bolster—was inherently defective but that the specific design was defective due to failure to use load limiters and/or change the location of the knee bolster and/or change the location of the belt anchor.

Id.

372 Id.

373 Id. at 893.


375 See Geier, 120 S. Ct. at 1918.

376 See id. at 1928.

377 Id.

378 Id. at 1919.

379 Id. at 1931-32 (Stevens, J., dissenting).

380 Id. at 1919.
minimum safety standards. Thus, the Supreme Court judiciously wrested from defendant automobile manufacturers the use of "regulatory compliance" as a complete defense under Standard 208. Furthermore, after Geier, a defendant auto manufacturer's defense that compliance with Standard 208 automatically exempts it from state common-law, whether the Federal Government meant the standard as an absolute requirement or merely a minimum one, will prove both baseless and futile.

See Geier, 120 S. Ct. at 1919.

Id. (citations omitted). See also id. at 1931-32 (Stevens, J., dissenting) ("I do observe however that even though good-faith compliance with the minimum requirements of Standard 208 would not provide [a manufacturer] with a complete defense on the merits, I assume that such compliance would be admissible evidence to negate charges of negligent and defective design.") (citations omitted).

Id. at 1919.
INFORMANT RELIABILITY UNDER THE FOURTH AMENDMENT IN FLORIDA V. J. L.

by Amanda Lisenby

I. INTRODUCTION

A police dispatcher receives an anonymous tip that the First National Bank on the corner of Fourth Street and Maple Street will be robbed at 3:00 on Friday afternoon. Police officers arrive at the bank on Friday and, using surveillance and observation, confirm the information provided by the anonymous informant. The police observe a car parked in front of the bank. They see three males dressed in black get out of the car in which one male remains. The police observe the three males put on masks and enter the bank. The police arrest the men based on the informant’s tip, combined with observation sufficient to confirm the reliability and truthfulness of the tip. In this situation, even though the informant remained anonymous, the police were able to verify the informant’s reliability and knowledge based on police observation and corroboration of the information.

A police dispatcher receives a phone call from an anonymous informant that a female standing on the corner of Elm Street and Walnut Street is carrying a gun. The police proceed to the described location but observe no conduct that would confirm the tip’s reliability or truthfulness. However, the police dispatcher who answers the call recognizes the informant’s voice and knows that this voice has provided reliable information regarding possible criminal activity on three occasions within the last week. In this situation, the police cannot corrobore the information provided by the informant, but should the police rely on the fact that this informant has given reliable and authentic information in the past and conduct a search of the female for the concealed weapon?

A police dispatcher receives a call from an anonymous informant that a tall Caucasian male wearing blue jeans and a white T-shirt is preparing to board subway train, number 593, carrying a bomb. The police immediately proceed to the subway station. Do the police officers need to corroborate the tip’s reliability before searching the man described, or is this a situation where the danger alleged in the anonymous tip is so great as to justify a search without first confirming an informant’s reliability?

Police officers have a difficult job knowing whether to rely on an informant’s tip to conduct a search. This job is especially difficult in situations where the information provided is not verified or in situations presenting danger to the responding police officer or the general public. The courts have not conclusively assisted the police with this difficult job and are still debating over answers to these questions.

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1 Amanda Lisenby is a J.D. Candidate for 2002 at Salmon P. Chase School of Law, Northern Kentucky University; B.A. degree in English from Western Kentucky University.
This article examines the standard currently being applied by police to confirm the reliability of an informant’s anonymous tip and presents the question of what standard should be applied by police to provide uniformity and assurance that their searches will be legal. Part II provides a brief summary of the Fourth Amendment Search and Seizure Law and an overview of the facts in the case of Florida v. J. L. Part III provides an overview of: the court’s reasoning in Florida v. J. L., the holding by the majority, and the concurring opinion by Justice Kennedy. Part IV recommends a uniform standard, a four-part test, for determining an informant’s reliability in all situations where the police must rely on an informant’s tip as a basis for conducting a search. This standard balances the four elements of the test against the privacy rights of the individual protected by the Fourth Amendment.

II. BACKGROUND

A. Brief History of the Fourth Amendment Search and Seizure Law

1. Fourth Amendment

The Fourth Amendment of the United States Constitution governs all searches and seizures conducted by persons acting on behalf of the government. This Amendment prohibits unreasonable searches and seizures and requires a finding of probable cause before conducting a search. Even though the language of the Fourth Amendment does not expressly require the issuance of a warrant, the Supreme Court has imposed a warrant requirement for searches and seizures and in order for a warrantless search to be considered legal in the circumstances, the probable cause for searching without a warrant must be reasonable.

Items obtained during a legal search can be used as evidence at the criminal trial, but when the search is illegal, the typical remedy under the Fourth Amendment is to exclude the evidence obtained during the illegal search under

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2 Florida v. J.L., 120 S.Ct. 1375 (2000) (referring to the defendant by his initials, J.L., because he is a minor).
3 Id.
4 See U.S. CONST. amend. IV. The 4th Amendment provides:

The right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated, and no Warrants shall issue, but upon probable cause, supported by Oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized.

Id. See also Mapp v. Ohio, 367 U.S. 643, 655 (1961) (concluding that the Fourth Amendment is applicable to state officials through the Fourteenth Amendment Due Process Clause).
5 See U.S. CONST. amend. IV.
7 See Allen, supra note 6, at 883; see also Hill v. California, 401 U.S. 797, 804 (1971).
what is termed "the exclusionary rule." The exclusionary rule is a doctrine that prohibits the introduction at a criminal trial of evidence obtained in violation of a defendant's Fourth Amendment rights. In order to avoid the exclusion of evidence obtained during a search, the search must meet the Fourth Amendment's probable cause requirement.

A search warrant will be issued only if there is probable cause to believe that seizable evidence will be found on the premises or person to be searched. The officer requesting the warrant must submit an affidavit to the issuing magistrate containing sufficient facts and circumstances to enable the magistrate to make an independent evaluation of probable cause; the officer cannot merely present his conclusion that probable cause exists. Probable cause is the amount of suspicion required to justify the search by the governmental agent, weighed against the privacy interests protected by the Fourth Amendment. Probable cause to conduct a search requires a probability that evidence of a crime will be found in the particular place to be searched. If the court finds the requisite probable cause to justify the search, the evidence obtained can be used against the defendant at trial.

2. Informants

There are several ways in which a governmental agent can secure the necessary probable cause before conducting a legal search. One such way is through information provided from an informant who is known to be reliable or whose information can be independently corroborated or confirmed by the police.

Police officers use informants to provide them with the probable cause needed in their affidavit to the magistrate to justify a search warrant. Informants may have firsthand knowledge of criminal activity and can share this knowledge with police officers to prevent further criminal activity from

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9 See Weeks, 232 U.S. at 398.
10 Id.
11 See U.S. Const. amend. IV.
14 See Allen, supra note 6, at 889 (citing Ornelas v. United States, 517 U.S. 690, 695 (1996)).
15 See Allen, supra note 6, at 890; see also Illinois v. Gates, 462 U.S. 213, 238 (1983).
16 See Gates, 462, U.S. at 246; see also Mapp, 369 U.S. at 655.
18 See Draper, 358 U.S. at 312-313.
19 See Gates, 462 U.S. at 234 (stating that even if the informant's motives are dubious, if he provides an explicit and detailed account of the alleged crime combined with a statement that he observed the event firsthand, then this would entitle his information to greater weight).
occuring. Police, before relying on the informant’s information, must determine whether the tip provides them with the necessary probable cause.\textsuperscript{20}

To determine whether an informant’s tip establishes probable cause, the court may apply a totality-of-circumstances approach that includes the informant’s honesty, reliability and basis of knowledge.\textsuperscript{21} Under the totality-of-circumstances approach, the police officer makes a practical, common-sense decision based on all of the circumstances at hand or as set forth in the affidavit before conducting a search.\textsuperscript{22} Factors regularly cited for police officers to consider include: the informant’s veracity and basis of knowledge,\textsuperscript{23} the officer’s objective observations, information from police reports, modes or patterns of operation of certain kinds of lawbreakers, and any other inferences or deductions that a trained officer may make from that information.\textsuperscript{24}

However, an informant’s honesty, reliability, and basis of knowledge are difficult to determine when the informant’s identity remains anonymous.\textsuperscript{25} Anonymous tips alone rarely confirm the informant’s basis of knowledge or honesty\textsuperscript{26} and should not be relied on to conduct a lawful search, unless there is something from which one could conclude that the caller is either honest or his information reliable.\textsuperscript{27} Thus, some tips lacking indicia of reliability would require further investigation before a search would be authorized.\textsuperscript{28}

3. Terry Stops Under Terry v. Ohio\textsuperscript{29}

Police have the authority to briefly detain a person for investigative purposes, even if they lack probable cause to arrest.\textsuperscript{30} To make such a stop, police must have a reasonable suspicion supported by articulable facts of criminal activity or of involvement in a completed crime.\textsuperscript{31} If the police also have reasonable suspicion to believe that the detainee is armed and dangerous, they may also conduct a frisk or limited search to ensure that the detainee has no weapons.\textsuperscript{32} The scope of the frisk is generally limited to a patdown of the outer
clothing for concealed weapons.\textsuperscript{33} However, an officer may reach directly into an area of the suspect’s clothing without a preliminary frisk when the officer has specific information that a weapon is hidden there, even if the information comes from an informant’s tip lacking sufficient reliability to support a warrant.\textsuperscript{34}

In \textit{Terry v. Ohio},\textsuperscript{35} a plain-clothes detective became suspicious of two men standing on a street corner who repeatedly peered into a store window, walked by the store, and looked back at the store at least a dozen times.\textsuperscript{36} Police observed two men talk with a third man and then walk further up the street.\textsuperscript{37} The police officer followed the men and confronted them, believing them to be planning a robbery.\textsuperscript{38} The police officer then identified himself and asked the suspects for their names.\textsuperscript{39} The two men mumbled something, and the officer proceeded to conduct a patdown of one of the men.\textsuperscript{40} During the patdown, the officer felt a gun on the suspect, and the suspect was later charged with carrying a concealed weapon.\textsuperscript{41} The court held the stop and frisk valid because the police officer, even though lacking a search warrant, had a reasonable articulated suspicion that the individual was involved in criminal activity, which justified the stop.\textsuperscript{42} The officer also had a reasonable articulated suspicion that the individual was armed and dangerous, which justified the frisk.\textsuperscript{43}

Prior to \textit{Terry v. Ohio},\textsuperscript{44} any restraint on the person amounting to a seizure for the purposes of the Fourth Amendment was invalid unless justified by probable cause.\textsuperscript{45} \textit{Terry} created a limited exception to this general rule, holding that certain seizures are justifiable under the Fourth Amendment if there is suspicion that a person has committed or is about to commit a crime.\textsuperscript{46}

\textit{Adams v. Williams}\textsuperscript{47} applied the same approach found in \textit{Terry} in the context of an informant’s report that an unnamed individual in a nearby vehicle was carrying narcotics and a gun.\textsuperscript{48} In \textit{Adams}, the police officer immediately reached into the car of the suspect and removed the concealed gun from the defendant’s waistband.\textsuperscript{49} The court stated that when the defendant rolled down his window

\begin{thebibliography}{99}
\bibitem{33} \textit{id.} at 30.
\bibitem{34} \textit{See Adams}, 407 U.S. at 147-148.
\bibitem{35} \textit{Terry v. Ohio}, 392 U.S. 1 (1968).
\bibitem{36} \textit{See id.} at 5-6.
\bibitem{37} \textit{id.} at 6.
\bibitem{38} \textit{id.} at 6-7.
\bibitem{39} \textit{id.}
\bibitem{40} \textit{id.} at 7.
\bibitem{41} \textit{See Terry}, 392 U.S. at 7.
\bibitem{42} \textit{id.} at 30.
\bibitem{43} \textit{id.}
\bibitem{44} \textit{Terry v. Ohio}, 392 U.S. 1 (1968).
\bibitem{46} \textit{id.}
\bibitem{47} \textit{Adams v. Williams}, 407 U.S. 143 (1972).
\bibitem{48} \textit{See id.} at 146.
\bibitem{49} \textit{id.} at 145.
\end{thebibliography}
instead of complying with the police officer's request to get out of the car so that
his movements could more easily be monitored, the revolver at defendant's waist
became an even greater threat to the police officer's safety. The police officer
was justified in conducting the stop and frisk by reaching into the car and
removing the gun, based on the informant's report and on the officer's
reasonable articulated suspicion that the suspect was armed and dangerous.

B. Facts of Florida v. J.L.

On October 13, 1995, the police in Dade County, Florida, received an
anonymous complaint that a concealed weapon violation was taking place. The
informant told the police that the person concealing the weapon was one of
several young black males standing at a particular bus stop. The informant
provided a description of the males, advising the police that the male with the
gun was wearing a plaid shirt. Police officers went to the bus stop and verified
that there were three black males, one of whom, respondent J.L., was wearing a
plaid shirt. Apart from the informant's tip, the police officers had no
reasonably articulated suspicion as to the conduct of the three males.

Upon approaching the three males, the police officer did not observe any
unusual movements by the males, and there was no firearm in plain view. One
of the officers frisked J.L., seized a gun from his pocket, and took J.L. into
custody. J.L., a 15 year old, was charged under Florida law with carrying a
concealed firearm without a license and possessing a firearm while under the age
of 18. No information was obtained regarding the informant.

The trial court granted the respondent's motion to suppress the gun as the
fruit of an unlawful search. In granting the motion to suppress, the trial court
held that the gun was obtained by a warrantless, and therefore illegal, search
because the anonymous complaint was uncorroborated by the police officers,
and J.L. had displayed no suspicious activity which might have supported the
information provided by the anonymous informant. The intermediate appellate
court reversed the holding of the district court and held the search valid.

50 Id. at 148.
51 Id.
53 See id. at 1377.
55 Id.
56 See J.L., 120 S.Ct at 1377.
57 Id.
58 Id.
59 Id.
60 Id.
61 Id.
62 See J.L., 120 S.Ct. at 1377.
However, the Supreme Court of Florida quashed that decision, holding the search invalid under the Fourth Amendment. The Florida Supreme Court reasoned that the tip from the anonymous informant lacked sufficient "indicia of reliability" to establish the reasonably articulated suspicion necessary for a Terry investigatory stop and frisk.

### III. COURT'S REASONING

#### A. Holding of Florida v. J.L.

The Supreme Court of the United States affirmed the decision of the Florida Supreme Court, holding that an anonymous tip that a person is carrying a gun is not, without more, sufficient to justify a police officer's stop and frisk of that person. In reaching this conclusion, the majority began by examining the law regarding "stop and frisk" decisions, specifically *Terry v. Ohio*.

According to the holding in *Terry*, if a police officer observes unusual conduct that reasonably leads him to the conclusion that criminal activity may be in progress and that the person with whom he is dealing may be armed and presently dangerous, after identifying himself and making reasonable inquiries, he is entitled to conduct a limited search of the person's outer clothing to discover any weapons that could be used to assault him or endanger others in the area. However, the court concluded that in the present case, the police officer's suspicion that the respondent was carrying a weapon was not based on the officer's observance of respondent's unusual conduct as required in *Terry*, but arose instead from an anonymous caller whose information and reputation could not be assessed for reliability.

Even though the informant's identity remained anonymous, the court reasoned that there are situations, as in *Alabama v. White*, where an anonymous tip will provide the reasonable suspicion necessary to make an investigatory stop, provided that the information is suitably corroborated and provides the indicia of reliability necessary to make the stop and frisk valid. The court distinguished *Alabama v. White* from the present case, concluding that the

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65 *Id.* at 1378 (citing *J.L. v. Florida*, 727 So. 2d 204, 209 (Fla. 1998)).
68 *See id.* at 1377.
69 *Id.* at 1378 (citing *Terry v. Ohio*, 392 U.S. 1 (1968)).
70 *See Terry*, 392 U.S. at 30.
71 *See J. L.*, 120 S.Ct. at 1378.
72 *See Alabama v. White*, 496 U.S. 325, 331-332 (1990) (stating that an anonymous telephone tip asserting that the defendant would be leaving a specific apartment at a specific time, that she would going to a specific place, and that she would be in possession of cocaine was corroborated by the police who followed her to the specified location, and therefore, showed sufficient indicia of reliability to provide reasonable suspicion to make a lawful investigatory stop).
73 *See J.L.*, 120 S.Ct. at 1378 (citing *Alabama v. White*, 496 U.S. 325, 329 (1990)).
anonymous tip lacked the necessary "moderate indicia of reliability" which was both present and critical to the court's decision in White.75 The court regarded White as a "borderline" decision, and stated that knowledge about a person's future movements, as was the case in White, indicates some familiarity with that person's affairs, but such knowledge does not necessarily indicate the informant knows whether that person is carrying hidden contraband.76 The Supreme Court concluded that this case was distinguishable from White because the anonymous call concerning the respondent, J. L., provided no information about future movements and, therefore, left the police without a means to test the informant's knowledge or credibility.77 The fact that the allegation concerning the concealed weapon turned out to be true did not, by itself, give officers the right to frisk the respondent to test the credibility of the information.78 In this case, the police acted solely on information provided by an anonymous caller who never explained how he knew about the gun and never provided any reliable information to establish the truth of his statements.79

The court then examined an argument raised by the prosecution that the tip was reliable because its description of the suspect's clothing, location, and race proved accurate,80 and a similar argument presented by the United States as amicus curiae.81 The United States as amicus curiae argued that a stop and frisk should be allowed when the tip provides an accurate description of the person and his location, the police promptly verify the details of the informant's tip, and there are no factors that would cast doubt on the reliability of the anonymous informant's tip.82 The court stated that "[t]hese contentions misapprehend the reliability needed for a tip to justify a Terry stop."83 The court stated that this type of information will merely help police officers identify the person being accused, not show that the informant has any real knowledge about whether the person is carrying a concealed weapon.84 The reliability requirement calls for more than merely being able to identify the accused.85

A second argument raised by the prosecution and dismissed by the court concerned whether Terry should be modified to include a "firearm exception," under which any tip alleging a concealed weapon would justify an investigatory search even if the accusation would ordinarily fail the standard reliability test.86

75 See J.L., 120 S.Ct. at 1379.
76 Id.
77 Id.
78 Id.
79 Id.
80 Id. (citing Brief for Petitioner at 20-21, Florida v. J.L., 120 S.Ct. 1375 (2000) (No. 98-1993)).
82 Id. (quoting Brief for United States at 16, J.L. (No. 98-1993)).
83 J.L., 120 S.Ct. at 1379.
84 See id.
85 Id.
86 Id.
Before dismissing this contention, the court provided an analysis of the serious dangers associated with firearms in an attempt to justify the "firearm exception" proposed by the prosecution. However, the court concluded that this exception would "rove too far," providing any person with an opportunity to cause another to be searched simply by making a telephone call and reporting a concealed weapon. This exception would also create possible arguments that the same exception should apply to tips regarding narcotics. These exceptions are not allowed under the Fourth Amendment.

The court concluded that the facts presented in Florida v. J.L. did not require an inquiry into whether, in certain situations, the gravity of the danger alleged in an anonymous tip might justify a stop and frisk regardless of the reliability of the tip. The court stated that this decision does not diminish a police officer's discrentional ability to conduct a protective search for weapons of a suspect that he has already lawfully stopped. Based on the court's reasoning, the gun seized from the respondent was the fruit of an unlawful search.

B. Concurring Opinion of Justice Kennedy in Florida v. J.L.

The concurring opinion by Justice Kennedy agreed with the majority's opinion, yet he wrote his concurrence to provide an analysis of several anonymous tip situations that the court has not yet explored. One area that Justice Kennedy believes has not yet been explored by the court concerns the difficulty that arises for a reviewing court in determining the credibility of an anonymous informant when the call is truly anonymous. In this situation, the informant has not placed his credibility at risk and will be immune from the proceeding. Another area not examined by the majority opinion involves situations other than the prediction of future conduct of the alleged criminal that may support reliability, so that the tip does in fact provide a lawful basis for a search.

One such situation may occur when an anonymous caller on two successive nights provides information of criminal activity that does in fact occur, and the voice sounds the same each night. In this situation, a third call should not
automatically be treated like the tip in the *Florida v. J.L.*\textsuperscript{100} In this instance, there would be a justifiable argument that police experience may outweigh some of the uncertainty typically found in an anonymous informant situation.\textsuperscript{101} Another situation providing a lawful basis for a search may arise if the informant tells the police officer face-to-face of criminal activity.\textsuperscript{102} Justice Kennedy also reasoned that current technology provides police officers with a means to instantly identify the informant by sending police units to the location of the telephone used to report the information, and that the ability of police officers to trace the caller's identity may be a factor that leads to reliability.\textsuperscript{103}

IV. ANALYSIS OF OPINION

The problem that results from the court's holding in *Florida v. J. L.*\textsuperscript{104} that the gun seized was the fruit of an unlawful search, is the difficulty of deciding where to draw the line in determining an informant's reliability and in determining what limits are imposed on police power to arbitrarily frisk private citizens.\textsuperscript{105} How much intrusion on an individual's privacy and the Fourth Amendment right to be free from arbitrary searches is too much when the officer is relying on an anonymous informant? The court in *Florida v. J. L.*\textsuperscript{106} reasoned that *Alabama v. White*\textsuperscript{107} is a close case on one side of the line, the side allowing the intrusion.\textsuperscript{108} The court reasoned that White is a close case because while an informant's "[k]nowledge about a person's future movements indicates some familiarity with that person's affairs,...having such knowledge does not necessarily imply that the informant knows, in particular, whether that person is carrying hidden contraband."\textsuperscript{109} *Florida v. J. L.*\textsuperscript{110} falls on the other side of the line, the side that disallows the intrusion, because there is no predictive information with which to test the informant's knowledge or credibility.\textsuperscript{111} Thus, the problem arises as to when an anonymous tip has sufficient reliability to push it to the side of the line where the intrusion will not be excessive or unreasonable.\textsuperscript{112}

The answer to the questions surrounding when a stop and frisk is justified based solely on information provided by an anonymous informant is through a

\textsuperscript{100} See *J.L.*, 120 S.Ct. at 1381.
\textsuperscript{101} Id.
\textsuperscript{102} Id. (stating that if an informant risks revealing his identity by providing information to police face-to-face, then the court could consider this in gauging the reliability of the anonymous tip).
\textsuperscript{103} Id.
\textsuperscript{104} *Florida v. J. L.*, 120 S.Ct. 1375 (2000).
\textsuperscript{105} See generally id.
\textsuperscript{108} See *J.L.*, 120 S.Ct. at 1379.
\textsuperscript{109} Id. at 1379 (citing *Alabama v. White*, 496 U.S. 325, 332 (1990)) (emphasis added).
\textsuperscript{111} See id. at 1379.
\textsuperscript{112} Id. at 1378-1379.
uniform standard to determine the informant's reliability. As the law currently stands, there are different rules for different situations based on the totality-of-circumstances approach introduced and applied in Illinois v. Gates,\textsuperscript{113} that allows law enforcement officers to weigh the evidence and make common-sense decisions based on all of the surrounding circumstances.\textsuperscript{114} This standard is somewhat vague and grants police officers too much discretion in making on-the-spot decisions about whether to intrude upon an individual's protected privacy. The only way to assist police officers and courts in determining when the informant should be trusted, and, at the same time, still protect citizens from unlawful searches of their person, is to provide a uniform standard or test to apply when confronted with anonymous-tip situations.

However, the court stated in Adams v. Williams,\textsuperscript{115} that a uniform standard is not the correct standard to apply.\textsuperscript{116} The court stated that because informants' tips may vary greatly in their value and reliability, rigid legal rules are inappropriate for an area of such diversity.\textsuperscript{117} Yet, I propose a four-part balancing test to conclusively decide if a search is justified based on an anonymous tip. This four-part test is more in-depth and uniform than the Illinois v. Gates\textsuperscript{118} totality-of-circumstances approach, and contains factors that should be considered in every situation involving an anonymous tip reporting potential criminal activity. The presence of each of the four factors should be weighed against the protected privacy right of every citizen provided by the Fourth Amendment.

First, could the informant's identity be instantly and reasonably available to the police?\textsuperscript{119} If police officers can, within seconds, readily determine the identity of the anonymous informant, that informant's reliability can be immediately investigated to determine whether police should rely on the informant's tip and conduct a search.\textsuperscript{120} As Justice Kennedy states in his concurring opinion, instant caller identification is widely available to police, and squad cars can be sent within seconds to the location of the telephone used by the informant.\textsuperscript{121} Voice recording of telephone tips might be used to locate the caller.\textsuperscript{122} The ability of the police to trace the identity of anonymous telephone informants should be a factor that leads to determining reliability.\textsuperscript{123} When faced with the issue of whether a search was justified based on an anonymous tip, the first factor the court should consider is whether the police adequately

\textsuperscript{114} See id.
\textsuperscript{115} Adams v. Williams, 407 U.S. 143 (1972).
\textsuperscript{116} See Gates, 462 U.S. at 232 (quoting Adams v. Williams, 407 U.S. 143, 147 (1972)).
\textsuperscript{117} See Gates, 462 U.S. at 232.
\textsuperscript{119} See J.L., 120 S.Ct. at 1381 (Kennedy, J., concurring).
\textsuperscript{120} Id.
\textsuperscript{121} Id.
\textsuperscript{122} Id.
\textsuperscript{123} Id.
investigated the informant’s reliability by attempting to ascertain his identity. Successful identification of the informant is not required as long as the police officer reasonably attempts to find out the basis of the informant’s knowledge before relying on the tip and conducting the search.

However, this requirement might dissuade informants from providing information to the police if they know or reasonably believe that their identity may be discovered. In their eyes, this revelation of their identity would defeat the purpose of providing an “anonymous” tip. Yet, adoption of this approach is a chance worth taking. The effect of having a few less informants provide information to the police for fear of their identity being discovered is preferable to having police officers conduct unreasonable searches based solely on informant’s tips. This preference is especially the case when the officer could have reasonably tested the reliability and truthfulness of the tip by ascertaining the informant’s identity prior to conducting the search. As Justice Jackson stated in Brinegar v. United States, “[Fourth Amendment] rights are not mere second-class rights but belong in the catalog of indispensable freedoms.” The significance of Fourth Amendment rights far outweighs the possibility of fewer informants providing information for fear their identity may be discovered.

Second, did the informant provide any predictive movement or describe any actions that will be taking place in the future? In Alabama v. White, the fact that the informant was able to predict the defendant’s future behavior demonstrated that the informant was familiar with the defendant’s affairs. In White, the court reasoned that this predictive information alone was sufficient to believe that the caller was honest and well informed, and to impart some degree of reliability regarding the allegation.

However, using the proposed four-part test, this factor alone would not be sufficient to justify the search. Anyone could observe another person leaving at the same time every day to go to work and arriving home at the same time every day. This observer would then be able to tell police, with precision, the time that person will be leaving his house, where he will be going, and when he will be returning home. This relaying of precise information does not mean that the observer knows with certainty whether criminal activity is taking place or is going to take place. Just because the informant supplied information about the

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124 Id. (concluding that the ability of the police to discover the identity of an anonymous informant could be one factor which gives reliability to an otherwise unreliable anonymous tip).
126 See id. at 180 (Jackson, J., dissenting).
129 See id. at 332.
130 Id.
131 See J.L., 120 S.Ct. at 1379 (stating that while knowing about an individual’s future movements may demonstrate an informant’s familiarity with a person’s activities, that knowledge alone does not in itself mean that the informant knows that the person is involved in criminality).
132 Id.
133 Id.
person's future behavior does not conclusively provide enough reliability to justify a search.\textsuperscript{134} Yet, this factor is not unimportant in determining reliability. Ability of an informant to predict a suspect's activities is only one factor to be considered. Before police can justifiably rely on an anonymous tip, they must first determine if reliability can even be established through the inclusion of future behavior of the criminal defendant.\textsuperscript{135}

One possible problem with this prong of the test arises when an informant can only provide precise information of past criminal activity based on firsthand knowledge, and not of any criminal activity that will be occurring sometime in the future. For example, an informant provides police with information about a drug selling operation based on reliable firsthand knowledge because she recently purchased drugs from the suspect, but cannot tell police precisely if the suspect will be selling drugs in the future. Does this mean that their information on past criminal activity is not reliable solely because they also did not include information on future movement? The answer, of course, is no.

The second prong of this proposed test requires the police to inquire into whether the information described any predictive movement. In this example of a drug-buying informant, if taken literally, the second prong would not be met. However, the police can assume, based on their knowledge and experience as police officers, that a drug dealer will probably not sell drugs only once. They can be infer from the informant's tip that the criminal activity will occur again in the future. Whether or not the informant provides some prediction of future behavior is not conclusive, but should be considered with the other three factors of the proposed test to determine reliability before conducting the search.

Third, is the information corroborated or confirmed by police observation or investigation before the search is conducted beyond merely identifying the defendant?\textsuperscript{136} If the police officer can confirm the information provided by the informant by either observation or investigation, there is potentially a proper basis for conducting the search,\textsuperscript{137} but only when examined with the other three factors proposed herein. This corroborating factor alone will not be sufficient because there is still the slight chance that the informant is not telling the truth or that the tipster may be a personal enemy of the person he is reporting.\textsuperscript{138} Select parts of the information provided by the anonymous tipster may be confirmed as truthful, but this does not necessarily mean that all the information, including the potential criminal activity, is truthful.\textsuperscript{139} A tip that shows nothing more than that

\textsuperscript{134} Id.
\textsuperscript{135} Id. (stating that since the anonymous caller gave no predictive information concerning the defendant, the police lacked the ability to test the informant's "knowledge or credibility").
\textsuperscript{136} See Florida v. J.L., 120 S.Ct. 1375, 1379 (2000) (stating that an anonymous tip which fails to provide predictive information that can be corroborated by police observation is not reliable).
\textsuperscript{137} Id.
\textsuperscript{138} See United States v. DeBerry, 76 F.3d 884, 886 (7th Cir. 1996).
\textsuperscript{139} See J.L., 120 S.Ct. at 1379 (stating that knowing about a person's future activities does not, in itself, demonstrate that the informant knows that the person is involved in criminality).
the informant had seen the person he was reporting could easily be a lie and is therefore, not sufficiently corroborated.140

However, several cases hold that even if a tip that a person is armed and possibly dangerous is only weakly corroborated, the police are still entitled to stop the person and search him for the gun.141 Yet, these cases are inconsistent with the court's holding in Florida v. J. L.142 because one could easily argue that the informant's tip in Florida v. J.L. was "weakly" corroborated since the informant precisely described the defendant and his location.143

In J. L., the precise description of the defendant and his location was not enough to find any corroborating to justify the search.144 How much corroborative is needed for "weak" corroborations? With this proposed four-part test, corroborations alone would never be sufficient. Corroboration is just one factor to be considered when determining the justifiability of the search. This four-part test would easily solve the "weakly" corroborated issue because corroboration would be considered in light of the other three factors and then collectively balanced against privacy protection. Before conducting a search, police officers should attempt to corroborate the informant's tip to test for reliability.145

Finally, does the police officer reasonably believe he or she is in danger or that the public in general is in danger?146 Public interest must be considered in determining the reasonableness of a governmental intrusion, which includes substantial public concern for the safety of police officers and the general public.147 Whether a police officer reasonably believes she is in danger should be determined by looking at specific inferences that the officer is entitled to draw from the facts in light of her experience as a police officer.148 Police officers should not take unnecessary risks in performing their duties as an officer;149 and therefore, this prong of the test is vital to determining the legality of a search. The public interest in protecting police officers and in protecting the

140 See DeBerry, 76 F.3d at 886.
141 Id. (citing United States v. McClintch, 660 F.2d 500, 502-03 (D.C. Cir. 1981); United States v. Clipper, 973 F.2d 944, 949-51 (D.C. Cir. 1992); United States v. Bold, 19 F.3d 99, 103-04 (2d Cir. 1994)).
143 See id. at 1377.
144 Id. at 1380.
145 Id. at 1379 (concluding that the reasonableness of the police suspicion should be measured against the knowledge the officer's possessed before conducting their search).
146 See Florida v. J. L., 120 S.Ct. 1375, 1380 (2000) which states:

The facts of this case do not require us to speculate about the circumstances under which the danger alleged in an anonymous tip might be so great as to justify a search even without a showing of reliability. We do not say, for example, that a report of a person carrying a bomb need bear the indicia of reliability we demand for a report of a person carrying a firearm before the police can constitutionally conduct a frisk.

Id.
148 See Sakyi, 160 F.3d at 167 (citing Terry v. Ohio, 392 U.S. 1, 27 (1968)).
149 See Sakyi, 160 F.3d at 167 (citing Terry v. Ohio, 392 U.S. 1, 23 (1968)).
general public should be weighed against the individual's right to personal privacy, free from arbitrary intrusions by the police.\textsuperscript{150} In order to justify a search or a stop and frisk based on an anonymous tip, the police officer should have an appropriate level of suspicion of criminal activity and an apprehension of danger for himself or the general public before conducting the search.\textsuperscript{151} This danger factor should not be taken alone as sufficient, but should be considered in light of the three other factors proposed herein.

Once all four of the factors have been considered, either by the police officer when deciding whether to search or the court when deciding if a search was legal, the total factors present should be weighed against an individual's right of privacy and right to be free from unreasonable searches and seizures by the government. As long as the factors of the four-part test outweigh the individual's reasonable expectation of privacy, the search should be considered legal. Courts and police officers will have a uniform standard for deciding when to rely on an anonymous tip, using this balancing approach.

The effectiveness of this proposed four-part test can be shown by applying it to the three situations in the introduction and by applying it to the facts of Florida v. J.L.\textsuperscript{152} In the first situation, the police received an anonymous tip about a bank robbery, and then confirmed the information by police observation. The first element of the proposed test is whether the informant's identity can be instantly and reasonably available to the police.\textsuperscript{153} In the first situation, it may be difficult for the police to determine the identity of the informant absent a voice recording or specialized equipment.\textsuperscript{154} The second element of the test is whether the informant provided any predictive movement or described any actions that will take place in the future.\textsuperscript{155} In the first situation, the informant did provide future actions, that a specific bank would be robbed on a specific day and time. The third element is whether the information provided is confirmed or corroborated by independent police observation.\textsuperscript{156} The police officers in situation one used surveillance and observation to confirm the tip before conducting a stop or a search. The fourth element is whether the police officer reasonably believes that there is a considerable amount of danger to the officer or to the general public.\textsuperscript{157} The suspects in situation one were said to be devising

\textsuperscript{150} See \textit{Sakyi}, 160 F.3d at 167 (citing Pennsylvania v. Mimms, 434 U.S. 106, 109 (1977)).

\textsuperscript{151} See \textit{Florida v. J. L.}, 120 S.Ct. 1375, 1380 (2000) (stating that the indicia of reliability of an anonymous tip necessary to justify a search may decrease as the potential danger to the officer or public increases).

\textsuperscript{152} \textit{Florida v. J. L.}, 120 S.Ct. 1375 (2000).

\textsuperscript{153} \textit{Id.} at 1381 (Kennedy, J., concurring).

\textsuperscript{154} \textit{Id.}

\textsuperscript{155} \textit{Id.} at 1379 (concluding that an anonymous call lacking predictive information that can be confirmed by police surveillance lacked the appropriate "indicia of reliability" necessary to justify a stop and frisk).

\textsuperscript{156} \textit{Id.} (stating that in order for an anonymous call to be found reliable, the caller must provide information concerning future events that police can corroborate to test the informant's knowledge or credibility).

\textsuperscript{157} \textit{Id.} at 1380 (concluding that the reliability of an anonymous tip necessary to justify a stop and frisk decreases as the danger to the police officer or the public increases, and that in certain
In the second situation, an anonymous caller alleged that a particular suspect at a precise location was carrying a concealed weapon. In this situation, a police officer applying the proposed four-part test would determine that a search of the suspect would be unlawful. The police could meet the first element of the test by attempting to determine the informant’s identity. However, the police officer would fail to meet the second, third and fourth prongs because: the anonymous tip failed to provide predictive information regarding the suspect’s movements; the police did not observe the suspect in order to corroborate or confirm the anonymous information; and the degree of danger presented to the officer or the general public was not sufficient to justify a search absent a showing of the reliability of the tip. Because only one of the four elements is present, there is not sufficient indicia of reliability in the anonymous tip to outweigh an individual’s reasonable expectation of privacy, and a search of the suspect would be illegal. The officer could readily determine the illegality of the search prior to subjecting the suspect to the unreasonable search by applying this test.

Applying this test to situation three would provide an effective way for the police officer to determine that a search would be legal. This situation involved an anonymous tip stating that a man is going to enter a subway train with a bomb. Even though the police do not attempt to discover the identity of the informant and do not corroborate the information by direct observation, the circumstances, the danger alleged in an anonymous tip might be so grave as to justify a frisk even absent a demonstration of reliability).

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158 See J.L., 120 S.Ct. at 1379.
159 Id.
160 Id.
161 Id. at 1381 (Kennedy J., concurring).
162 Id. at 1379.
163 Id.
164 See J.L., 120 S.Ct. at 1380.
165 See Florida v. J. L., 120 S.Ct. 1375, 1381 (2000) (Kennedy, J., concurring) (concluding that the ability of law enforcement to determine the identity of an anonymous telephone informant may be a factor lending reliability to an unreliable tip).
informant did provide some information on future actions, 167 and there is a considerable amount of danger involved due to the presence of a bomb. 168 In this situation, since the degree of danger to the general public is great 169 and the anonymous tip provided information regarding future actions by the suspect, 170 a search of the suspect would be reasonable under the circumstances. 171 By using this four-part test, the police can determine whether the search would be legal before searching and before risking the possibility that their search may later be found to be unreasonable, resulting in the exclusion of any evidence discovered.

Also, by applying this test to Florida v. J. L., 172 the effectiveness of the test is proven because the police officer would have known beforehand that he could not legally search J. L. for the concealed weapon, based solely on the informant’s tip. The police did not meet any of the four elements. 173 The officer did not attempt to discover the informant’s identity to assist in determining reliability. 174 The informant did not provide the officer with any predictive movement or future actions by J. L. 175 The officer did not corroborate the information by direct observation. 176 The officer could not reasonably believe that he was in danger or that the public in general was in danger. 177 If the police officer had applied this test, he would have recognized that none of the elements required were present. 178 Therefore, any search he conducted of J. L. required either further evidence or a search warrant showing probable cause before being legal. J. L.’s right to be free from an unreasonable search was not outweighed by any other factors. Had the officer applied this test, he would not have searched J. L., and J. L.’s Fourth Amendment rights would not have been violated.

V. Conclusion

Law enforcement officers need a uniform standard to apply in order to determine whether to rely on an informant’s tip to conduct a search. A uniform standard is especially necessary in situations where the anonymous information

167 Id. at 1379 (concluding that in determining whether an anonymous tip provides the indicia of reliability necessary to justify a stop and frisk, it is essential that the tip provide some information on future events).
168 Id. at 1380.
169 Id.
171 Id. at 1379-1380.
173 See generally id.
174 See id. at 1381 (Kennedy, J., concurring).
175 Id. at 1379.
176 Id.
177 Id. at 1380 (stating that the facts in the instant case did not require speculation regarding the circumstances where the danger alleged by an anonymous informant to the officer or the public may be so grave that it justifies a search even absent a sufficient indicia of reliability).
provided is not verified or in situations that are potentially dangerous to the police officer or the general public. Police officers should not be required to make on-the-spot decisions based on a totality-of-circumstances approach. This totality-of-circumstances approach gives police too much discretion. Police officers should determine an informant's reliability before conducting a search by considering whether the informant's identity is reasonably available, whether the informant provided any predictive movement regarding criminal activity in the future, whether the information is corroborated by police observation, and whether the situation creates a reasonable possibility of danger.

Once the officer considers these four factors, she should weigh their presence against an individual's protected privacy right to determine if the search would be too intrusive. This proposed uniform standard should be applied to determine an informant's reliability in all situations where the police must rely on an anonymous tip to determine whether to conduct a search. Ultimately, the application of this standard will ensure that the fundamental privacy right granted to all citizens by the Fourth Amendment is not invaded.
LEAVING THE GATE OPEN: THE NINTH CIRCUIT ERASES
THE PRE-TRIAL DAUBERT HEARING REQUIREMENT
IN UNITED STATES V. ALATORRE

by Chris Kapsal

I. INTRODUCTION

To resolve complex factual issues at some trials during the middle ages, one
or both sides was required to produce a number of persons, called compurgators,
to swear an oath as to the justice of their side’s case.2 This process was
surrounded with complex procedural rules, and if the witnesses appeared and
spoke their words correctly, it was determined that the great unknown Deity
must be on their side, and that witness’ party should prevail.3

Today, to resolve complex factual issues at some trials, one or both sides
must produce a number of persons, called expert witnesses, to opine under oath
as to the justice of their side’s case. This process is surrounded with complex
procedural rules,4 and if the witnesses appear and speak their words convincingly, it is determined that the great unknown Science must be on their
side, and that witness’ party should prevail.

Perhaps sensing this irony of approaches, Congress and the courts have
revised today’s expert rules into a confusing state of flux over the past few
decades. The current rule was born in 1993, when the U.S. Supreme Court ruled
that a California federal district court judge had wrongly rejected evidence
attempting to show Bendectin caused birth defects.5 In 2000, after more years of
medical research, manufacturers still have found no evidence of Bendectin’s
dangers, and are working to remarket the drug.6 That unconvincing birth of what
has become known as the Daubert rule for admitting expert testimony was
recently dealt another blow in a Ninth Circuit case, United States v. Alatorre.7
There the court held that Daubert imposed no requirements on a trial judge to
hold an evidentiary hearing, much less a pre-trial Daubert hearing.8

Part three of this note argues that in deciding a separate pre-trial hearing was
unnecessary under Daubert, the Ninth Circuit misapplied Daubert’s meaning of

1 Chris Kapsal is a J.D. Candidate for 2001 at Salmon P. Chase College of Law; B.S. degree in
Mechanical Engineering Management from the U.S. Military Academy at West Point, N.Y.

2 See Peter W. Murphy, Symposium: The Science of Proof: Some Reflections on Evidence and
Probability, 40 S. TEX. L. REV. 327, 336 (Summer 1999).

3 See id.

4 See generally FED. R. CIV. P. 26(b); FED. R. EVID. 701, 702, 703.


6 See Lauran Neergaard, Morning Sickness Drug May Make Comeback, THE ADVOCATE (Baton

7 Alatorre, 222 F.3d at 1098.

8 Id. at 1105.
flexibility, and in the process permitted the judge to shift his evaluative role to the jury. Part four addresses why requiring a pre-trial hearing will shift the gatekeeping function back to the judge. Part five discusses reasons judges would prefer to avoid this role; part six argues why the current system needs pre-trial hearings. Part seven looks at commonly proposed corrections to the expert issue, and part eight offers a proposal to implement pre-trial hearings. Public criticism of the abuses of the current expert system requires that courts take steps to protect the integrity of the judicial system.

II. BACKGROUND

A. Explosion in Use of Experts at Trial: Common Law Development

The common law began recognizing its first expert witnesses over six hundred years ago, mainly in cases involving shipping or accounting. With the development of the Industrial Age in the United States came the growth in scientific and technical applications and knowledge that impacted courts in two major ways: first, proof of injuries, crimes and other subjects of litigation became more complex and technical; second, courtroom advocates began to apply advanced knowledge to courtroom truthfinding through experts increasingly being hired by private parties.

The issue in courtrooms became whether the scientific or technical expert testimony was even real science, and if it was, was it applied properly in the proceeding. The major drawback answering these questions was as true then as it is today: the judge, as referee of the process, had limited capability to address the two issues. Justice Breyer expressed it bluntly, that “judges are not trained scientists and do not have the scientific training that can facilitate the making of such decisions.”

The common law of evidence in place during the early part of this growth typically required a three-part foundation for admitting expert scientific evidence. First, the witness who conducted the test must have been qualified to conduct the test by his training and experience. Second, the reading device or procedure had to be in good working order and used properly. The third and pivotal issue was that the device or procedure had to be scientifically valid. These three elements had to be proven by the party choosing to admit the

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10 Id.
11 See generally Frye v. United States, 293 F. 1013 (D.C. Cir. 1923) (setting the modern standard to answer these questions in the courtroom).
15 Id.
16 Id.
17 Id.
These three elements had to be proven by the party choosing to admit the evidence through its expert witness, whether it be the state offering radar gun results against a speeding driver, or a plaintiff in a toxic tort using epidemiological studies.

The pivotal issue of scientific validity is the area where Justice Breyer's comment reflected the historical problem. The judge, with no scientific training, had to evaluate the validity of the proposed testimony. One solution came in 1923, interestingly, from the Court of Appeals for the District of Columbia, but soon became the national standard. In *Frye v. United States*, one sentence in a brief opinion took the decision out of the judges' hands, and made the test simply that "the thing from which the deduction is made must be sufficiently established to have gained general acceptance in the particular field in which it belongs."

For seventy years this general acceptance test was the standard. Difficulties arose with this test over time. Not only did it invade the judges' discretion in admitting testimony, but importantly, the growth in science that gave birth to the rule proved its demise: new science or technology could clearly not have gained "general acceptance" by virtue of its newness.

**B. Statutory Changes**

In the meantime, Congress adopted the Federal Rules of Evidence in 1975. Rule 702 addressed when to admit expert scientific testimony. The common law of evidence was then viewed as surviving the adoption of the rules, at least as an aid to statutory interpretation of the new Rules. What was not addressed was whether the *Frye* test also survived the Rules, particularly when the Rules did not even mention *Frye*.

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18 Id.
21 293 F. 1013 (D.C. Cir. 1923). The *Frye* court used this rationale to reject defendant's use of an early form of polygraph test in his defense to second degree murder. Id.
22 Id. at 1014.
23 See Daubert, 509 U.S. at 585 (holding that it had been previously superceded by the 1975 federal rules, although it had remained the standard for the intervening eighteen years).
24 Id. (using the term "novel science" to describe the rapid advances in technology).
26 Rule 702 requires only two foundational elements: the testimony will assist the trier of fact, and the expert is qualified. Fed. R. Evid. 702.
27 See Daubert, 509 U.S. at 588.
28 See, e.g., United States v. Downing, 753 F.2d 1224, 1232 (3rd Cir. 1985) (explaining that the status of the Frye test after adoption of the Rules was uncertain). This case is particularly noteworthy in that regard, because in many other respects, *Daubert* adopted many of the views in this opinion, including the factors test. Id.
The pivotal decision in *Daubert* some eighteen years later answered that question by explicitly stating "we hold that the *Frye* test has been superseded." General acceptance, then, was no longer the standard. The Court introduced a new, flexible test that would comport with the more liberal Rules. Further extensions in *Joiner* and *Kumho Tire*, the other two cases in the "*Daubert* trilogy," meant that the judge had broad discretion with expert evidence admissibility, and the same test applied to all expert testimony.

Thus, a new standard of admissibility was established. However, its application in the "trilogy" cases was all to summary judgment decisions: there had never been a discussion of when the standard would be applied during litigation. *Frye* had involved evidence excluded before trial. *Daubert* words stated that the determination would be one made "at the outset." But, *Alatorre* stands as the Ninth Circuit's answer that "at the outset" does not mean that a pre-trial hearing is required.

### III. Timing of the *Daubert* Hearing: The Ninth Circuit's Approach in *Alatorre*

#### A. Facts of United States v. Alatorre

Jorge Alatorre was arrested entering the United States from Mexico at the port of entry near San Diego, California. While stopped at the checkpoint in his car along with his two children, he drew the attention of a U.S. Customs

29 See *Daubert*, 509 U.S. at 589 n.6. The case arose when two minor children, born with birth defects to a mother who had used Bendectin during pregnancy, brought suit against the manufacturer. *Id.* at 579. Merrell Dow's expert had reviewed all the available studies and found no evidence of a link between the drug and birth defects. *Id.* Plaintiff's experts did not dispute his findings, but instead attempted to present a statistical re-analysis of those studies. *Id.* The trial court rejected those attempts as not valid science. *Id.* See also *Blum v. Merrell Dow Pharmaceuticals, Inc.*, 764 A.2d 1 (2000) (providing that the Pennsylvania Supreme Court rejected the same evidence under both the *Daubert* and *Frye* tests, and held on to the *Frye* test as the best way to prevent junk science).

30 See *id.* at 593. The new test included general acceptance but added considerations of testing, peer review and rate of error of the theory or technique. *Id.*

31 General Electric Co. v. *Joiner*, 522 U.S. 136 (1997). The Court upheld the trial court's exclusion of epidemiological studies offered to prove a causal link between the plaintiff electrician's exposure to PCBs at work and his later lung cancer. *Id.*

32 *Kumho Tire v. Carmichael*, 526 U.S. 137 (1999). In a product liability case where decedent's death was allegedly caused by tire tread separation, the Court upheld the trial court's exclusion of plaintiff's tire expert's testing methodology because of its failing to satisfy the *Daubert* inquiry, although it was not considered as scientific evidence. *Id.*

33 See *Joiner*, 522 U.S. at 139 (holding that abuse of discretion is the proper reviewing standard). The significance of this decision is that whatever method the judge uses will be reversed only if "manifestly erroneous." *Id.* Although the *Daubert* factors provide law to apply to a judicial review, the subjectivity inherent in Rule 702 and the flexibility of *Daubert* together put almost any decision on expert testimony beyond review. *Id.*

34 See *Kumho Tire*, 526 U.S. at 151 (applying the *Daubert* test to all expert testimony).

35 222 F.3d 1098 (9th Cir. 2000).

36 See *id.* at 1099.
inspector who began questioning him. During the questioning, a dog alerted to the car, and a search revealed sixty eight pounds of marijuana in a compartment above the rear tire well. Alatorre was indicted on federal charges of importing marijuana and possession of marijuana with intent to distribute.

The prosecution offered an expert witness, senior Customs Special Agent Lee Jacobs, to testify to the value of the drugs found and whether it was a distributable quantity. Since the Customs Service investigators had taken no fingerprint evidence from the tire compartment or drug packages, he would also testify, if the defense raised the issue, to the organization and structure of drug enterprises to show that Alatorre’s only task would be to drive the drugs across the border, explaining the missing fingerprints.

At an in limine hearing before trial, Alatorre requested a separate Daubert hearing be held, outside the presence of the jury, to challenge the value testimony on the grounds that the agent had no expertise on value of drugs, and the value was irrelevant to prove knowledge. The trial judge rejected a separate hearing, but permitted an at-trial voir dire of the witness. The judge explained the denial was because he had heard in numerous previous trials the agents testify to how they determined the drug prices, and any challenge would be a “fishing expedition.” However, he would permit a separate hearing if the expert’s testimony at trial indicated the need for one.

After an extensive voir dire into the agent’s basis for valuation, Alatorre’s renewed Daubert motion was overruled. He was convicted on both counts and sentenced to twenty one months imprisonment. Alatorre appealed on the basis of the denied pre-trial Daubert hearing.

B. The Ninth Circuit’s Holding in United States v. Alatorre

1. The Court’s Reasoning

The court in Alatorre was faced with a proffer of expert “specialized knowledge” testimony in the form of a customs inspector testifying to the value of marijuana found in defendant’s car crossing the Mexican border into the

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37 Id.
38 Id.
39 Id.
40 See Alatorre, 222 F.3d at 1100.
41 Id.
42 Id.
43 Id.
44 Id. at 1099 n.2.
45 Id.
46 See Alatorre, 222 F.3d at 1100.
47 Id.
48 Id. at 1099.
U.S. 49 Since Alatorre's defense was lack of knowledge, he challenged both the relevance of the agent's testimony (how value related to his knowledge) and reliability (how Customs know the value of the marijuana). 50 Although this situation fits squarely within the Daubert elements that trigger a Daubert analysis, the trial judge denied Alatorre's request for a pre-trial Daubert hearing to challenge the testimony; the customs agent testified, and Alatorre was convicted. 51

On appeal, the Ninth Circuit recognized that Kumho Tire extended the Daubert test to this type of testimony, 52 but that the form of the inquiry was never addressed in either the Daubert trilogy or any of its prior holdings. 53 The issue for decision became whether Joiner's abuse of discretion review standard permitted the judge to reject a pre-trial hearing in favor of a voir dire before the jury.

The court based its decision on its consideration of three factors: lack of authority expressly mandating a pre-trial hearing, coupled with the flexibility of the Daubert test application. 54 Within the flexibility analysis, the court looked at the Supreme Court's statements about broad latitude afforded trial courts, the latitude afforded both decisions and methods of arriving at those decisions, and the general policy of avoiding unnecessary reliability proceedings. 55 It then looked to opinions from other circuits on the issue, and concluded that Alatorre's voir dire was the "functional equivalent" of an "inquiry at the outset." 56

2. Factors in the Ninth Circuit's Decision

a. No Authority Mandating a Pre-Trial Hearing

The Court's reasoning examined its natural sources of authority, the Supreme Court, its own prior holdings, holdings from other circuits, and secondary authority to find any express guidance on timing, and concluded that nowhere in the Daubert trilogy did the Supreme Court mandate the form of the inquiry. 57 nor did its own prior decisions. 58 It then looked to the Tenth Circuit, citing their decisions in United States v. Nichols, 59 and distinguished their more recent decision in United States v. Velarde. 60 The court also looked to the

49 Id. at 1100.
50 Id. at 1099.
51 Id. at 1102.
52 See Kumho Tire, 526 U.S. at 151 (extending the Daubert inquiry to all expert testimony).
53 Id.
54 Id. at 1100.
55 Id. at 1102.
56 Id. at 1103-04 (concluding that any form of challenge would suffice as a reliability challenge).
57 See Alatorre, 222 F.3d at 1102.
58 Id.
59 169 F.3d 1255 (10th Cir. 1999).
60 214 F.3d 1204 (10th Cir. 2000).
Seventh Circuit in *Kirstein v. Parks Corp.* In all of these decisions, the Ninth Circuit found that the trial courts had been affirmed in refusing requests for admissibility hearings. It also found support from Weinstein that a trial judge is not required to hold an admissibility hearing on expert evidence.

**b. Flexibility of the Daubert Test**

The Ninth Circuit acknowledged the trial court's duty as a gatekeeper to screen expert testimony under the *Daubert* standard for relevance and reliability. It went on to note that the inquiry was meant to be flexible in its application. Finding no contrary authority regarding timing, the court concluded that flexibility extended to the timing and form as well. The court found that the trial court's own determination as to form would be reviewable only under *Joiner*’s abuse of discretion standard, strengthening the flexibility analysis.

**c. Policy of the Federal Rules**

The Ninth Circuit reasoned that if the Federal Rules "seek to avoid 'unjustifiable expense and delay' as part of their search for 'truth' and the 'just determination of proceedings,'" then requiring a *pre-trial* hearing for every proffer of expert testimony would defeat the trial judge's discretion in pursuing those ends. In *Alatorre*, the trial judge had heard the drug value testimony "so many times" that he found it admissible on that basis. In his view, one can infer, he would come to the same conclusion after a hearing anyway. Combining these justifications, the Ninth Circuit concluded that, absent a per se rule requiring a separate *pre-trial* hearing, the broad latitude of the *Daubert* test and the policy of the Rules meant that no *pre-trial* hearing was required.

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61 159 F.3d 1065 (7th Cir. 1998).
62 See *Alatorre*, 222 F.3d at 1103-04.
63 See 4 *Weinstein’s Federal Evidence* § 702.02(2) (2d ed. 2000), quoted in *Alatorre*, 222 F.3d at 1103.
64 See *Alatorre*, 222 F.3d at 1103 (quoting 4 *Weinstein, supra* note 64, at § 702.05(2)(a)).
65 See *Alatorre*, 222 F.3d at 1101.
66 Id.
67 Id. at 1102.
68 Id. at 1101.
69 Id. (stating that the law allows the same broad latitude to be applied to the final conclusion as to the method for how that decision was made).
70 Id. at 1102 (citing *Kuhmo Tire*, 526 U.S. at 152-53).
71 See *Alatorre*, 222 F.3d at 1102.
72 Id. at 1099 n.2.
73 Id. at 1105.
C. Analysis of the Ninth Circuit's Holding

1. Daubert's Unanswered Timing Question

The Daubert decision on its face established a new standard of how expert testimony was to be evaluated. The major concurrent effect and motivating reason was to change the "who" element. There has been a profusion of writings on all aspects of "how" the standard is applied (the Daubert factors), but almost nothing on either the "who" aspect (who makes the decision) much less "when." However, the timing of the Daubert inquiry directly affects who is actually making the evaluation of the expert's testimony. Under Frye, the validity was determined by the relevant community; now, under Daubert, the evaluation is the responsibility of the trial judge. This analysis will show that a cursory evaluation by a trial judge, believing that broad latitude and discretion are his guidelines, effectively allows him to relocate the true evaluation of the expert's testimony to the jury, defeating the intent of Daubert.

The profusion of literature on the subject suggests one fact: Daubert is not working as it was intended. Courts have come under heavy fire for decisions based on what is generally termed "junk science." This analysis will discuss how and why courts avoid their gatekeeping duty, often simply by using the timing issue to effectively defer evaluation to the jury. However, due to the excesses and abuses of the expert witness system, both real and perceived, it is imperative that courts do not avoid their role, and proper timing of the Daubert inquiry, i.e., at a separate pre-trial evidentiary hearing, may be the most effective way to ensure proper application. Numerous fixes, detailed below, have been proposed to Daubert; this analysis looks at the significant proposals and integrates those that complement the pre-trial hearing, and is aimed at the federal courts and states that follow the federal rules.

The function of Daubert was to answer the ultimate question for expert witnesses: "upon what may the expert rely?" Necessarily part of that question is the further question of "who is to say (upon what the expert may rely)?" Under

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74 See Daubert, 509 U.S. at 593 (overruling the Frye test, and establishing factors analysis).
75 Id. at 597 (describing the judge as the gatekeeper under this system, replacing the "relevant community" under Frye).
76 See, e.g., Cynthia Kent, Daubert Readiness of the Texas Judiciary, 6 TEX. WESLEYSAN L. REV. 4 (1999) (describing results of a survey of Daubert-related literature that revealed over 1,600 items by that date).
77 See generally Peter B. Oh, The Proper Test for Assessing the Admissibility of Nonscientific Expert Evidence under the Federal Rule of Evidence 702, 45 CLEV. ST. L. REV. 437 (1997) (cataloging difficulties in applying Daubert, such as lack of objective criteria for the factors, no guidance on the relevance prong, and other unclear aspects that have led to confusion and inconsistent application).
78 See generally PETER W. HUBER, GALILEO'S REVENGE: JUNK SCIENCE IN THE COURTROOM 13 (1991) (defining junk science as pseudoscience that is made to look like real science, and presented by coached witnesses with impressive credentials).
79 See Daubert, 509 U.S. at 592.
all standards, the judge runs the courtroom and controls evidence. However, the manner in which he exercises that control has changed. While the judge’s ability to evaluate scientific claims has always been recognized as limited due to background and training, his ability to evaluate evidence and implement procedure has not been so limited. The solution under Frye was to have the judge evaluate not the scientific claims, but the evidence offered by experts to establish, by way of the underlying scholarship of their analysis, that the validity of the proposed testimony was recognized in the relevant scientific community. Before Daubert overruled the Frye test, the adoption of Rule 702, as part of a trend of liberalizing the admission of evidence, changed the prior requirement of a “necessary” standard of utilizing experts to a “helpful” standard. But not until Daubert was the responsibility placed back on the trial judge to make the determination of admissibility.

Thus Daubert attempted to reconcile the liberal “helpful” standard of Rule 702 but still maintain the validity element of Frye. However, after Daubert, the trial judge is the gatekeeper of not only qualifications of witnesses, but also on what they may rely. Validity, meaning that the underlying science or specialized knowledge proves what it says it proves, and reliability, meaning it has been applied properly in this case, have been collapsed into a single standard termed reliability. The most significant change was that Daubert allows the flexible application of its factors to cover “novel” expertise, previously unavailable under Frye. Kumho Tire extended the analysis to all expert testimony.

2. The Ninth Circuit’s Timing Decision in Alatorre

The Ninth Circuit held that it was not an abuse of discretion for the trial court to deny the defendant a separate pre-trial hearing to challenge the expert witness on relevance and reliability under Daubert. It arrived at that decision by emphasizing two characterizations of the Daubert test made in Daubert itself and later in Kumho Tire: in Daubert, it found the guidance that the “inquiry...
envisioned by Rule 702 is . . . a flexible one;” from *Kumho Tire*, the court added that the “inquiry must be tied to the facts of a particular case.”

Based on this case-by-case flexibility, the court decided that the decision regarding the timing should also be flexible. This flexibility, reviewed only for abuse of discretion, meant that trial courts had broad latitude in not only how to apply the test, but also when to apply it.

3. Results Without Reasons: Case Law in Alatorre

The Ninth Circuit’s extension of the “flexibility” aspect of the *Daubert* test to timing and form is neither unreasonable nor flatly incorrect. However, this analysis will set out below that not only does *Daubert* give sufficient guidance to support a pre-trial hearing requirement, but countervailing policy considerations and practical impacts on litigation likewise support this requirement to fix a system of expert testimony under heavy criticism as permitting junk science. As such, this analysis examines the *Alatorre* decision to show that flexibility and latitude do not necessarily extend to timing and form.

   a. Stretching Flexibility Too Far

The *Alatorre* court emphasizes the frequent use of the term flexibility within the *Daubert* trilogy as a justification for its timing decision. But it is clear from *Daubert* that the use of “flexibility” in that opinion applied to a choice among substantive factors of the test depending on the circumstances, rather than how or when the test was to be applied. The *Alatorre* court’s reference to *Daubert* flexibility is a reference to using the factors to determine scientific validity. Citing *Kumho Tire*’s reference to flexibility, the Court is merely acknowledging that this flexibility means which factors to apply to non-scientific evidence. Likewise, in citing *Kumho Tire* that “unjustifiable expense and delay are avoided” if the trial court has “latitude” to decide “whether and when special briefing or other proceedings are needed to investigate reliability,” the court examines the passage out of its total context. The “when” quoted refers not to timing, but as the section immediately preceding indicates, refers to situations when the expert relies on certain types of testimony that may already have been

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88 Id.
89 Id.
90 See *Daubert*, 509 U.S. at 593-94. Flexibility was never defined by this court. See generally id.
91 See *The American Heritage Dictionary* 513 (2d ed. 1982). Flexibility is susceptible of two meanings: flexibility can mean either capable of being bent or twisted, or capable of adapting in response to new circumstances. *Id.*
92 See *Alatorre*, 222 F.3d at 1101 (citing *Daubert*’s calling for the inquiry to be a “flexible one”: read in the context of novel science, it becomes clear that certain factors, such as general acceptance and peer reviewed, would not apply to new science; thus, the flexibility goes to the factors to apply, not the timing).
93 *Id.* at 1102 (referring to the trial court’s broad latitude in deciding whether to admit expert testimony and how to test reliability). *But see Kumho Tire*, 526 U.S. at 141 (applying flexibility to the choice of factors to apply).
94 *Id.*
recognized as valid, and that the factors should be flexibly applied to such a situation.95 This also puts the court’s Weinstein citation in perspective, in that “reliability proceedings are not always required,”96 because even Daubert allows for scientific evidence so firmly established that it is properly subject of judicial notice under Rule 201.97 The flexibility that the Alatorre court strains to see grants discretion in method, where “the discretion endorsed . . . is not discretion to abandon the gatekeeping function.”98

b. Flexible Case Law

The court finds support for its timing conclusion in its own prior decisions, although none of the cases cited directly address timing or form. The court mentions its decision in United States v. Hankey99 to allow expert testimony about codes of silence within gangs.100 In Hankey, the defendant was also charged with intent to distribute drugs.101 When one co-defendant testified that the other defendant was not involved in the drug transaction at issue,102 the prosecution offered expert testimony of a police gang expert to prove that the alibi testimony resulted from the gang practice of killing or beating members who testified against other members.103 However, in Hankey, the expert testimony was offered only to impeach, subject to a limiting instruction, and only after a separate hearing outside the presence of the jury had already been conducted.104 The Alatorre court also looks to Hopkins v. Dow Corning Corp.,105 an early Daubert-era case involving expert testimony that particular breast implants caused the plaintiff’s connective tissue disease.106 Without any reason given, the court merely asserted that a Rule 104(a) hearing was not required.107 Neither of these cases offer support for the Ninth Circuit’s approach to the timing issue.

Looking to other circuits, the court found support for its ultimate holding in two Tenth Circuit cases that had similar underlying circumstances. The first was United States v. Davis,108 where two suspects in the armed robbery of a credit

95 Id. (differentiating between circumstances where the testimony may be properly taken for granted and when it gives cause to question the expert’s reliability).
96 4 Weinstein, supra note 64, at § 702.05(2)(a), quoted in Alatorre, 222 F.3d at 1103 (commenting on the current state of the law, but not prescribing lack of guidance on timing).
97 See Daubert, 509 U.S. at 592 n.11.
98 Kumho Tire Co. v. Carmichael, 526 U.S. 137, 158 (Scalia, J., concurring).
99 203 F.3d 1160 (9th Cir. 2000).
100 Id. at 1164.
101 See id. at 1165.
102 Id. at 1164.
103 Id.
104 Id. at 1166.
105 33 F.3d 1116 (9th Cir. 1994).
106 Id. at 1118.
107 Id. at 1124.
108 40 F.3d 1069 (10th Cir. 1994).
union appealed convictions obtained using FBI laboratory DNA evidence. Their asserted errors were essentially that the prosecution failed to prove that the lab followed proper procedures (termed "protocols" by the court) before admitting the evidence. On appeal, the Tenth Circuit upheld the conviction, citing that the "lengthy hearing" on DNA testing conducted by the district court, in front of the jury and without defense objection, was ample opportunity to determine if protocol was followed. The Tenth Circuit termed this hearing the "functional equivalent" of a pre-admission hearing.

Since the Ninth Circuit adapted this "functional equivalence" rationale in Alatorre, it is important to note the differences in circumstances. First, although Davis was tried just after Daubert was decided, both parties had used the Frye standard to stipulate that DNA testing was, in itself, valid. On appeal, however, the circuit court incorporated Daubert post hoc into its opinion, and in so doing sidestepped a circuit split over how to handle protocol challenges: it noted that the Second Circuit treated such challenges as jury questions, while the Eighth Circuit viewed the question as preliminary to admission. Here the functional equivalence of an inquiry in front of the jury satisfied both views. But Alatorre’s challenge was made under Daubert, and went to both relevance and reliability of the agent’s testimony. The Tenth Circuit addressed only the relevance inquiry, while Daubert inquiries primarily address reliability inquiries, and require this more involved analysis to be conducted “at the outset.”

The second Tenth Circuit case relied on was United States v. Nichols, a case similar to Davis. Nichols, on trial for the 1993 Oklahoma City bombing, challenged FBI lab bomb testing protocol. Unlike Davis, Nichols had a substantive challenge to lab procedures, provided by Dr. Frederick Whitehurst, an FBI lab employee who had made public the lab’s deficiencies. The trial court managed to avoid a protocol challenge in Nichols when it excluded Whitehurst as a witness. Without opposing evidence, the court again held that the at-trial voir dire of the prosecution’s FBI expert alone was sufficient to establish reliability and relevance. Nichols also differed from Alatorre in that Nichols was not challenging bomb identification methodology, but lab protocols, to which the Daubert factors would not apply. Alatorre was challenging the underlying validity of the agent’s testimony, and requested the pre-trial hearing to apply the Daubert factors to that evidence.

109 Id. at 1073 n.5.
110 Id. at 1075.
111 See Alatorre, 222 F.3d at 1103 n.6.
112 See Davis, 40 F.3d at 1072 n.4.
113 Id. at 1074 n.7.
114 See Alatorre, 222 F.3d at 1100.
115 169 F.3d 1255 (10th Cir. 1999).
116 Id. at 1263.
117 Id. at 1267.
118 Id. at 1263 (stating that the contentious issue was the flaws in the laboratory testing, while the testing methodologies themselves are well known and routinely used by chemists). Compare with Alatorre, 222 F.3d at 1100 (challenging the underlying methodology of determining drug values).
When the Tenth Circuit did entertain an actual reliability challenge in United States v. Velarde, the Ninth Circuit parted company with the Tenth. In Velarde, the prosecution gained a conviction for sexual abuse of a child using testimony of a pediatrician to prove that the behavior of the child was consistent with such abuse. When the defendant challenged the expert’s reliability on the grounds that she exceeded her expertise in testifying about psychology, the trial judge refused a separate hearing, stating that he had “heard this testimony before in trials.” The Tenth Circuit reversed because of a lack of any reliability determination by the court. Acknowledging that the Alatorre judge rejected the hearing for the same reason as the Velarde court, frequency of that kind of testimony, the Ninth Circuit stated that the opportunity to voir dire in Alatorre was the distinction. However, as this analysis will later show, that is a distinction without a difference, as it does not fulfill the requirements of a Daubert preliminary hearing at the outset. An improperly conducted hearing, using inexact standards and in a situation not conducive to a thorough airing, is an inadequate substitute for an adequate evidentiary hearing on the record. Velarde was not based on “functional equivalence,” because, unlike Davis and Nichols, it was a reliability challenge; rather, the rationale was based on Kumho Tire’s requirement that the judge has the ultimate responsibility to make a reliability determination.

The Seventh Circuit’s decision in Kirstein v. Parks Corporation was similarly not applicable in this context. There, plaintiff wanted to use an expert to show that a chemical linoleum stripper had inadequate warnings that led to his being severely burnt. However, the trial court granted summary judgment based on opposing briefs showing that the expert had actually done no testing at all. No pre-trial hearing was required because the expert’s lack of testing left no issue to be resolved in a hearing.

The Ninth Circuit also used a policy argument to support its approach derived from Rule 102. The elliptical rationale emphasizes avoiding expense and delay as favoring less rigorous hearings. But Rule 102 also includes

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119 214 F.3d 1204 (10th Cir. 2000).
120 Id. at 1207.
121 Id. at 1210.
122 Id. at 1211.
123 See Alatorre, 222 F.3d at 1104. The trial judge in Alatorre also refused to conduct a reliability determination, but the Ninth Circuit said that the opportunity was the functional equivalent. Had Alatorre not conducted voir dire or cross examination, then under this rationale, presumably this case would also have been reversed. Id.
124 See Velarde, 214 F.3d at 1211.
125 159 F.3d 1065 (7th Cir. 1998).
126 Id. at 1066.
127 Id. at 1067.
128 See Fed. R. Evid. 102, Purpose and Construction. “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.” Id.
129 See Alatorre, 222 F.3d at 1102.
"fairness in administration," promoting "growth and development of the law of evidence" with this growth aimed at ascertaining truth. In the context of the whole rule, reliability proceedings will be unnecessary only when they are not needed to fairly determine the truth, such as when the evidence can be judicially noticed.

c. Implications of the Holding

Overall, *Alatorre* was probably not the best case for the Ninth Circuit to stake out its position on this controversial issue. *Alatorre* involved a straightforward criminal charge, and the routine expert testimony played a simple function, albeit important to the defendant’s conviction and sentencing. *Daubert* seems more suited to complex causation issues and even the Ninth Circuit recognized that pre-trial hearings “may be appropriate in certain cases.” Thus, the danger of this decision is that, under the “broad latitude” and abuse of discretion standards that it endorses, the trial judge within the Ninth circuit will never be required to fulfill his gatekeeping function.

IV. PUTTING THE GATEKEEPER BACK AT THE GATE: THE TIMING REQUIREMENT IN *DAUBERT*

*Daubert*’s notion of the trial judge as gatekeeper, in the ordinary sense, is that he is to be more in control of access through the gate, rather than figuratively standing there to keep it open. With that idea as the backdrop, this analysis looks to *Daubert* to show that a pre-trial hearing is a necessary condition. However, since this requirement was not expressly stated by *Daubert*, this analysis looks at practical reasons judges, as in *Alatorre*, would want to avoid the duty; how the judicial system is being undermined in the process; and, why a pre-trial hearing is the solid gate to restore lost integrity to the judicial system in the public eye.

In addition to the idea of gatekeeping, *Daubert* gives other support to conducting a pre-trial hearing within its own words, within the meaning of Rule 104(a), and from the circumstances of the trilogy cases.

The judge’s gatekeeping function, taken together with his screening role, indicate that the trial judge is to exercise purposeful control over what is admitted into evidence. In *Daubert*, the Court held that the analysis was to be made by the trial judge, “at the outset, pursuant to Rule 104(a).” The Court went on to state that “[t]his requires a preliminary assessment of whether the

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130 FED. R. EVID. 102.
131 Id.
132 Id.
133 *Alatorre*, 222 F.3d at 1105.
134 See *Daubert*, 509 U.S. at 597 (describing “gatekeeping” in the sense of preventing some information from reaching the jury by application of the factors).
135 See *Daubert*, 509 U.S. at 597.
136 Id. at 589.
137 Id. at 592.
reasoning or methodology underlying the testimony is scientifically valid and of whether that reasoning or methodology properly can be applied to the facts in issue. 138

The ordinary meaning of outset is "beginning; start" or "initial stage." 139 The ordinary meaning of preliminary is "prior to or preparing for the main matter." 140 For a Court that overruled Frye on strict interpretation principles, 141 it seems unlikely they would have been careless with these terms. Likewise, Rule 104(a) has as its purpose the allocation of responsibility between the judge and jury, where admissibility is solely the judge’s function. 142

Timing guidance comes not only from the words of the opinion, but from the circumstances of the cases that stated the rule. Daubert, Joiner, and Kumho Tire 143 were all decided on summary judgment motions where the expert testimony was the critical issue. Daubert, on remand, 144 reaffirmed the trial court’s grant of summary judgment, 145 even under the new Daubert standard, reasoning that the plaintiff’s experts’ studies were not sufficiently reliable to create an issue of fact on Bendectin’s causation. 146 Further, the thoughtful opinion by Judge Kozinski indicates a thorough review of the proffered experts’ underlying principles and methodology. 147

V. WHY COURTS AVOID DAUBERT HEARINGS

Daubert shifted the responsibility for making determination of admissibility of expert witnesses back to the trial judge, where it had not been for 70 years. 148 Judges, however, have been reluctant to accept this burden, and as discussed below, for apparently good reasons. The science issues are difficult, complex, and technical. Judges, by background, training, and education are ill-equipped to cope with the complexities presented. Faced with this difficulty and their own inherent inability to deal with it, judges are tempted to fall back on the liberal

138 Id.
139 See THE AMERICAN HERITAGE DICTIONARY 883 (2d ed. 1982).
140 Id. at 977.
142 See FED. R. EVID. 104 advisory committee’s note.
143 See, e.g., Daubert, 509 U.S. at 583 (granting summary judgment for defendant when court rejected plaintiff’s reanalysis of defendant company’s product testing which showed no medical harm); Joiner, 522 U.S. at 140 (granting summary judgment for defendant when court rejected plaintiff’s cancer causation studies as “speculative”); Kumho Tire, 526 U.S. at 146 (granting summary judgment for defendant tire companies after court rejects plaintiff’s tire expert analysis under Daubert).
144 43 F.3d 1311 (9th Cir. 1995).
145 Id.
146 Id. at 1322.
147 Id. at 1315. Judge Kozinski begins by fully detailing the judge’s new responsibilities under the new standard, then applies each of the factors to the plaintiff’s evidence, resulting in rejection for essentially the same reason as in the original case. Id.
148 See Daubert, 509 U.S. at 589 n.6 (overruling Frye, the standard since 1923).
bias of the Federal Rules, to "let it in" and let the jury sort it out.\textsuperscript{149} However, there is nothing sacred about this approach,\textsuperscript{150} and it has been the source of many of the public perception problems the judiciary has faced.\textsuperscript{151}

\textbf{A. Complexities and Uncertainties of Science}

The inherent difficulty of dealing with complex technical evidence comes from several sources. Science and technology, both hard and soft, are complex and continuously developing. Difficulties come from statutory sources, in that the Federal Rules of Evidence provide little in the way of firm guidance or standards. And finally, evolving case law attempting to clarify rules results in even more confusion. Ultimately, evidence law must come to grips with the reality that the reach of many of its rules exceeds the grasp of both law and science.

Science\textsuperscript{152} does not easily do what is commonly expected of it in the courtroom. With ordinary witnesses, lawyers, judges, and jury members, one can expect that if eyewitness A saw the defendant shoot the victim, and there is absolutely no grounds to impeach the witness, that she got it wrong or lied about it, then it must have happened as A said it did. These same expectations seem to be transferred to experts paradigmatically, that although the expert was not there, but by the use of a magical black box based in science, he can tell us what happened.\textsuperscript{153} As it turns out, there are some problems with this paradigm. Science itself is capable of producing only a certain level of certainty; it is capable of answering only specific, precise questions; and there is no "across the board" approach that gives an understanding of all sciences for all time.

The level of certainty of science is a function of its process. Traditionally, scientific reasoning is thought of as consisting of a reiterative process including five steps: observation, tentative description, hypotheses and prediction, testing of the hypotheses, and modification of the results by repetition of all the elements.\textsuperscript{154} However, as Justice Blackmun noted in \textit{Daubert}, "it would be unreasonable to conclude that the subject of scientific testimony be ‘known’ to a

\textsuperscript{149} See Peter W. Huber, \textit{Galileo’s Revenge: Junk Science in the Courtroom} 17 (1991) (quoting In re Air Crash Disaster at New Orleans, 795 F.2d 1230, 1234 (5th Cir. 1986)).

\textsuperscript{150} See generally Shonubi, 895 F. Supp. at 496 (explaining that this view expressed in the code is a compromise of two competing views along a spectrum, and that this spectrum is subject to shifting).

\textsuperscript{151} See, e.g., Joe Baker, \textit{The Truth About the Whole Truth in the Court; Just as in American Society, The Courtroom No Longer Employs the True Pursuit of the Truth}, Orlando Sentinel, August 20, 2000, at G1 (criticizing the judicial system for allowing the use of “hired gun” expert witnesses to distort the courtroom process).

\textsuperscript{152} For purposes of this analysis, “science” is meant to include all expert testimony, since the original \textit{Daubert} opinion was extended by \textit{Kumho Tire}.

\textsuperscript{153} See Daubert, 509 U.S. at 592. Despite the popular view of the function of science, the extensive briefs sent to the court emphasized the limitations of science to reach high levels of certainty and, likewise, to prevent definitive statements about what the expert is testifying. Id.

certainty; arguably, there are no certainties in science." Consequently, experts are no longer required to characterize their conclusions as a scientific certainty, especially since such a conclusion would be inherently dishonest in most cases. The problem for the court is to find the line between reasonable probability and scientific certainty that will allow science to play an evidentiary role; the utility of science in the courtroom is affected not only by its uncertain nature, but also by the manner in which it is used. It can answer precisely framed questions, in the way the expert thinks. The danger comes from imprecise questions that permit answers that point to a conclusion with more certainty than is warranted, or go beyond what the question asked, even beyond the actual expertise of the expert.

Likewise, the lawyer and judge may be hearing different answers than the expert is giving, resulting in a distortion of issues and priorities, such as where the lawyer is looking to fix liability for a problem that science may not yet even understand.

To further complicate matters for the non-scientist, there is no "one size fits all" approach to science. The term science is broad and includes a long and divergent list, made longer by Kumho Tire's extension into all expert testimony. The list ranges from chemists to art historians, handwriting analysts to building inspectors, and engineers to lawyers. Evidence standards can not easily be applied, once developed for one context, to all sciences in other contexts, because:

- each science is at a different stage of sophistication; each field uses different tools, operates on different assumptions employs different methodologies, and has different goals, resulting in large cultural and language gaps.

Examples of complexities abound. Toxicology, for example, has to explain not only general causation, whether a particular disease can be caused by this chemical, but also specific causation, whether this disease happened this way to this plaintiff. Tracing causation may require relying on reconstructive modes, animal study extrapolations, and disease histories that progress over lifetimes. Even in a more common example, in the Intoxilyzer test used to combat drunk

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155 See Daubert, 509 U.S. at 590.
157 See Stephen D. Easton, Ammunition for the Shoot-Out with the Hired Gun's Hired Gun: A Proposal for Full Expert Witness Disclosure, 32 ARIZ. ST. L.J. 465 (Summer 2000) (Note by this title that many critics of the current system compare it to the other medieval method for fact-finding - trial by combat - where the experts are the parties "hired guns").
158 See Daubert, 509 U.S. at 597. Justice Blackmun described the difference: law seeks to resolve disputes finally and quickly, whereas scientific conclusions are subject to perpetual revisions. Id.
161 Id.
driving, certain variances affect the certainty of what is known, as this testimony example shows:

Q. Okay. Again, because of the variance, because you are not actually taking blood and measuring it, now you’ve got another variance in there. You are trying to transfer information taken from a breath test into a blood content and you have to apply an arbitrary ratio, arbitrary only in the sense that it varies individual to individual?

A. Yes, that’s correct.

Q. There can be, again, a range of inaccuracy up to 10 percent on that, isn’t that right?

A. That’s correct. 162

As the current trend of lowering blood alcohol levels for legal driving continues, courts are not interested in rehearing the issues of possible uncertainties in the “black box” testing equipment. Of course, despite (or because of) this complexity, experts perform a valuable role in court to clarify or resolve factual disputes. But this use must be governed wisely, so that juries are not basing verdicts on junk science.

B. Difficulties Inherent in the Federal Rules

One tool for the court to use in resolving these complexities is Rule 702. Evidence rules have their own inherent problems, such as imprecise wording, militating against consistent application, a particular problem when public opinion shifts in favor of certain results, and the rules provide a basis for any position. Lack of qualifying standards is another serious deficiency. For example, Rule 702 allows expert opinion when it will be helpful. 163 Factual assistance, however, is actually a highly subjective determination 164 without objective standard, particularly critical when abuse of discretion is the standard of review. Also, the trial judge has usually just met the jury, and cannot possibly know what assistance each of them personally or collectively needs. Beyond that, Rule 702 provides no threshold for evaluating credentials necessary to qualify as an expert. 165 Naturally, most professional experts prefer to submit lengthy credentials to obtain the aura of superior knowledge and enhance their credibility, but courts often look at these credentials without establishing the nexus to the factual issue. 166 The consequence of this hazy approach provided in


163 See Fed. R. Evid. 702 (requiring that expert testimony merely “assist the trier of fact”).


165 Id. (providing somewhat circularly that the expert be “qualified as an expert” by “knowledge, skill training, or education”). Rule 702 does not specify the form of an objective inquiry into what levels of each is required to be an expert, even at the threshold, or even specify that the qualification be relevant to the testimony. Id.

166 Id.
rule 702 is that courts too easily have used it to admit junk science. Further, once public policy shifts, this standard can shift with it, resulting in a lack of consistent application. For example, liberalized expert rules, developed to accommodate fast-growing scientific and technical progress, have recently been under criticism, such as when the defense bar persuades the public that runaway verdicts are the product of junk science. Responding to public pressure, judges will shift the standard, and in the process exclude otherwise helpful experts.

C. Case Law Confusion

Once shifting begins and attendant criticism follows, courts will rule to clarify matters. Often this creates more confusion in application than before, leaving practitioners puzzled as to what the standard actually is. Typical of the confusion, outlined below, are the questions of whether Frye really is no longer the standard, how reliability is then determined, and to what types of experts Daubert applies.

Daubert explicitly overruled Frye's general acceptance standard on the one hand, but then retained peer review as a factor for determining general acceptance on the other. Kumho Tire requires a "standard of intellectual rigor of the professional in the field," sounding more like the Frye standard of general acceptance "in the particular field in which it belongs." If the standard is Frye-like, then the Daubert pre-trial hearing becomes even more necessary to provide an opportunity to review the relevant scholarship or to determine the intellectual rigor of the professional in the field. Although courts speak of determining validity and reliability, general validity under Frye has been collapsed into Daubert reliability, but the courts recognize the two really are not the same, although Daubert treats them as such. And Daubert used scientific principles and reasons based on extensive briefs on the subject to develop its factors, with the majority expressly limiting its application to scientific evidence, and with a particular emphasis on addressing novel science. The rationale developed for scientific application has been extended to all experts, without justification in the underlying rationale.

167 See generally Trevor Armbrister, Suing Like Crazy, READERS DIGEST, October 2000 (reflecting popular sentiment about abuses in the system, and legislative attempts to control the runaway judicial system). See also State ex rel. Ohio Academy of Trial Lawyers v. Sheward, 715 N.E.2d 1062 (Ohio 1999) (invalidating an Ohio statute placing, inter alia caps on damage awards in civil actions and establishing by statute a judicial standard for the granting of summary judgment in toxic exposure cases).

168 See Daubert, 509 U.S. at 594 ("[G]eneral acceptance' can yet have a bearing on the inquiry").

169 See Kumho Tire, 526 U.S. at 152.

170 Frye, 293 F. at 1014.

171 See, e.g., James J. Brosnahan, Motions in Limine in Federal Civil Trials, SE56 ALI-ABA 1, 29 (describing hearings on admissibility that lasted from several days to several weeks, for example, noting the time involved in wading through the volumes of documentary record on the science of breast implants in Allison v. McGhan Medical Corp., 184 F.3d 1300, 1306).

172 See Daubert, 509 U.S. at 592, n.11.
A good portion of this confusion originated in Daubert. Within the same opinion the Court mentions both the "liberal thrust" of the Federal rules173 while at the same time describing the judge as having a "gatekeeping role" for "screening" expert testimony.174 These conflicting goals were present at the drafting of the original Federal Rules, as Judge Weinstein explains in his lengthy, informative opinion rendered in United States v. Shonubi.175 Essentially, he argues that the Rules represent a compromise between competing positions articulated by, on the one hand, John Wigmore, favoring a system of precise, clear rules for any evidentiary situation,176 and James Thayer on the other, whose views favored rejecting outdated mechanistic systems in favor of broad principles of relevancy.177 The compromise of the Rules initially leaned in Thayer's direction,178 but the trend of the revisers has been in the direction of more restrictive rules.179 As a result, many courts have viewed Daubert as imposing more rigorous standards than under Frye.180

Alatorre shows the results of this confusion: other cases result in reversal for using the same approach as the Alatorre trial court.181 Many courts view Daubert as applicable only to instances of novel science, but otherwise seem to follow the apparent reversion to Frye, so that where expert testimony has been frequently heard, no further analysis is needed.182

D. Judicial Capability

The original thrust of Frye was to remove validity judgments from trial judges' hands and put the burden on the expert to establish his own validity.183 Daubert relocated that responsibility to the trial judge, and the majority asserted its confidence in judges to handle the responsibility.184 However, as this analysis

173 Daubert, 509 U.S. at 588.
174 Id. at 596.
176 Id. at 495. Wigmore's view was that an evidence code, as a practical guide, should deal less with abstractions and give concrete rules for each situation. Id. However, as Judge Weinstein pointed out, the numerous volumes and complexity in his writings are in themselves evidence of how elusive this goal can be. Id.
177 Id. at 494.
178 Id. at 496.
179 Id. (describing, for example, Rule 412 and its detailed evidence provisions).
180 See, e.g., Alaska v. Coon, 974 P.2d 386, 397 (Alaska 1999) (describing certain types of evidence that would be admissible under Frye's general acceptance standard, but fail admissibility tests imposed under Daubert)
181 See, e.g., United States v. Velarde, 214 F.3d 1204 (10th Cir. 2000) (refusing a Daubert hearing even though the judge had previously seen the proffered evidence). This case was reversed for a lack of reliability determination. Id.
182 See, e.g., Alatorre, 222 F.3d at 1105 n.9 (refusing a separate hearing because the trial judge had often heard the testimony). But see Velarde, 214 F.3d at 1210 (reversing trial judge who refused a hearing because, to him, the testimony was not "new and novel").
183 See Frye, 293 F. at 1014.
184 See Daubert, 509 U.S. at 592-93. Both the majority and dissent expressed confidence in federal trial judges, but as the opposing views show, this confidence can have a nebulous meaning. Id.
will discuss, this confidence may be less than fully warranted, as evidenced by both the judiciary's own admissions as well as the stark reality of judicial capabilities.

The debate over judicial capability to handle this new responsibility was apparent in Daubert itself where the majority stated its confidence that trial judges were able to handle this analysis. The dissent by Chief Justice Rehnquist gave the opposite view, in essence, that judges would have to become "amateur scientists" in this new role. Courts themselves also recognize their limited abilities in evaluating science. Critical literature likewise reflects this view of the limitations of judicial capacity.

Texas Judge Cynthia Stevens Kent conducted a study that revealed the common perception of judges as unable to deal with technical questions was justified. This study provides statistical evidence of the capabilities of one state's judiciary to adapt to the role envisioned by Daubert. It is unfortunately unique in that it appears to be the only one of its kind published.

The thrust of the study was to collect data on the background, education, and training of Texas judges, and also their perceptions of their own readiness to fulfill the gatekeeping function. Generally, the study found that around 90% of the judges had had a few courses involving the scientific method, but on average that experience was more than 20 years removed. More telling was that 83% reported no training in the application of the scientific method to legal analysis in law school. Despite these shortcomings, 70% of the judges perceived themselves capable of performing gatekeeping functions under Daubert. The most telling result, however, was that 40% of the judges had not even read the Daubert opinion. Whatever the self-reported perception of readiness was based on, for many it was not based on a clear understanding of either their role or of the scientific process. As far as any remedial effort was involved, less than 30% of the judges reported having taken Continuing Legal Education (CLE) courses in the scientific method. Even that number may be

185 Id. at 601 (Rehnquist, C.J., dissenting).
186 See, e.g., State v. Graham, 322 S.W.2d 188 (Mo. App. 1959) (stating "this court yields to no group in its collective ignorance of science in general").
187 See, e.g., Joe Baker, The Truth About the Whole Truth in the Court; Just as in American Society, The Courtroom No Longer Employs the True Pursuit of the Truth, ORLANDO SENTINEL, August 20, 2000, at G1 (opining in the mainstream media that judges often "be dumb, act dumb, and don't ask any questions" to avoid looking more foolish when confronted with technical questions, and a general reluctance to educate themselves on these matters).
188 See Cynthia Kent, Daubert Readiness of the Texas Judiciary, 6 TEX. WESLEYAN L. REV. 4 (Fall, 1999).
189 Id. at 4.
190 Id. at 5.
191 Id. at 4.
192 Id. at 14.
193 Id.
194 See Kent, supra note 189, at 15.
195 Id. at 16.
196 Id. at 18.
overstating things, in that less than half of the CLE providers were confident that their programs contributed significantly to preparing judges in their roles as gatekeepers.197

One likely explanation for the lack of urgency to address these limitations of judicial capability is that the Federal Rules provide an escape route to avoid heavy analysis.198 This easy out for the judges exists because of the Rules’ liberal bias toward admitting evidence, where the subjective standards for factual assistance and low threshold for qualifications is the justification to allow in evidence. The only check is the abuse of discretion standard under Joiner, conveniently administered by other untrained judges. In practice, Daubert provides no additional restriction beyond the hazy Rule standards. For example, the Tenth Circuit ruled in Compton v. Subaru of America199 that Daubert merely provided additional factors to the Rule 702 analysis.200 The Second Circuit in McCullock v. H.B. Fuller Co.,201 refused to invade the jury’s province and elevate itself to the role of “St. Peter at the gates of heaven,”202 again just an elaborate way of deferring the heavy lifting to the jury.

At the same time it emphasized the role of the judge as gatekeeper, the Daubert court also emphasized the role of the jury, citing the need to believe in the effectiveness of “[v]igorous cross examination, presentation of contrary evidence, and careful instruction on the burden of proof.”203 However, these procedures in turn depend on the adequacy of pre-trial disclosure and placement of necessary information before the jury. If jurors are to use their common sense and life experience as the final safeguards, then, they need information that will inform their common sense.204

VI. WHY PRE-TRIAL EVALUATION SHOULD NOT BE AVOIDED

A. Abuses Under the Current System

Although the complexity of scientific and technical information and the judiciary’s inherent limitations in dealing with it lead to avoidance of the problem through the escape route the Rules provide, it is critical to the interests of justice and public perception that judges shoulder this responsibility. Expert testimony is prone to abuse, and the trial safeguards that Daubert presupposes

197 Id. at 17.
198 See PETER W. HUBER, GALILEO’S REVENGE: JUNK SCIENCE IN THE COURTROOM 3 (1991) (stating that the “‘let-it-all-in’ legal theory creates the opportunity”).
199 82 F.3d 1513 (10th Cir. 1996).
200 Id. at 1519.
201 61 F.3d 1038 (2nd Cir. 1995).
202 Id. at 1045.
203 See Daubert, 509 U.S. at 596.
204 See e.g., Stephen D. Easton, Ammunition for the Shoot-Out with the Hired Gun’s Hired Gun: A Proposal for Full Expert Witness Disclosure, 32 ARIZ. ST. L.J. 465 (Summer 2000) (arguing that court-imposed restrictions on full disclosure of attorney-expert communications hampers the cross-examination process that is ordinarily expected to reveal flaws in the expert’s testimony).
can be overwhelmed. Coupled with this basis is the mechanism that both attorneys and experts are motivated by the nature of the adversary system to present expert testimony in a less than objective manner. The result of these factors is an undermining of the judicial system, both in public perception and in practical effect.

Abuse of expert testimony comes from the naive faith in science's claim to certainty in both evidence law and popular consciousness. However, the potential for abuse of this faith had been recognized from early on. Shortly after Frye was announced, Dean Wigmore noted that use of expert testimony had reduced American litigation to "a state of legalized gambling." And before that, foreshadowing a modern sentiment, one court noted in 1899 that "[t]here is hardly anything, not palpably absurd on its face, that cannot now be proved by some so-called 'experts.'"

Daubert extolled the virtue of juries to ferret out the true meaning of scientific evidence. And yet, as this analysis will show, that is precisely what experts and lawyers work to defeat. Attorneys shop for favorable experts who are, in fact, chosen carefully for their ability articulate and defend the position the client needs them to take. These experts by training and experience are able to evade the jury's scrutiny in a way that ordinary fact witnesses normally are not. The attorney gets a believable witness, and the expert finds an agreeable way to earn a living.

The attorney has several effective methods available for controlling and shaping expert testimony to support his victory. These methods fall generally into two categories. The first category involves the attorney's at-will employment relationship with the expert: here, the attorney selects, hires, and decides whether that expert will testify, based on whether the expert can be used to gain a favorable outcome. The second category involves the attorney's ability to shape the expert's testimony by controlling the information flow to him and directing his analysis, always with an eye toward what that testimony has to

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205 See, e.g., Downing, 753 F.2d at 1236 (agreeing with the proposition that scientific evidence may "assume a posture of mythic infallibility in the eyes of a jury of laymen").


207 See Keegan v. Minneapolis & St. Louis R.R. Co., 78 N.W. 965, 966 (Minn. 1899).

208 See Daubert, 509 U.S. at 595-6.


210 See generally PETER W. HUBER, GALILEO'S REVENGE: JUNK SCIENCE IN THE COURTROOM 19 (1991) (describing not only this selection procedure, but the opportunities available, such as seminars, for professional experts to learn the tips of the trade). For a flavor of the types of expert witness coaching materials available, see generally Steven Babitsky, The 10 Biggest Mistakes Experts Make During Depositions (last modified Dec. 16, 2000) <http://expertpages.com/news/ten_biggest_mistakes.htm>.

be to achieve victory. An extreme example cited by professor Easton involved an attorney who wrote a doctor’s report denying that injuries were sustained in an accident, and had the doctor retype the report on his own stationery. Even the rules of Professional Responsibility cannot diminish the attorney’s control efforts because he is charged with zealously representing his client.

The expert is on the other end of this relationship. He is selected for his ability to testify convincingly, and will work and be paid only so long as he is able to do so. On his side are several advantages: he presents a long list of impressive credentials, is accorded expert status, and then by virtue of the superior knowledge and communication skills he was selected for, is then permitted by Rule 704(a) to give his opinion even on ultimate issues. Although courts now permit questions into fees and percent of work spent testifying, experts largely will be able to charm their way through these issues. These powerful advantages, giving heightened credibility, work no less for a government expert, like the Customs Inspector in Alatorre, who assumes the expert role as part of his job.

Although this manner of operating produces victories for parties or convictions for the government, at the same time it undermines the legal system. Strange verdicts at odds with common sense or overturned criminal convictions create a poor perception of the system in the lay population, and erode public confidence accordingly. This erosion can have two opposite effects. At one end, the judicial system will be overwhelmed with frivolous claims supported by the shakiest of evidence that proponents believe this system

212 Id. at 495.
213 Id. at 500 n.115 (citing one of several examples where the attorney successfully wrote the expert’s opinion for his signature).
214 See generally id. at 503 n.121 (describing the Model Code of Professional Responsibility provision that imposes a duty on lawyers to zealously represent their clients, and parallel provisions in the Model Rules of Professional Conduct). Clearly, fraud is not acceptable, but the utmost efforts to acquire helpful expert testimony is acceptable). Id.
215 See, e.g., Committee on Legal Ethics of the West Virginia State Bar v. Sheatsley, 452 S.E.2d 75, 80 (1994) (disciplining an attorney for a contingent fee arrangement with a witness, yet at the same time acknowledging in a concurring opinion by Cleckley, J., that the system already has a built-in incentive for experts to shape testimony to fit the needs of the case if they expect to work).
216 See FED. R. EVID. 704(a) (permitting opinion evidence, other than on mental states or conditions of criminal defendants, to “embrace” ultimate issues to be decided by the trier of fact).
217 See supra note 210 (showing an example of how experts are coached to answer these questions).
218 See Alatorre, 222 F.3d at 1100.
219 See, e.g., Amy Ridenour, Court, Congress Move to Fight Junk Science, CINCINNATI ENQUIRER, April 4, 1999, at B-7 (stating the view of some members of the public that expert witness reform will help correct a U. S. litigation crisis which is said to cost consumers $150 billion per year and adding 2.5 percent to the cost of every new product in America).
220 See generally Junk Science: Separate Fact from Lies, CINCINNATI ENQUIRER, September 24, 2000, editorial at F-2 (describing a system of class actions where trial lawyers hire carefully rehearsed expert witnesses to brainwash juries with junk science into giving them huge awards for even bogus liability, thereby rewarding the wrong people, hurting politics and preventing the innovation in new product development).
will permit. On the other hand, because the public, as jurors, is co-opted into legitimizing improper verdicts, the average citizen will be less inclined to resort to the judicial system for the peaceful resolution of disputes. And ultimately, if the criticism grows too large, legislatures will respond with controls over the judiciary.

B. Why a Separate Pre-trial Hearing is the Answer

The trend now is to construe Daubert so that ill-equipped judges can avoid the gatekeeper role, even though the abuses of expert testimony clearly affect the integrity of the system. Many of these problems can be avoided by declaring that a separate, pre-trial Daubert hearing is required. Of course, adjusting the timing cannot fix all of the problems, but the explicit emphasis on the trial judges' role will prompt other fixes, as will be discussed in the following sections. Requirement for pre-trial hearings will have other concomitant advantages on the trial system as well, since a pre-trial hearing will impact trial strategy and will provide a more effective safeguard than manifestly ineffective alternatives of motions in limine, or voir dire or cross-examination during trial.

The Ninth Circuit in Alatorre acknowledged that there would be appropriate circumstances for the trial judge to conduct a separate pre-trial hearing. But an analysis of the impacts of pre-trial hearings shows that they would always be appropriate. The alternative methods, voir dire or cross-examination, cannot, by their nature, be as effective. The emotionally charged atmosphere of the courtroom is not appropriate for resolving scientific issues. Any mid-trial challenges would necessarily involve trial delays, to which elected state judges would especially be sensitive, particularly when it comes to

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221 See generally Ridenour, supra note 219 (reporting that even Supreme Court Justice Breyer has publicly criticized the expert witness system, ridiculing in a 1998 speech a court that had allowed a witness to testify that dropping a can of orange juice could cause breast cancer).

222 See, e.g., Raul A. Gonzalez et. al., A Hypothetical Conversation Between a Judge and an Expert, 9 KAN. J.L. & PUB. POL'Y 56 (1999) (describing the role of juries to legitimize the actions of the judiciary).

223 See, e.g., Ohio Academy of Trial Lawyers v. Sheward, 715 N.E.2d 1062 (Ohio 1999). Here, the Ohio legislature imposed statutory controls on judicial determinations of toxic tort cases. Id.

224 See generally Board of Regents v. Roth, 408 U.S. 564, 592 (1972) (demonstrating an analogous situation requiring fact-finding administrative agencies to develop a factual record when decisions must be justified with sound reasons, conduct in making those decisions is likely to be more cautious, careful, and circumspect). But see Joiner, 522 U.S. at 146 (holding that judges are held to an abuse of discretion standard). Cf Alatorre, 222 F.3d at 1105 (requiring no particular form of pre-trial hearing).

225 See Judge Harvey Brown, Procedural Issues Under Daubert, 36 Hous. L. Rev. 1133, 1144 (Winter 1999) (comparing advantages of a pre-trial Daubert hearing, among them that key strategic decisions that depend on the expert may be irrevocable in the middle of trial).

226 See Alatorre, 222 F.3d at 1105.

227 See Daubert, 509 U.S. at 596 (advocating these traditional means of attacking evidence). The Court does forecast how these means would work in a contrived environment. Id.

explaining to their electors who are the jurors why they must wait for something to be done that could have been better done before trial.\(^\text{229}\) In some instances this time factor can be quite significant: the thorough briefing required of a realistic Daubert hearing in particularly complex subjects could consume from days to weeks.\(^\text{230}\) At the same time, the party against whom the expert testimony is offered can avoid the prejudice, particularly if later excluded, of having the jury exposed to the evidence during jury voir dire, opening statements, and questions to witnesses.\(^\text{231}\) Both sides of the issue would benefit from adjusting their trial strategy. An opportunity to obtain a definitive pre-trial ruling\(^\text{232}\) would allow them to pre-try issues and educate the judge, while avoiding the expense of preparing a doomed trial plan. Courts, too, would benefit by being able to rule on cases at summary judgment before trial, if the expert issues were thoroughly briefed and resolved then.

Cross-examination and voir dire, considered sufficient to make the record in Alatorre, are manifestly ineffectual ways to present a useful Daubert challenge. If the questioner lacks the benefit of adequate disclosure or his own expert to guide him, his examination would be fruitless.\(^\text{233}\) Worse, he runs the risk of failing to adequately explain complex points to the jury, and may reveal enough to make matters worse.\(^\text{234}\) And the expert, by the act of having been hired, will likely survive this type of questioning by virtue of his superior knowledge and practiced communications skills.

VII. COMMONLY PROPOSED CORRECTIONS

A review of the literature reveals numerous suggestions to correct the deficiencies of the Daubert hearing application. Several scholarly analyses have urged emphasis on enforcing existing disclosure rules under Civil Procedure Rule 26 and Criminal Procedure Rule 16.\(^\text{235}\) However, disclosure alone would be

\(^{229}\) See Harvey Brown, *Procedural Issues Under Daubert*, 36 Hous. L. Rev. 1133, 1144 (Winter 1999) (listing some of the steps many judges will take to minimize this problem, as well as the additional frustration jurors will feel, when striking the expert upon whom the case relied would amount to a directed verdict and their efforts would have been wasted).

\(^{230}\) See, e.g., James J. Brosnahan, *Motions in Limine in Federal Civil Trials*, SE56 ALI-ABA 1, 29 (describing hearings on admissibility that lasted from several days to several weeks).

\(^{231}\) Id. (including expense to the parties of having experts getting high fees for appearances at whatever time during the trial the judge will hold whatever reliability proceeding he selects).

\(^{232}\) Cf. Luce v. United States, 469 U.S. 38, 41 (1984) (providing an exposition of the principle that motions in limine are subject to change, and the trial judge is free in the exercise of discretion to alter a previous in limine ruling).


\(^{234}\) See, e.g., THOMAS A. MAUET, *FUNDAMENTALS OF TRIAL TECHNIQUE* 382 (2000) (illustrating why voir dire can turn back on the challenger when the trial judge directly or indirectly validates the witness as an expert and showing the challenger as having been ineffective).

\(^{235}\) FED. R. CIV. P. 26 and FED. R. CRIM. P. 16 both provide for disclosure of expert testimony from adverse parties. *But see* FED. R. CIV. P. 26 advisory committee's notes for an explanation of why
inadequate without a meaningful opportunity to use this information adequately. Court-appointed experts are permitted under Rule 706, but in practice this has not yielded a solution since courts are reluctant to impose this cost on parties. Delegating the evaluation to a panel would solve the capability issue, but impartial panels would be difficult to implement on a widespread basis, and again abdication of judicial responsibility claims would be raised. Still others have suggested imposing ethical restraints on experts, a solution that might work for the regulated legal profession, but would be impractical for the dispersed, heterogeneous scientific community.

A recent real attempt at change has occurred. In the years since the adoption of the Federal Rules, numerous proposals have been made for amendments, with the most recent change to the rule at issue, Rule 702, taking effect in December, 2000. The amended Rule 702 adds provisions to require that expert opinion testimony is permitted:

provided that (1) the testimony is sufficiently based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case.

This change appears to codify portions of Daubert, but still does not answer timing or competence issues. At least one commentator advocates rewriting the Rules completely since adjusting faulty rules will not solve the problems they currently engender.

VIII. PROPOSAL

Based on the analysis above, a proposal to address the problems stated would have three main elements: (1) a pre-trial Daubert hearing that would result in a final ruling on the record on admissibility of expert testimony; (2) a renewed emphasis on the Frye general-acceptance feature of Daubert; and (3) continuing legal education requirements for attorneys and judges in applying law to scientific evidence.
First, the pre-trial aspect would provide more time\textsuperscript{241} to brief and analyze the issues, and make use of the judge's institutional advantage over jurors in evaluating the proffered evidence.\textsuperscript{242} In the event the judge decides the testimony is familiar from previous cases and reliable, he can take judicial notice of it or emphasize its general acceptance in his ruling. The final ruling will encourage the judge to explain his decision, which will further encourage better analysis and efforts at bias correction.\textsuperscript{243}

Second, the \textit{Frye} general-acceptance standard was overruled in \textit{Daubert} because of the Court's "plain meaning" approach,\textsuperscript{244} but the earlier decision in \textit{Downing}\textsuperscript{245} upon which the \textit{Daubert} court drew,\textsuperscript{246} agreed with other decisions that \textit{Frye} survived adoption of the Federal Rules,\textsuperscript{247} and regarded it as decisive in many cases.\textsuperscript{248} Even novel science would have some basis in generally accepted principles; the burden of proof would be on the proponent to satisfy a \textit{Daubert} challenge.\textsuperscript{249} The independent advisor appointed under Rule 706 would assist the judge in evaluating the extensive evidence as needed, with the judge making the final ruling based on this guided review.\textsuperscript{250}

Since science cannot always be certain to a one-hundred-per-cent level, there will be times when experts in good faith can disagree on their opinions, and so the judge would still have a critical decision-making role, particularly in cases with conflicting evidence. These decisions would be informed by continuing education, where judges will acquire sufficient background for cases as they currently must do when performing review of agency actions.\textsuperscript{251} When there are so many alternatives to correct the real and perceived shortcomings of the current system, a broad grant of discretion to the trial judge to implement essentially subjective standards is not the answer, particularly where, as the

\textsuperscript{241} See Judge Harvey Brown, \textit{Procedural Issues Under Daubert}, 36 Hous. L. Rev. 1133, 1144 (Winter 1999). The author, a judge, recommends that \textit{Daubert} challenges be made at least thirty days before trial. \textit{Id}.

\textsuperscript{242} See United States v. Shonubi, 895 F. Supp. 460, 479-80 (E.D.N.Y. 1995). Since \textit{Kumho Tire}'s extension of the \textit{Daubert} analysis to all expert testimony, courts will also likely benefit from the additional time to ascertain the standards of fields not previously subject to such analysis. \textit{Id}. See, \textit{e.g.}, \textit{Kumho Tire}, 526 U.S. at 150 (reiterating the diverse types of expertise available, to which courts must adapt the flexibility provided in \textit{Daubert}).

\textsuperscript{243} \textit{Id}. at 487.


\textsuperscript{245} United States v. Downing, 753 F.2d 1224 (3rd Cir. 1985).

\textsuperscript{246} \textit{Daubert}, 509 U.S. at 594.

\textsuperscript{247} \textit{See Downing}, 753 F.3d at 1234.

\textsuperscript{248} \textit{Id}. at 1238.

\textsuperscript{249} \textit{Id}. at 1242.

\textsuperscript{250} \textit{See}, \textit{e.g.}, \textit{Joiner}, 522 U.S. at 149 (Breyer, J., concurring) (advocating the use of court-appointed experts as an integral part of coping with the increasing use of scientific and technical experts in litigation of all types).

\textsuperscript{251} \textit{See}, \textit{e.g.}, \textit{Ethyl Corp. v. EPA}, 541 F.2d 1, 68 (D.C. Cir. 1976) (Leventhal, J., concurring) (explaining that the present system assumes that judges will acquire whatever technical knowledge is necessary as background for decisions, particularly in the complex area of review of agency actions).
Ninth Circuit endorsed in *Alatorre*, the authority permits the judge to shift his burden to the jury, in the hope that they can somehow evaluate expert evidence that he can not.

**IX. CONCLUSION**

The current level of public criticism directed at the courts cries out for reasoned change, change that will not happen with minor Rules amendments or court opinions seeking to further shift the analytical burdens to an untrained jury. Prior delegation of the responsibility under *Frye* left the judiciary unprepared to assume the role of gatekeeper, but efforts to educate the legal community, motivated by the need to make informed, recorded decisions in advance of trial, will benefit the quality of litigation in today's courts.