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Editor's Corner

The Annual Meeting of the MidAtlantic Academy of Legal Studies in Business was held on March 24-25, 2006, at the High Regency Baltimore in Baltimore, Maryland. The Annual Meeting was attended by approximately thirty-two faculty and students. Normally, the academic program includes papers on teaching, employment, constitutional, curriculum development, civil procedures, tort, intellectual property, environmental, accountant liability, bankruptcy law and corporate law.

We give special thanks to Program Chair Dan Cahoy, Penn State University, for planning the academic program. We also give a special thanks to West Publishing and Penn State University for their generous support of the 2006 MAALSB Annual Meeting.

The next Annual Meeting will be held in St. Michaels Maryland, in March 2007. Please join us in St. Michaels. We encourage all ALSB members, other professors and professionals to participate. We will have paper presentations and a great luncheon, we look forward to seeing you in St. Michael's.

The *ALJ* is a refereed journal. The *ALJ* is listed in *CABELL'S* DIRECTORY OF PUBLISHING OPPORTUNITIES IN MANAGEMENT AND MARKETING. We encourage all readers to prepare and submit manuscripts for publication in the *Atlantic Law Journal.*

James E. Holloway
Editors-in-Chief

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ARTICLES

Nonprofit Status and the Public Policy Exception Revisited: How Much Does Freedom of Belief Cost?

Karen Gantt*

I. Introduction

In recent years, the fundamental beliefs of some morally- or religiously-based organizations[1] have come into conflict with the values of other segments of society. This clash of values can be seen in areas such as life support[2], the morning after pill and faith-based hospitals[3], stem cell research[4] and gay rights.[5] Freedom of association necessarily results in the exclusion of or discrimination against other segments of society.

At the same time, many religious organizations are involved in the local community and have a primary mission of service including

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[1]. Examples include the Boy Scouts, the Christian Legal Society and religiously-affiliated hospitals. This paper does not address religious institutions themselves such as churches, synagogues or mosques as standards governing the internal operations of these institutions have developed under a different line of court reasoning.

[2]. *See* Schiavo *ex. rel.* Schlinder v. Schiavo, 357 F. Supp. 2d 1378 (2005), wherein it was alleged, *inter alia*, that Theresa Schiavo's right to exercise her religion was burdened by the state court's order to remove the feeding tube.

[3]. Christopher Keating, THE HARTFORD COURANT, *Bishops Accept Contraceptive Law,* September 28, 2007, at A1. In a major softening of their position, the state's Roman Catholic bishops announced that Catholic hospitals would comply with a new law that requires all hospitals in the state, including Catholic facilities to dispense emergency contraceptive pills to rape victims. Catholic Bishops had lobbied strongly against the legislation for over a year. Although the bishops and other Catholic health care leaders believe that this law is seriously flawed, they do not believe it is sufficiently flawed to bar compliance with the laws provisions at this time.

[4]. Nicholas Wade, *Clarification Issued on Stem Cell Work*, THE NEW YORK TIMES, Sept. 2, 2006, at 13 (criticism from the United States Conference of Catholic Bishops, which pointed out that embryos used in the research were being destroyed).

[5]. Peter Steinfels, *The Combat of America's 'Culture Wars' Takes Place Within Political Parties Instead of Between Them*, THE NEW YORK TIMES, Aug. 5, 2006, at 11 (Same sex marriage is opposed by 78 percent of white, evangelical Protestants and 74 percent of African-American Protestants. Moreover, 58 percent of white, non-Hispanic Catholics are opposed to the sex marriage. Mainline Protestants are almost split evenly. Only those identified by the researchers as "secular" are solidly in favor, by 63 percent to 27 percent).

providing food and clothing for the needy, maintaining soup kitchens and food pantries, providing shelter to the homeless and counseling individuals and families.[6] Some may question whether these nonprofit organizations, whose religious beliefs motivate them to serve the community, should be punished for adhering to their fundamental moral or religious beliefs, which are protected by the First Amendment,[7] when those beliefs clash with societal beliefs.

This article examines the impact this conflict can or should have on a nonprofit organization's tax exempt status and other government subsidies. As well, this article provides some suggested guidance on the standard that the Internal Revenue Service (I.R.S.) should use in determining whether tax exempt status should be affected by the nonprofit's stance.

II. Freedom of Association – Boy Scouts of America v. Dale

In *Boy Scouts of America v. Dale*,[8] the Boy Scouts approved Dale's application for the position of assistant scoutmaster of Troop 73. Around the same time, Dale left home to attend Rutgers University. After arriving at Rutgers, Dale first acknowledged that he was gay. He became the co-president of the Rutgers University Lesbian/Gay Alliance. In 1990, a newspaper interviewed Dale about his advocacy of homosexual teenagers' need for gay role models. In early July 1990, the newspaper published the interview and Dale's photograph over a caption identifying him as the co-president of the Lesbian/Gay Alliance. Later that month, Dale received a letter from Boy Scouts revoking his adult membership in the Boy Scouts. Dale was told that the Boy Scouts "specifically forbade membership to homosexuals."[9]

Dale filed a complaint against the Boy Scouts in the New Jersey Superior Court alleging that the Boy Scouts had violated New Jersey's public accommodations statute by revoking Dale's membership based solely on his sexual orientation. New Jersey's public accommodations statute prohibits, *inter alia*, discrimination on the basis of sexual orientation in places of public accommodation.[10] The Boy Scouts asserted that homosexual conduct was inconsistent with the values it seeks to instill in young people. Specifically, it asserted that homosexual conduct was inconsistent with the Boy Scout requirement

[6] Ram Cnaan, *Our Hidden Safety Net: Social and Community Work by Urban American Religious Congregations*, Brookings Rev., Spr. 1999, at 50, 50-51.

[7] U.S. CONST. amend I.

[8]. 530 U.S. 640 (2000).

[9] *Id.* at 643.

[10] *Id.*

of being "morally straight." The United States Supreme Court held that the Boy Scouts have a First Amendment right to "expressive association" and can revoke and/or refuse membership to an avowed homosexual and gay rights activist since requiring the group to grant membership would limit the Boy Scouts' ability to express its viewpoint. As a result, the Court determined that as applied to the Scouts, New Jersey's laws banning discrimination violated the Boy Scouts' First Amendment rights.[11]

Years earlier, in *Norwood v. Harrison*,[12] state of Mississippi officials loaned state-owned textbooks to students attending racially-segregated private schools in the State. It was undisputed that the creation and enlargement of private schools in Mississippi occurred simultaneously with major events in the desegregation of public schools. The Court held that providing the textbooks was, in effect, a form of indirect funding and endorsement of the schools' discriminatory practices. The Court, under these circumstances, noted that while "invidious private discrimination may be characterized as a form of exercising freedom of association protected by the First Amendment, it has never been accorded affirmative constitutional protections."[13]

Later, in *Roberts* v. *United States Jaycees,*[14] the Court noted that "implicit in the right to engage in activities protected by the First Amendment"[15] is "a corresponding right to associate with others in pursuit of a wide variety of political, social, economic, educational, religious, and cultural ends."[16] The right to expressive association is "especially important in preserving political and cultural diversity and in shielding dissident expression from suppression by the majority."[17] Regulations that force a group to accept members it does not want can impair the group's ability to espouse its views and therefore, "[f]reedom of association . . . plainly presupposes a freedom not to associate."[18]

[11] *Id.* at 656. Earlier, the Supreme Court of New Jersey had ruled that the Boy Scouts were a "public accommodation" for purposes of the State sexual orientation anti-discrimination law. *See* Dale v. Boy Scouts of America, 160 N.J. 562, 605, 734 A.2d 1196, 1219 (1999)).

[12] 413 U.S. 455 (1973).

[13] *Norwood*, 413 U.S. at 470 (The court distinguished permitting funding to private, religious schools under the first amendment's free exercise clause for secular purposes, such as textbooks from funding racial discrimination which violated the thirteenth amendment).

[14] 468 U.S. 609 (1984).

[15] *Id.* at 622

[16] *Id.*

[17] *Id.*

[18] *Id.*

Although *Dale* confirmed the right to freedom of association, *Norwood* and many subsequent lower court decisions make clear that public funds should not subsidize the right of expressive association of nonprofit organizations.[19] At the same time, some question whether refusing to fund expressive association constitutes punishing a group for adhering to its moral or religious beliefs, which are protected by the First Amendment, simply because those beliefs clash with societal beliefs.

III. Federal Tax Exemption

The approach taken by the Courts and the I.R.S. has not been viewed as a question of punishing a set of beliefs. Rather, it has become a question of whether society should pay for actions, which the majority deems discriminatory. As discussed more fully below, taxpayers may be viewed as indirect contributors to nonprofit organizations. Sometimes charitable organizations provide a benefit that society would not have chosen, but it must be a benefit that serves and is in harmony with the public interest and there are certain actions which have been deemed categorically against the public interest.

A. Denial of Exemption Based on Discrimination

Bob Jones University v. United States[20]provides some guidance but does not completely resolve the issue. In *Bob Jones*, the nonprofit University had an official policy of denying admission to married interracial couples or to individuals who publicly advocated interracial marriage or interracial dating. The sponsors of Bob Jones University genuinely believe that the Bible forbids interracial dating and marriage.[21] Because the University's admissions policy was discriminatory under federal law, the I.R.S. revoked the University's tax-exempt status.

In an earlier Revenue Ruling the I.R.S. had established that "a school not having a racially nondiscriminatory policy as to students is not 'charitable' within the common law concepts reflected in Sections

[19] *See, e.g.*, Boy Scouts of America v. Wyman, 335 F. 3d 80 (2nd Cir. 2003), *cert. denied*, 541 U.S. 903 (2004), Evans v. City of Berkley, 38 Cal. 4th 1, 129 P.3d 394, 40 Cal. Rptr. 3d 205 (2006), *cert. denied*, 127 S. Ct. 434 (2006).

[20] 461 U.S. 574 (1983). Bob Jones University v. United States, 461 U.S. 574 (1983), was heard together with Goldsboro Christian Schools, Inc. v. United States, 461 U.S. 574 (1983).

[21] *Id.* at 580.

170 and 501(c)(3) of the Internal Revenue Code.[22] . The University claimed that the Services actions violated the University's rights to freedom of religion under the First Amendment. Moreover, in the companion case of *Goldsboro Christian School,*[23] the private school's tax exemption was denied because Goldsboro Christian School, for the most part, only accepted white students. The School maintained, based on its interpretation of the bible, that mixing of the races was a violation of God's command.

The Court affirmed the I.R.S.s revocation of Bob Jones' tax exemption and denial of Goldsboro's tax exempt status. The Court reasoned that an entity's activities may so violate public policy, in this case the public policy against racial discrimination, that the entity involved cannot be deemed to provide a public benefit worthy of "charitable" status under § 501(c)(3) of the Internal Revenue Code.[24] The Court concluded that the School's First Amendment Free Exercise Clause is not violated when schools cannot receive funding for discrimination based on, sincerely held religious beliefs.[25] The Court emphasized that the government has a compelling, overriding interest in eradicating racial discrimination in education that substantially outweighs whatever burden the denial of tax benefits places on the Schools' exercise of its religious beliefs.[26] In addition, the Court determined that the Service's regulation did not violate the Establishment Clause of the First Amendment because the Service's regulation is based on a neutral, secular policy that applies uniformly to all religiously operated schools.[27]

According to *Bob Jones*, if a nonprofit's activity violates fundamental public policy, the group cannot be considered charitable within the meaning of Section 501(c)(3). The Court stated that:

> Section 501(c)(3) therefore must be analyzed and construed within the framework of the Internal Revenue Code and against the background of the congressional purposes. Such an examination reveals unmistakable evidence that, under-lying all relevant parts of the Code, is the intent that entitlement to tax

[22] Rev. Rul. 447, 1971-2 C.B.230.

[23] 461 U.S. 574 (1983).

[24] *Bob Jones*, 461 U.S. at 598.

[25] Earlier, in *Runyon v. McCrary*, 427 U.S. 160 (1976) the U.S. Supreme Court decided similarly in a case involving discrimination by a private, commercially-operated, non-sectarian school that discriminated against two black applicants on the basis of race. There, the Court found that there was no violation of the right of free association.

[26] *Id.* at 603.

[27] *Id.* at 604.

> exemption depends on meeting certain common-law standards of charity -- namely, that an institution seeking tax-exempt status must serve a public purpose and not be contrary to established public policy.[28]

The Court's decision concerned religious, educational institutions but did not address other religious institutions such as churches. In fact, the *Bob Jones* Court noted:

> We deal here only with religious *schools* -- not with churches or other purely religious institutions; here, the governmental interest is in denying public support to racial discrimination in education. As noted earlier, racially discriminatory schools "[exert] a pervasive influence on the entire educational process," outweighing any public benefit that they might otherwise provide, (*internal citations omitted*).[29]

The Court did not address what would happen in cases involving discrimination by churches or other religiously based nonprofit institutions. However, the Court's analysis and reasoning in *Bob Jones*, would apply to other nonprofits.

Section 501(c)(3) of the Internal Revenue Code provides that "[corporations] . . . organized and operated exclusively for religious, charitable . . . or educational purposes" are entitled to tax exemption.[30] Petitioners in *Bob Jones* asserted that I.R.C. § 501(c)(3) gave them tax exempt status without being required to be a "charitable" institution. They argued that they merely needed to be organized for educational purposes. However, the Bob Jones Court rejected Petitioner's argument and stated that all Section 501(c)(3) organizations must meet a charitable standard. In defining charity, the Court noted that:

> "'Charity' in its legal sense comprises four principal divisions: trusts for the relief of poverty; *trusts for the advancement of education*; trusts for the advancement of religion; and trusts for *other purposes beneficial to the community*, not falling under any of the preceding heads." (*emphasis added*)[31]

Thus, the Court's rationale that "charitable" organizations would include educational institutions, such as Bob Jones University, religious

[28] *Bob Jones*, 461 U.S. at 587.
[29] *Id.* at 604.
[30] I.R.C. §501(c)(3) (1988).
[31] *Bob Jones*, 461 U.S. at 589.

institutions, and all other categories of organizations that benefit the community[32]

> The court also relied on *Perin* v. *Carey* and stated that: [It] has now become an established principle of American law, that courts of chancery will sustain and protect . . . a gift . . . to public charitable uses, *provided the same is consistent with local laws and public policy. . .*"[33]

The Court continued its analysis by noting that "Congress sought to provide tax benefits to charitable organizations, to encourage the development of private institutions that serve a useful public purpose or supplement or take the place of public institutions of the same kind."[34]

The Court suggested that without an accompanying "charitable" requirement, the term "educational" could be interpreted to include the 'Fagin School for Pickpockets' or a school for training students for guerrilla warfare or terrorism in other countries. Justice Rhenquist, writing for the dissent, was bothered by the Court's adoption of a concurrent "charitable" standard. He noted that if any clarity was needed in order to determine what Congress meant by the term "educational" in I.R.C .§ 501(c)(3), the I.R.S. had already provided it.[35] He explained that the definition contained in the Treasury Regulations[36] was clearly sufficient to exclude pickpocket, terrorism and guerilla warfare training.[37]

One commentator brought up the fact that the September 11, 2001, terrorist attacks opened our eyes to the fact that U.S. taxpayer dollars were indeed going toward funding terrorist activities overseas.[38] At a minimum, clarification of the Treasury regulations defining what constitutes "educational" activities within the meaning of I.R.C. §

[32] *Id.*
[33] *Id.* at 588 (citing Perin v. Carey, 24 How. 465, 501 (1861) (emphasis added)).
[34] *Id.*
[35] *Id.* at 617 (Rehnquist, J., dissenting).
[36] Treas. Reg. § 1.501(c)(3)-1(d)(3), 26 CFR 1.501(c)(3)-1(d)(3) (1982). The Regulation defines "educational" as instruction or training of the individual for the purpose of improving or developing his capabilities; or instruction of the public on subjects useful to the individual and beneficial to the community." *Id.* Because the disjunctive "or" is used in the regulation, perhaps a pickpocket school would qualify since it is developing the criminal's capabilities!
[37] *Bob Jones*, 461 U.S. at 617.
[38] *See, e.g.*, Hinnen, *The Cyber-Front in the War on Terrorism: Curbing Terrorist Use of the Internet*, 5 COLUM. SCI. & TECH. L. REV. 5 (2004) (Hinnen states that "[b]y publicizing terrorists' use of charity websites to raise funds and by encouraging donors to learn about a charity before contributing to it, government and private organizations can reduce the amount of unwitting donations made to terrorist groups" *Id.*).

501(c)(3) is needed. Certainly the requirement of a simultaneous "charitable" standard, made clear that terrorist activities are not valid educational organizations because they do not meet the public policy requirement for charitable organizations

Prior commentaries have discussed the benefits, legislative history and Congressional intent in establishing a charitable deduction. These include serving a desirable public purpose and relieving the government of financial burden that would otherwise exist.[39] Accordingly, in floor debate in 1917 concerning charitable tax exemption, Senator Hollis stated the reason for the tax exemption as follows: "For every dollar that a man contributes for these public charities, educational, scientific, or otherwise, the public gets 100 per cent."[40] Finally, in 1938, according to the *Congressional Record*, the purpose of the charitable deduction was stated as follows:

> The exemption from taxation of money or property devoted to charitable and other purposes is based upon the theory that the Government is compensated for the loss of revenue by its relief from financial burdens which would otherwise have to be met by appropriations from other public funds, and by the benefits resulting from the promotion of the general welfare.[41]

In *Bob Jones*, the Court affirmed that when the government grants a tax exemption, it not only affects the institution receiving the exemption, but all of society. In effect, taxpayers are indirect donors or contributors to the organization. Charitable organizations must therefore serve a public benefit. A benefit which society or the community may not have chosen, but which advances the work of the government or public institutions supported by tax revenues.[42]

Furthermore, the Court emphasizes that in order to be exempt under I.R.C. § 501(c)(3), an institution must fall within one of the several categories listed in I.R.C. § 501(c)(3) and must "serve and be in harmony with the public interest. The institution's purpose must not be so at odds with the common community conscience as to undermine any public benefit that might otherwise be provided."[43] Therefore, the test for exempt status is two-fold; and if an organization's purpose is not in harmony with the public interest or so against the community

[39] *See, e.g.*, Reiling, *Federal Taxation: What Is a Charitable Organization?*, 44 A. B. A. J. 525 (1958).

[40] 55 Cong. Rec. 6728. (1917).

[41] H. R. Rep. No. 1860, 75th Cong., 3d Sess., 19 (1938).

[42] *Bob Jones*, 461 U.S. at 591.

[43] *Id.* at 592.

conscience, a religiously-based educational institution, and presumably other types of nonprofits, will not satisfy the public benefit requirement for exempt status.

B. Exemptions and Permissible Discrimination

Not addressed by the Court in *Bob Jones* is whether there are times when discriminating against groups is permissible by a nonprofit organization and what standard should be used. The recent decision in *Doe v. Kamehameha Schools*[44] and earlier I.R.S. rulings are instructive. In *Kamehameha Schools*, the school is a tax-exempt charitable trust created by the will of Bernice Pauahi Bishop. The purpose of the trust is "to erect and maintain in the Hawaiian Islands two schools, each for boarding and day scholars, one for boys and one for girls, to be known as, and called the Kamehameha Schools."[45] The school requires that all admitted students have "at least one Hawaiian ancestor."[46]

The Hawaiian lineage requirement is only one of many factors considered when making admissions decisions for the Kamehameha Schools. The school receives more applications from potential students than it can accommodate. It therefore turns away many people who are interested in attending. However, all students admitted must have at least one Hawaiian ancestor. This Hawaiian lineage admission requirement was challenged as discriminatory.

The Kamehameha Schools are non-profit, rather than commercial. But the schools still charge tuition (albeit at a rate that represents only a fraction of the cost to educate students), and a bargained-for exchange of payments for instruction exists.[47] As a result, the Court determined that § 1981[48] applies in determining whether the admissions policy was impermissibly discriminatory on the basis of race.[49]

The United States Court of Appeals for the Ninth Circuit held that a § 1981 suit against this purely private, non-profit school is governed by the standards applicable to race-based challenges brought

[44] 470 F.3d 827 (9th Cir. 2006).

[45] *Id.* at 831.The schools are now combined into one co-educational school enrolling both boys and girls.

[46] *Id.* at 831.

[47] *Kamehameha*, 470 F. 3d at 837.

[48] 42 U.S.C. § 1981 (This section requires equal protection in making and enforcing contracts and the enjoyment of all benefits privileges, terms, and conditions of a contractual relationship.... *Id.* at § 1981 (a) and (b)).

[49] The Court noted that "we need not and do not decide whether § 1981 would apply if the Schools charged no tuition at all, but simply donated education to Native Hawaiian students." *Kamehameha*, 470 F. 3d at 837.

pursuant to Title VII of the Civil Rights Act of 1964 (Title VII).[50] This test has three parts. First, the plaintiff must establish a prima facie case of intentional race discrimination. Secondly, the defendant must show that there is a legitimate nondiscriminatory reason justifying the challenged practice. Finally, if such a reason is offered, the plaintiff may show that the reason proffered by the defendant is merely a pretext for unlawful race discrimination.[51]

The Title VII test for evaluating affirmative action plans applied. The court of appeals then adapted the Title VII employment framework to the educational context and unique historical circumstances of this case. To justify its remedial racial preference, the private school demonstrated that specific, significant imbalances in educational achievement presently affect the Hawaiian population as a whole. At the same time, the school was able to demonstrate present disparities in educational achievement as distinguished from general past societal discrimination.[52]The court of appeals then focused on the rights of members of the non-preferred group noting that an admissions policy must not "unnecessarily trammel" the rights of students in the non-preferred class or "create an absolute bar" to their advancement. Finally, the court stated that an admissions policy must do no more than is necessary to remedy the imbalance in the community as a whole.

The court of appeals concluded that since the Schools preferential admissions policy is designed to counteract the significant, current educational deficits of Native Hawaiian children in Hawaii, and because Congress clearly intended § 1981 to exist in harmony with its other legislation providing specially for the education of Native Hawaiians, that the admissions policy is valid under 42 U.S.C. § 1981.[53]

In a 1975 General Counsel Memorandum[54] responding to an inquiry from the I.R.S. concerning a racially restrictive scholarship trust limited to Caucasian students, the native Hawaiian ancestry policy was also considered. There, it similarly concluded that the Hawaiian ancestry requirement was not contrary to public policy because "[t]he limited preference that has been given to all applicants who can

[50] 42 U.S.C. § 2000(e) *et seq.* (2004).

[51] *See McDonnell Douglas*, 411 U.S. at 802. Note that Title VII scrutiny requires the Schools to merely "present evidence that the plaintiff was rejected, or the other applicant was chosen, *for a legitimate nondiscriminatory reason.*" *Patterson v. McLean Credit Union*, 491 U.S. 164, 187, 105 L. Ed. 2d 132, 109 S. Ct. 2363 (1989) (emphasis added).

[52] *See City of Richmond v. J. A. Croson Co.*, 488 U.S. 469, 505-06 (1989).

[53] *Kamehameha*, 470 F. 3d at 849.

[54] Gen. Couns. Mem. 36, 363, (Aug, 7, 1975).

establish the smallest possible degree of Hawaiian ancestry does not appear to be contrary to any clearly-established public policy with regard to racial discrimination. The program was determined to be directed toward furthering a public policy to assist a limited class, and was not of a type which operated contrary to the public policy against racial discrimination such as the Caucasian only policy.

In an earlier General Counsel Memorandum,[55] a testamentary gift establishing a racially restrictive scholarship trust in favor of African-American students was determined to be deductible. Although it was later noted that the opinion should be revoked on other grounds, the memorandum went on to state that it did not necessarily reject the ultimate conclusion in favor of the scholarship.[56]

The I.R.S. performed a similar analysis in a 1977 Private Letter Ruling involving a tax-exempt scholarship fund limited to males.[57] In the ruling the I.R.S. observed that Federal courts have not established that sex discrimination is clearly contrary to public policy. Relying on *Stanton v. Stanton*,[58] the I.R.S. used a "rationality" test to determine that the classification met a fair and objective governmental purpose. According to the I.R.S., the classification based on sex is not automatically against Federal public policy and can be educationally and socially beneficial to the community at large.
Upholding programs that benefit racial minorities on the basis of correcting current disadvantage suffered by the group due to historical injustices have been upheld by both the courts and the I.R.S.. Such restrictive programs tend to meet the charitable definition.

IV. CURRENT DISCRIMINATION CASES RESULTING IN DENIAL OF GOVERNMENT FUNDING

A number of state court decisions have adopted policies denying funding to organizations that discriminate in violation of state laws. In *Boy Scouts of America v. Wyman*,[59] the state of Connecticut refused to permit the Boy Scouts to participate in a state employee charitable giving program[60] because the Boy Scouts' policy of

[55] Gen. Couns. Mem. 33,752 (Feb. 12, 1968),

[56] *See* Gen. Couns. Mem. 36, 363, (Aug, 7, 1975).

[57] *See* Priv. Ltr. Rul. 7744007 (Jul. 28, 1977).

[58] 421 U.S. 7, 13 (1975).

[59] *Wyman*, 335 F. 3d 80.

[60] *Id.* Connecticut state employees make voluntary contributions to charities selected from a list of participating organizations set forth in a booklet that is distributed at the workplace. Gifts are made by payroll deduction. The amount deducted is collected by the Comptroller and transmitted to a principal combined fund-raising organization, usually the United Way, that administers the Campaign for the state.

excluding homosexuals from membership violated Connecticut's Gay Rights Law.[61] In order to qualify for the charitable giving program, an organization was required, among other things, to sign a document certifying that the organization has a written policy on nondiscrimination.[62]

The Boy Scouts of America (BSA) had participated in the charitable giving campaign for 30 years and in its applications, the organization answered that it had a written policy of nondiscrimination. However, The Connecticut Commission on Human Rights and Opportunities ("CHRO") became concerned that by allowing the BSA to participate in the Campaign and to benefit from a fundraiser that used state resources, the Committee potentially made the state a party to discrimination. The BSA policy stated:

> In the exercise of its constitutional rights, Boy Scouts does not employ known or avowed homosexuals as commissioned professional Scouters or in other capacities in which such employment would interfere with Scouting's mission of transmitting values to youth. However, other jobs within Scouting are open to known or avowed homosexuals. . . . . In the exercise of its constitutional rights, Boy Scouts does not register known or avowed homosexuals as adult volunteer leaders or youth members.[63]

The *Dale* Court recognized the Boy Scouts' right to expressive association and held that the organization could not be compelled to admit persons who would compromise its message.[64] However, the Court did not resolve whether if rather than compelling the Boy Scouts to admit homosexuals, a state can remove the Boy Scouts from receiving funding if they choose not to satisfy the state's nondiscrimination policy.

The Supreme Court of Connecticut in *Wyman* held that refusing to fund the Boy Scouts did not violate the Boy Scouts' First Amendment expressive association rights, since it involved a nonpublic forum[65] and as in *Cornelius v. NAACP Legal Defense & Educational Fund, Inc.*[66] exclusion from the charitable giving campaign was not based on suppression of the Boy Scouts' viewpoint.[67] Excluding the Boy Scouts also did not violate the unconstitutional conditions

[61] Conn. Gen. Stat. §§ 46a-81a -46a-81r.
[62] *Wyman*, 335 F. 3d at 84.
[63] *Id.* at 85.
[64] *Dale*, 530 U.S. at 656.
[65] *Wyman*, 335 F. 3d at 92.
[66] 473 U.S. 788 (1985).
[67] *Wyman*, 335 F. 3d at 93.

doctrine. This doctrine requires that the government's exclusion of a group from funding be rational and not based on suppressing a particular viewpoint which it views as dangerous.[68]

According to the Second Circuit in *Wyman*, a law is viewpoint discriminatory only if its purpose is to specifically target and adversely impact a particular viewpoint.[69] On the other hand, a neutral law or regulation is valid even though it impacts an organization's ideas or philosophies.[70] Here, the purpose of Connecticut's Gay Rights Law is to protect people from the economic and social harms of discrimination rather than suppress the Boy Scouts of America's viewpoint.[71] Thus, the Boy Scouts' right to expressive association is not violated and no viewpoint discrimination exists by refusing to permit the group to participate in a state giving campaign.

Interestingly, the state supreme court had stated in dicta that a state may have a compelling interest, under the Fourteenth Amendment, in enforcing its anti-discrimination policies even if the federal government has not recognized the group's claim for equal protection purposes.[72] The Supreme Court of Connecticut emphasized that the Dale Court held that anti-discrimination laws were not sufficient to justify prohibiting freedom of association. But the state supreme court concluded that enforcing state anti-discrimination laws that *infringe upon*, but do not prohibit, freedom of association may be justified.[73]

Infringement upon the rights of expressive association, rather than prohibition, appears to be the objective in another case against the Boy Scouts. In *Evans v. City of Berkeley,*[74] the City had a policy of allowing nonprofits to dock their boats for free at the city-owned marina. The Sea Scouts, who are affiliated with the Boy Scouts, learn sailing, seamanship and other skills for a career in maritime.[75] The city of Berkeley rescinded the group's free marina berth after the Sea Scouts refused to abandon its policy towards gays and atheists.[76] The

[68] *See* Regan v. Taxation with Representation of Washington, 461 U.S. 540 (1983).
[69] *See Wyman,* 335 F.2d at 94 (citing R.A.V. v. The City of St. Paul, Minnesota, 505 U.S. 377, 390 (1992)).
[70] *Id.*
[71] *Id.*
[72] *Id.* at 92.
[73] *Id.*
[74] Evans v. City of Berkley, 38 Cal. 4th 1, 3 (2006), *cert. denied*, 127 S. Ct. 434 (2006).
[75] Craig Lazzeretti &Martin Snapp, *Berkeley Again Wins Row with Sea Scouts: State's high court rules city legally took subsidy away from group because of Boy Scouts affiliation, possible discrimination,* CONTRA COSTA TIMES (Mar. 10, 2006).
[76] *Evans*, 38 Cal. 4th at 9.

California Court of Appeals held that the City could condition access to a public benefit on the Boy Scout's voluntary relinquishment of its constitutional right to choose its membership. The Court of Appeals in *Evans* cited several U.S. Supreme Court decisions that state that a decision not to subsidize an organization does not violate a fundamental right.[77]

In a unanimous opinion, the Supreme Court of California affirmed the Court of Appeals decision and stated that "we agree with Berkeley . . . a government entity may constitutionally require a recipient of funding or subsidy to provide written, unambiguous assurances of compliance with a generally applicable non-discrimination policy."[78] The United States Supreme Court subsequently denied the Boy Scouts' petition for writ of certiorari, thus giving support to *Evans*, a California Supreme Court decision.[79]

The Sea Scouts contended that by refusing to allow them to participate in programs, the government is engaging in viewpoint discrimination.[80] However, the city of Berkeley did not refuse to let the Sea Scouts use the marina. Indeed, the Sea Scouts can still use it, but they now have to pay $500 per month. Further litigation is anticipated.[81]

In two other decisions in California, the federal courts reached similar decisions in discrimination controversies. First, in *Barnes-Wallace v. Boy Scouts*,[82] the city of San Diego and the Boy Scouts were sued by a lesbian and an agnostic couple and their Boy Scout-aged sons over leases which the city entered into with the Scouts. The Boy Scouts lease park facilities from the city. The District Court invalidated the Boy Scouts' lease on the grounds that the lease program violated the establishment clause. The city of San Diego maintained leases for the Girl Scouts, Camp Fire Boys and Girls, the YMCA, the Jewish Community Center, and several Presbyterian churches. The city of San Diego settled the case and agreed to pay Petitioner $950,000 in the settlement.[83] The Boy Scouts maintain that excluding them from the lease program amounts to viewpoint discrimination. According to the Civil Rights Division of the Department of Justice, "singling out the

[77] *Id.* at 11 (*citing*, Rust v. Sullivan, 500 U.S. at p. 198; *accord*, United States v. American Library Assn., Inc., 539 U.S. 194 (plur. opn. (2003)).

[78] *Id.* at 10.

[79] *See Evans*, 38 Cal. 4th at 1.

[80] *Id.* at 13.

[81] Lasseretti, *supra*, at n.75.

[82] 275 F. Supp. 2d 1259 (S.D. Cal. 2003), *petition for cert. filed*, 530 F. 3d 776 (9th Cir. 2008).

[83] George A. Davidson, Hughes, Hubbard and Reed, LLP, PR Newswire, *Boy Scouts' Statement in Response to City Settlement* (Jan. 8, 2004).

Boy Scouts for exclusion from the city's leasing program based on their viewpoint would raise serious First Amendment concerns." The Department Counsel noted that the Establishment Clause[84] is not violated when religion-related organizations are treated equally when granting participation in government programs.[85]

Christian Legal Society v. Kane[86] is a second and more recent federal court decision. In *Christian Legal Society*, the University of California refused to include the Christian Legal Society (CLS) as a recognized student organization and refused to fund the organization because of the CLS' position concerning homosexual students and non-orthodox Christians. Although CLS permitted everyone to attend meetings and participate in prayer and other activities, individuals who do not sign the CLS' statement of faith, individuals who engage in "unrepentant homosexual conduct"[87] or members of religions whose tenants of faith differ from those set forth in CLS' Statement of Faith could not become members or officers.[88] The University refused to allow the CLS to use college facilities and refused to fund their activities because the Group did not meet the requirements of Hastings' Non-Discrimination Policy.

The United States District Court for the Northern District of California concluded that CLS was not being *forced* to include certain members. However, the University could place conditions on both using the campus and providing subsidies. Thus its rights to expressive association were not violated.[89] Moreover, the District Court found that the nondiscrimination policy did not violate CLS' free speech rights as the policy regulated conduct and not speech. In other words,

[84] U.S. CONST. amend. I.

[85] Letter from Eric W. Treene, Special Counsel for Religious Discrimination, U.S. Department of Justice – Civil Rights Division, Office of the Assistant Attorney General. On file with the author.

[86] Christian Legal Soc'y v. Kane, No. C 04-0.4484 JSW, U.S. Dist. LEXIS 27347 (2006).

[87] 'Persons engaging in extramarital sexual conduct' was the exclusion used in Christian Legal Soc'y v. Crow, No. CV 04-2572-PHX-NVW, U.S. Dist. LEXIS 25579 (2006) (Christian Legal Society (CLS) and Arizona State University reached a settlement when the member and officer criteria evolved to exclude 'persons engaging in extramarital sexual conduct' and persons of different religious beliefs. The University acquiesced to permitting religious student organizations to require a shared religious belief, so long as the discrimination is not also based on a prohibited characteristic. *Id.* at 15.).

[88] *Kane*, U.S. Dist. LEXIS, at 11.

[89] *Id.* at 51.

the policy set forth what CLS had to do in order to receive benefits. The policy did not prohibit the group from expressing its viewpoint.[90]

In *Hsu v Roslyn Union Free School*,[91] a public high school subject to the Equal Access Act refused recognition of an after- school Bible Club on the ground that not allowing non-Christians to be officers of the club violated school policy prohibiting all students from discriminating on the basis of, inter alia, religion. In *Hsu*, the United States Court of Appeals for the Second Circuit held that when a sectarian religious club discriminates on the basis of religion for the purpose of assuring the religious character of its meetings, a school must allow it to do so. The court of appeals made the comparison that the chess club might require its officers to be skilled at chess-playing and emphasized that its holding was a narrow one. *Hsu* can be distinguished from the *Christian Legal Society* because in *Hsu*, the Equal Access statute specifically required religious organizations to have the same access to school facilities as other groups, the school's non discrimination policy did not prevent the Bible Club from having a Christian-only officer requirement.

Federal and state courts have permitted the denial of funding for nonprofits that discriminate, though the discrimination is based upon a fundamental belief of the religiously-based organization.[92] *Rumsfeld v. Forum for Academic and Institutional Rights*[93] yielded a somewhat different result. Although, the Supreme Court, in essence, affirmed the rationale of the lower state and federal court decisions. Nevertheless, the *Rumsfeld* decision also raises new questions that will be discussed at the end of this Part. In *Rumsfeld,* an association of law schools consisted of members whose policies opposed discrimination based on sexual orientation among other things. The schools wanted to restrict the military from recruiting on campuses because of the military's policy towards homosexuals in the military.[94] The schools challenged the enforcement of the Solomon amendments that require schools to provide military recruiters access to campus facilities equal

[90] *Id.* at 26; *See also*, Chi Iota Colony of Alpha Epsilon Pi Fraternity v. City University of New York, 502 F. 3d 136 (2nd Cir. 2007); *But see* Christian Legal Soc'y v. Walker, 453 F. 3d 853 (7th Cir. 2006).

[91] 85 F.3d 839 (2nd Cir. 1996), *cert. denied*, 519 U.S. 1040 (1996).

[92] Although not mentioned in these cases, states may be considered sanctioning or, indeed, participating in discrimination by permitting the organizations in question to continue to receive state funds or subsidies. *See, e.g., Norwood*, 413 U.S. at 470.

[93] 126 S. Ct. 1297 (2006).

[94] *See* 10 U.S.C. § 654 (2006). The provision provides that " a person generally may not serve in the armed forces if he has engaged in homosexual acts, stated that he is a homosexual or married a person of the same sex." *Id.*

to that provided to other recruiters or lose certain federal funds.[95] In effect, the schools sought to impose the same restriction on military recruiters that had been imposed on the Boy Scouts and Christian Legal Society. The schools argued that they were being forced to choose between enforcing their non discrimination policies or receiving funds and that the Solomon Amendments violated their freedom of expressive association and freedom of speech.

The Supreme Court stated that the schools' ability to say what they felt about the government's military employment policy also was not limited. The schools were not compelled to share the government's message. The Solomon Amendment regulates conduct (what the school must do to receive funding), not speech. The freedom of expressive association was not violated because the military recruiters did not become members of the school. The schools remained free to express their viewpoints.

Unlike the *Boy Scouts* and *Christian Legal Society* cases, the military in *Rumsfeld* was permitted to participate in activities, though it did not comply with the school anti-discrimination policy. There may be several distinctions that account for the different result. First, the *Rumsfeld* case involves Congress' broad powers to provide for the common defense and to raise and support armies.[96] The court stated that great deference must be given to this Congressional power.[97] Second, the government in *Rumsfeld* was not *seeking* funding from the University (albeit it was seeking assets in the form of campus recruits). Instead, it was *providing* funding conditioned on the school's compliance with its policies.

Rumsfeld did not address whether the Supreme Court would have allowed a recruiter, other than a military recruiter, to participate on campus if it discriminates.[98] The law is clear that organizations cannot discriminate in hiring or employment. *Rumsfeld* does not answer the question of whether organizations that discriminate can recruit on campus. The Supreme Court in *Rumsfeld* has indicated that

[95] *See* 10 U.S.C. § 654.

[96] U.S. CONST. art. I, § 8, cl. 1.

[97] Rumsfeld v. Forum for Academic and Institutional Rights, 126 S. Ct. 1297, 1306 (2006).

[98] *See also* Cuffley v. Mickes, the Ku Klux Klan, 208 F. 3d 702 (8th Cir. Mo. 2000), *cert. denied*, Yarnell v. Cuffley, 532 U.S. 903 (2001)(The court of appeals held that the Ku Klux Klan could not be denied the right to participate in the state's adopt-a-highway program solely because of its segregationist and racial superiority viewpoint. Unfortunately, the Supreme Court declined to hear the case.); *Cf.* Texas v. Knights of the Ku Klux Klan, 58 F. 3d 1075 (5th Cir. 1995)(The court of appeals denied the Klan's application to adopt a highway outside a public housing project to prevent the Klan from intimidating residents was reasonable and viewpoint neutral.).

merely allowing such an organization on campus is not an endorsement of the organization or its views by the university.[99]

V. *Removal of Federal Tax Exemption – The Future*

The Supreme Court has never addressed the specific issue of whether it is constitutional to require an organization to forego its constitutionally protected freedom of expressive association in order to obtain or maintain a Section 501(c)(3) tax-exemption. However, both Congress and the Supreme Court have addressed the issue of requiring an organization to voluntarily give up its free speech rights in order to obtain tax-exempt charitable standing. Under Section 501(c)(3), lobbying by charitable organizations is prohibited. In *Regan v. Taxation With Representation,*[100] the Supreme Court held that Congress' requirement that charities agree not to lobby Congress in order to meet the requirements for 501(c)(3) tax-exempt status is not a violation of the First Amendment because Congress is not required to, in effect, fund lobbying by granting a tax-exemption.[101] Although lobbying Congress is a free speech right, the Supreme Court in *Taxation With Representation* held that this right is not violated by the government's withdrawal of 501(c)(3) tax-exemption.

The standard announced in *Bob Jones* for revocation of tax exemption is violating a fundamental public policy and being so at odds with the community conscience as to undermine any public benefit that the organization might otherwise provide.[102] A number of states have found that an organization, such as the Boy Scouts of America or the Christian Legal Society, that exercises its right of expressive association also engages in discrimination that violates public policy. State and Federal courts have upheld denials of funding or subsidies as a result. However, the federal government has not, to date, removed federal tax exemptions in those same instances.

The Internal Revenue Service (I.R.S.) may decide in the future to revoke the tax-exempt status of quasi-religious organizations based on a discrimination standard. The issue of gay rights is an example. Currently, the civil rights laws do not make sexual orientation a

[99] *Rumsfeld*, 126 S.Ct. at 1309.

[100] Regan v. Taxation with Representation of Washington, 461 U.S. 540 (1983).

[101] Taxation with Representation of Washington, 461 U.S. at 540.

[102] *Bob Jones*, 461 U.S. at 592.

protected class.[103] Congress also passed such provisions as the Defense of Marriage Act and the Solomon Amendments both of which place limitations on the rights of homosexuals. However, in November 2007 the U.S. House of Representatives made history when it passed the Employment Non-Discrimination Act (ENDA).[104] ENDA would ban discrimination based on sexual orientation in employment. It would apply to employers with 15 or more employees including government employers, employment agencies and labor organizations, from discriminating in employment or employment opportunities on the basis of actual or perceived sexual orientation[105]. While the Senate came close to passing ENDA in 2002,[106] it did not pass. Should that law pass, removal of tax exemption for groups such as the Boy Scouts of America or the Christian Legal Society that discriminate based on sexual orientation could occur because the discrimination would be against clearly established public policy.

VI. *Impracticability of Applying a Differing Standard*

Without question, many religious organizations provide immeasurable help to communities. They are involved in the local communities and have primary missions of service including providing food and clothing for the needy, maintaining soup kitchens and food pantries, providing shelter to the homeless and counseling to individuals and families.[107] Despite the value that these organizations provide, there are times when these organizations believe that following societal law violates a fundamental belief or mandate.[108] In these instances, it is doubtful that first amendment religious or moral underpinnings alone will prevent removal of tax exempt status.

[103] 42 U.S.C. § 2000e *et seq.*, Title VII of the Civil Rights Act of 1964 prohibits employment discrimination based on race, color, religion, sex and national origin. *See also*, Romer v. Evans, 517 U.S. 620 (1996).

[104] Employment Non-Discrimination Act of 2007 (ENDA), H.R. 3685, 110th Cong., 1st Sess. (2007).

[105] *Id.*

[106] Employment Non-Discrimination Act of 2002, (ENDA), S. 1284, H.R. 2692 (2002). ENDA failed in the Senate by one vote (49-50) on September 10, 1996, the same day the Defense of Marriage Act legislation passed. ENDA was introduced again in 1997, 1999, and 2002 but failed to gain enough support in Congress to be debated or passed, Washington Office for Advocacy, http://www.uua.org/uuawo/new/article.php?id=429 (last visited August 1, 2006).

[107] Cnaan, *supra* note 6, at 50.

[108] Current examples include the Catholic Church and the morning after pill, requiring a religious organization to allow an atheist to be eligible for a leadership position or gay rights.

To date, with the exception of racial discrimination, the I.R.S. has not removed tax exemption for an organization's discriminatory treatment because no clearly established federal public policy exists prohibiting the treatment. However, if such public policy comes into existence, it would be difficult to establish a separate bright-line test for quasi-religious organizations. The I.R.S. would have difficulty distinguishing "permissible" discrimination based on a fundamental religious belief from "impermissible" discrimination based on that same belief. For instance, a religiously based organization cannot discriminate against minorities even if that is the group's fundamental belief.[109] Current law mandates enforcement of a neutral law of general applicability, even if that law impacts First Amendment rights[110].

To impose a different standard for quasi-religious groups would require the I.R.S. and the courts to examine the internal workings of a religious belief.[111] As an example, if a Christian group wants to exclude atheists, agnostics or those with non-orthodox beliefs from leadership positions, as the Christian Legal Society attempted, the Service would be required to evaluate the validity and underpinnings of the group's religious faith. In so doing, the Service would become unnecessarily entangled in the religious operation of the organization in order to determine tax exemption.[112] Congressional legislation similar to the Equal Access Act discussed in *Hsu*[113] or legislation granting a "shared religious belief" exemption may be a better approach.

It is also impracticable for courts to make a determination that some activities of the organization are permissible and the remaining activities impermissible and taxable. Although this approach is used when nonprofits are involved in commercial activities through Unrelated Business Income Tax provisions (UBIT),[114] it cannot apply

[109] *See Bob Jones*, 461 U.S. at 592; *See Goldsboro*, 461 U.S. at 592.

[110] Employment Div., Dep't of Human Resources of Oregon v. Smith, 494 U.S. 872 (1990). The Court has however articulated some exceptions to this general rule including a non facially neutral attempt to regulate religious beliefs, Smith, 494 U.S. at 882, and laws whose specific object is to infringe upon or restrict practices because of their religious motivation must meet strict scrutiny requirements, Lukumi Babalu Aye v. City of Hialeah, 508 U.S. 520 (1993).

[111] Esbeck notes that courts should not make determinations concerning the centrality of the belief or practice in question to an overall religious system. *See* Esbeck, *A Constitutional Case For Governmental Cooperation With Faith-Based Social Service Providers*, 46 EMORY L.J. 1 (1997)(*citing*, *See* Lyng v. Northwest Indian Cemetery Protective Ass'n, 485 U.S. 439, 451 (1988) (rejecting free exercise test that "depends on measuring the effects of a governmental action on a religious objector's spiritual development"); Thomas v. Review Bd., 450 U.S. 707, 715-16 (1981) (holding that it is not within the judicial function or competence to resolve religious differences)).

[112] *Id.* at 1.

[113] *Hsu*, 85 F.3d at 389.

[114] I.R.C. §§ 502, 511-13 (2000).

in these cases. Courts have consistently determined that the organization, once it violates public policy, is no longer a charitable organization. Unlike UBIT cases, no separate, commercial subsidiary is involved. Instead, the group itself is involved in the discriminatory practice.

VII. Conclusion

Religious organizations have provided social benefits including a stabilizing influence on community life.[115] They played central roles in such issues as abolition of slavery, prohibition and civil rights.[116] They have also helped provide food and clothing for the needy, maintained soup kitchen and food pantries, provided shelter to the homeless and counseling to individuals and families.[117] Fundamental moral beliefs of some organizations have come into conflict with the values of greater society. 'Race-mixing' in education was a prime example. Countless other areas of conflict have and will continue to develop including homosexuality, abortion and the morning after pill.[118] There may be some point at which a group's moral beliefs conflict with the majority and their rights of expressive association unlawfully discriminate against a protected class of people. Groups may seek Congressional legislation similar to the Equal Access Act discussed in *Hsu*[119] or legislation granting a "shared religious belief" exemption in instances where that belief system is fundamental to the group's existence. However, such legislation should not encompass discrimination on a basis other than religion. In other instances, the Service may decide to remove federal tax exemption where it is determined that the group's discrimination violates established public policy, despite the fundamental moral belief upon which the discrimination was based.

[115] Waltz v. Tax Comm, 397 U.S. 664 (1970).

[116] *See* Steffen N. Johnson, *Of Politics and Pulpits: A First Amendment Analysis of IRS Restrictions on the Political Activities of Religious Organizations*, 42 B.C. L. REV. 875, 882 (2001).

[117] Cnaan, *supra* note 6, at 50.

[118] *See generally supra* notes 2-4 and accompanying text.

[119] *Hsu*, 85 F.3d at 389; Esbeck, *supra* note 111, at 1.

Legal Concerns Associated with Blogging as a Marketing Tool

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I. Introduction

Web logs or "blogs" are virtual bulletin boards, essentially running online journals on the Internet. A "blogger" establishes the parameters of the blog and then invites and controls postings to create an interactive running discussion on a variety of issues. Popular blogs are known to attract thousands of visitor/contributors each day—enough to also attract marketers to advertise within these forums. Depending on which opinion one accepts, the advent of blogging is anything from the most important communication event since the printing press[1] or just another "turn on the wheel" in communications technology, passé in the next minute.[2] This article examines the legal environment of blogs from a marketing perspective. While much research has examined the growth and creation of blogs,[3] little research has focused on the areas of legal concern and reported decisions that have directly involved bloggers' rights and responsibilities. This paper

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[1] *Blogs Will Change Your Business*, BUSINESS WEEK ONLINE, May 2, 2005 [http://www.businessweek.com/magazine/content/05_18/b3931001_mz001.htm], Accessed 19 July 2006.

[2] Maney, *Once Blogs Change Everything, Fascination With Them Will Chill*, U.S.A. TODAY, May 24, 2005 [http://www.usatoday.com/money/industrytags/techno/maney/2005_05_24_blogs_x.htm], Accessed 19 July 2006.

[3] Bill Comcowichl, *How to Create a Successful Business Blog: 8 Planning Tips*, MARKETINGPROFS.COM, April 4, 2006 [http://www.marketingprofs.com/6/comcowich2.asp], Accessed 17 April 2006; Bill Comcowich, *How to Create a Successful Business Blog: 9 Steps to Implementing*, *MARKETINGPROFS.COM*, April 11, 2006 [http://www.marketingprofs.com/6/ comcowich3.asp], Accessed 17 April 2006; Marqui, *Invisible Marketing: What Every Organization Needs to Know in the Era of Blogs, Social Networks, and Web 2.0*, A Marqui Whitepaper, 2006 [http://www.marqui.com/Solutions/Whitepapers.aspx], Accessed 21 July 2006.

provides such an investigation by addressing jurisdictional issues, intellectual property rights, and employment law concerns. According to recent surveys, 8 million Americans have created their own blogs[4] and traffic to blogs has grown to 58.7 million visitors representing 34% of the total Internet audience[5]. Blog creation is clearly a global phenomenon as well. As of June 2006, the Internet search firm Technorati claims to have indexed 44.1 million blogs worldwide.[6] Blogs are also becoming recognized as a leading source for breaking news and information. Shortly after the first London subway terrorist attack in July 2005, a passenger with a camera cell phone posted to a blog a picture of the smoking damage, effectively beating the networks in reporting the news.[7] Indeed, the United States Supreme Court has even cited a blog as a reliable source of legal information.[8]

II. Expanding the Use of Blogs

Bloggers primarily use this tool for applications such as a) sharing factual information and insights about a focused topic area of interest, b) advocating a position on a social, economic, or political issue, and/or c) promoting the reputation of the blogger or the blogger's business. The first two applications, coined "Amateur Journalism" or "Peer to Peer Journalism," have garnered much attention from the courts and traditional media. From a legal perspective, much of the focus is on First Amendment speech and press rights, as well as the subsequent legal consequences when bloggers exceed those rights. Some bloggers draw criticism for flagrant violations, but many blogs are now routinely cited within print and electronic media as an important source for reliable news and opinions.

[4] Rainie, *Data Memo: The State of Blogging*, Pew/Internet, Pew Internet & American Life Project, Jan. 2005 [http://www.pewinternet.org/pdfs/PIP_blogging_data_pdf], Accessed 19 July 2006.

[5] EMARKETER, *Blogs, Blogs, and More Blogs* (July 18, 2006) [http://www.emarketer.com/Article.aspx?1004072], Accessed 20 July 2006.

[6] About Technorati [http://www.technorati.com/about/], Accessed 16 July 2006.

[7] Porter, *London Bombings: The Unread Newspaper, First Draft by Tim Porter*, July 7, 2005 [http://www.timporter.com/firstdraft/archives/ 000468.html], Accessed 16 July 2006.

[8] U.S. v. Booker, 543 U.S. 220, 125 S.Ct. 738, 160 L.Ed.2d 621, 2005 U.S. Lexis 628, 73 USWL 4056 (2005). Citation to blog made at 543 U.S. 278.

Commercial use of blogs is also growing. Marketers, especially those in high technology businesses, are using blogs for a variety of applications. including integrated marketing communications, search engine marketing, Internet marketing strategy, institutional corporate public relations, product support, company/customer problem solving, product promotion, and tracking consumer opinions of products[9]. The interactivity, humanizing quality, and immediacy are among the noted reasons why marketers use blogs.[10] In light of the Sarbanes-Oxley Act of 2002,[11] which sets new rules for corporate financial disclosure, blogs also allow corporations to quickly disclose events that may have a significant impact on company financial performance.[12] Some technology companies even encourage their individual employees to maintain their own blog in support of a firm's marketing efforts.[13] Other companies have reached out to bloggers as an extended public relations tool. For instance, Wal-Mart has attempted to work directly with bloggers by feeding them exclusive news and information, suggesting topics for postings, and even inviting them to visit its corporate headquarters.[14]

III. BLOGGING LEGAL CONCERNS FOR MARKETERS

As was the case for websites in the late 1990's, blogs are beginning to draw their share of legal scrutiny. While the reported

[9] EMARKETER, *Time to Take Another Look at Business Blogs*, July 14, 2006 [http://www.emarketer.com/Article.aspx?1004062], Accessed 14 July 2006; Joe Laratro, *Blogs ~ Learn How and Why They Fit Into Your Search Engine Marketing & Optimization Campaigns*, A More Visibility Whitepaper, 2005 [http://www.morevisibility.com/whitepaper/2005/Blogs.pdf], Accessed 21 July 2006; Bart A. Lazar, *Marketing Blogs Present New Legal Issues*, MARKETING NEWS, at 6, 6 (2005); Daniel Terdiman, *Why Companies Monitor Blogs*, *CNET News.com*, January 3, 2006 [http://news.com.com/Why+companies+monitor+blogs/2100-1030_3-6006102.html], Accessed 12 May 2006.

[10] Cargill, *The Case for Blogging*, Direct, June 1, 2005 [http://www.directmag.com/mag/marketing_case_blogging/], Accessed 14 July 2005.

[11] P.L. 107-204, 116 Stat. 745 (2002).

[12] Susan Solomon, *Attention, CEOs: It's Time to Blog*, *MARKETING PROFS.COM*, February 1, 2005 [http://www.marketingprofs.com/webnews/5/ news2-1-05.txt], Accessed 1 February 2005.

[13] Mark, *IBM Urges Employees to Blog with Care*, Internetnews.com, May 16, 2005 [http://www.internetnews.com/ent-news/article.php/3505296], Accessed 17 May 2005.

[14] NEW YORK TIMES, *Wal-Mart Working with Bloggers to Create Positive Postings*, March 7, 2006 [http://www.nytimes.com/2006/03/07/technology/ 07blog.html], Accessed 10 March 2006.

decisions are few and principally focused on First Amendment struggles of bloggers, more varied litigation and legal exposure is likely to follow. According to a recent M.I.T survey of bloggers, 36% have experienced legal entanglements of some kind because of information contained within blogs, 12% said they knew other bloggers who had gotten into legal or professional jeopardy, and 66% said they never or almost never ask permission to blog about a person or organization.[15] Because blogs are similar to their more staid cousin, the interactive website, there is good legal reason for treating blogs in the same way. That means the same statutes and court decisions helping or limiting websites by protecting intellectual property, privacy, and reputation and punishing illegal, false, or fraudulent speech may begin to be applied to blogs.[16] Such cases are expected to arise over time.

A. Defamation and Disparagement

Web publishing of an untrue statement of fact that damages an individual or firm's reputation or disparages its products is an actionable intentional tort in courts in the U.S. and worldwide. Online marketers are considered to be "publishers," and web "cyber libel" has presented exposure on a vast scale.[17] Such publishing has led to suits against websites in distant U.S. courts and those in foreign countries as well.[18] Where a civil suit can be properly filed and the defendant case required to defend it is a frequent question in defamation cases.

The majority view in U.S. courts is that website operators must be found to target, and "purposely avail" themselves of the state or country where they are sued before jurisdiction can be asserted over them.[19] Highly interactive e-commerce sites would normally qualify to

[15] Viégas, *Bloggers' Expectations of Privacy and Accountability: An Initial Survey*, 10(3), J. COMPUTER-MEDIATED COMM., Art. 12 (2006) [http://www.jcmc.indiana.edu/vol10/issue3/viegas.html], Accessed 16 July 2006.

[16] Malik, *Are You Content with the Content?, Intellectual Property Implications of Weblog Publishing*, 21, J. MARSHALL COMPUTER & INFO. L. 439 (2003); Rosen, *Watch Your Weblog*, Computerworld, Nov. 1, 2004 [http://www.computerworld.com/softwaretopics/software/groupstory/0,10801,97009], Accessed 28 May 2005.

[17] Michael T. Zugelder & Theresa B. Flaherty, *Legal Issues Associated with Marketing and Webpage Management*, 4 *ATLANTIC L. J.* 31, 31-50 (2001).

[18] Dow Jones & Comp., Inc. v. Gutnick (2002), HCA 56 (December 10, 2002); Yahoo.com.Inc. v. LaLigue Contre Le Rascime et L' Antisemitisme, 169 F.Supp.2d (N.D. Cal. 2001), 198 F.3d 1083 (9th Cir. 2002); Michael T. Zugelder, Theresa B. Flaherty & James P. Johnson, *Legal Issues Associated with International Internet Marketing*, 17 *INTL MARKETING REV.* 253, 253-71 (2000).

[19] Cybersell v. Cybersell, 130 F.3d 414 (9th Cir. 1997); Michael T. Zugelder,

be sued wherever business is targeted or a contract is made.[20] However, access to a website, and for that matter a blog, which is largely a posting place for information and discussion, may not be enough to create jurisdiction.[21] In one of the first reported blogger defamation cases in the U.S. to address jurisdiction, the plaintiff, Software Development and Investment of Nevada, d/b/a Traffic-power, a Nevada-based web marketer, sued a Pennsylvania blogger, Aaron Wall d/b/a/ SEOBook.com, in a Nevada state court, contending his blog published third-party comments that defamed the marketer and compromised trade secrets. Besides offering a forum to comment and criticize web business generators like Traffic-power, Wall also sold books via his blog on web topics—something even U.S. courts can seize upon to find jurisdiction. Still, the Nevada Court dismissed the case for lack of jurisdiction, noting Wall's largely conversational blog neither targeted nor conducted any significant business in the state.[22]

B. Defamation Suits in Foreign Courts

But bloggers may not be so lucky elsewhere in the world. Quite recently, the Indian government shut off access to blogs hosted by many popular American services.[23] Frequently, free speech and promotional rights are more restricted in favor of defamation plaintiffs, as several leading defamation cases filed against U.S. website operators in foreign courts have demonstrated. For example, in Dow Jones & Co. v. Gutnick,[24] a defamation action was brought in Sydney by a local financier. The High Court of Australia allowed the libel suit against Dow Jones to proceed in Victoria, arising from a story posted on the Dow Jones website originating from a Barron's magazine online article published in New York. Applying Australian law and its "place of the injury" rule, the plaintiff's residence and business location, and not the place of the original publication, was determined to be the appropriate location for the suit to proceed.

Theresa B. Flaherty & Irvine Clarke III, *Jurisdictional Issues for Electronic Marketing*," J. INTERNET COMMERCE, at 11,11-26 (2003).

[20] Zippo Mfg. Co. v. Zippo Dot Com, Inc., 952 F.Supp. 1119 (W.D. Pa. 1997).

[21] Bensusan Restaurant Corp. v. King, 126 F.2d 25, 44 U.S.P.Q.2d 1051 (2d Cir. 1997).

[22] Software Development and Investment of Nevada d/b/a Traffic-Power.com v. Wall d/b/a SEObook.com, No. 2:05-CV-01109-RLH-LRL (D. Nev. 2/13/06).

[23] K. Oanh Ha, *Ban of Blogs Stirs Outrage from India to Silicon Valley*, (July 21) [http://www.siliconvalley.com/mld/siliconvalley/15082363.htm], *Mercury News*, July 21, 2006, Accessed 21 July 2006.

[24] *Gutnick, supra* note 18, at n. 11.

Jurisdictional issues become clearer when there is a higher level of interactivity. For instance in *Yahoo.com v. LaLigue Contre Le Rascime et Anti-Semitisme*,[25] a French court ruled that San Diego based Yahoo's portal and interactive auction clearly established jurisdiction in France. The court ordered Yahoo! to block French access to its site or face per diem damages for violating French defamation laws caused by collectors trading Nazi war memorabilia using the Yahoo! auction. The plaintiffs latter attempted to domesticate the French judgment in a San Diego Federal court and began collections proceedings. Though Yahoo! initially succeeded in enjoining the judgment's enforcement on First Amendment grounds (asserting the speech and association rights of the collectors), the Ninth Circuit Court of Appeals vacated the injunction in favor of the French plaintiffs.[26] These jurisdiction-expanding decisions should constitute a serious warning to bloggers that they too may be forced to defend defamation suits in foreign courts applying foreign law.

C. *Protection under the Communication in Decency Act of 1996*

Conversely, it should be expected that blogs sued for defamation in the U.S. will benefit from Internet legislation passed to protect an "interactive computer service", as broadly defined by the Communications Decency Act of 1996 (CDA).[27] Section 230 of the Act provides immunity from defamation suits arising from posted third-party content, even if it remains posted after objection, so long as the website operator did not "contribute" to the content.[28] Courts have generally held that editing or partial deletions do not constitute such contribution that would defeat the immunity.[29] In fact, the courts' application has been even broader than Congress had perhaps intended, by providing immunity for posted defamation on intranet employer e-mail sites, listservs, and a wide variety of interactive commercial and noncommercial websites.

It is quite possible that the courts may extend the CDA's protections to blogs. The Ninth Circuit affirmed something close to that very result in the *Batzell v. Smith* case involving listservs in 2003.[30] Robert Smith was a handyman working in the home of attorney Ellen

[25] *Yahoo.com., supra* note 18, at 11.

[26] *Id.*

[27] 47 U.S.C. § 230 (1996); Daniel Lyons, *Attack of the Blogs*, FORBES, (November 14, 2005), 128-38; *Yahoo.com., supra*, at 9.

[28] 47 U.S.C. § 230(c)(1) (Supp. 4. 1999).

[29] Blumenthal v. Drudge, 992 F.Supp. 44 (D.D.C. 1998); McManus, *Rethinking Defamation Liability for Internet Service*, 35 SUFFOLK U. L. REV. 647 (2001).

[30] Batzell v. Smith, 333 F.3d 1018 (9th Cir. 2003).

Batzell when he noticed paintings believed to be looted by the Nazi's during World War II. Smith e-mailed his opinion to Tom Cremers, who operated a listserv called the Museum Security Network (MSN), which works with museums and authorities to identify and return such stolen works. Cremers posted the e-mail with some minor edits. The pictures were not stolen Nazi loot, and when Batzell saw the posting she sued Smith, Cremers, and MSN and won in trial court. On appeal, the Ninth Circuit reversed as to Cremers and his listserv MSN.[31] The decision has been widely hailed by bloggers for its broad holding: "[A] service provider or user is immune from liability under Section 230(c)(1) when a third person or entity that created or developed the information in question furnished it to the provider or user under circumstances in which a reasonable person in the position of the service provider would conclude that the information was provided for publication on the Internet or other interactive computer service."[32] To many legal and marketing commentators, this means bloggers too would be immune under the *Batzell* decision, so long as they have reason to believe that the content they received, though defamatory, was intended for posting.[33]

This ruling was applied in another Ninth Circuit case following *Batzell*. In *Carafano v. Metrosplash*,[34] CDA immunity was given to a commercial dating service from a defamation suit brought by an actress, Carafano, arising from a third-party posting. The service, Matchmaker.com, allowed users to post personal profiles, and a user posted a fraudulent and provocative profile of the plaintiff. Taken together, these and other cases are establishing a broad general rule of no defamation liability for publishing third-party content on the Internet per section 230. These rulings should directly benefit blogs which, by their nature, often accept multiple postings by third parties. Other commentators, however, are quick to note that the CDA provides no clear protection for blogger-originated content and that the cases are still not unanimous in granting immunity, where the service provider edits or otherwise manipulates the third party content.[35] Even if the company blog is deemed an ISP for liability purposes, the company blog that allows third-party comments to be posted anonymously can still face

[31] *Id.*

[32] *Id.* at p. 1035.

[33] *Court Decision Protects Bloggers from Libel Lawsuits*, USA Today.com, July 2, 2003 [http://www.usatoday.com/tech/news/techpolicy/2003-07-02-blogger-libel_x.htm], Accessed 2 July 2003.

[34] Catafano v. Metro Splash, 339 F.2d 1119 (9th Cir. 2003).

[35] J. H. Lee, *Batzel v. Smith & Barrett v. Rosenthal: Defamation Liability for Third-Party Content on the Internet*, 19 BERKELEY TECH. L. J. 469 (2004).

litigation demanding disclosure of records and information to identify the "Doe" anonymous sources.[36]

III. INTELLECTUAL PROPERTY LOSS AND INFRINGEMENT

Online marketers need to understand that the very nature of their blogging operation can cause an even greater exposure to violation of the intellectual property rights of others though the content input from others. Though there are only a few reported decisions at this time, it is clear that the application of intellectual property law to website marketers is slowly being applied to blogs. The three main areas of interest are trademark, copyright, and trade secrets.

A. Trademark

A trademark or service mark is any symbol used to identify a good or service and its source to the buying public.[37] A recent search of the U.S. Patent and Trademark office website shows 96 service marks awarded to firms and individuals that use the term "blog" as part of their distinguishing mark. A cursory review of the trademark holders show them largely to be web software and web service firms, many operating a blog.[38]

Because trademark infringement has become the leading cause of web litigation, bloggers who, without permission, intentionally or carelessly use the trademarks of others as their own domain name or on their blog should expect the same kind of legal issues associated with websites.[39] Bloggers likewise should avoid the known dangerous practices of unauthorized deep linking into another's website.[40] They should also avoid the use of metatags embedded with another's trademark to drive search engines to their blog.[41] Framing, the practice

[36] S. Wilson, *Corporate Criticism on the Internet: The Fine Line Between Anonymous Speech and Cybersmear*, 29 PEPP. L. REV. 533 (2002); Michael Vogel, *Unmasking 'John Doe' Defendants: The Case Against Excessive Hand Wringing Over Legal Standards*, 83 OR. L. REV. 395 (2004).

[37] 15 U.S.C. § 1127 (2006).

[38] Website of the United States Patent and Trademark Office [http://www.uspto.gov/], Accessed 19 July 2006.

[39] *Id.* at n. 17.

[40] Ticketmaster Corp. v. Microsoft Corp., No. 2:97-CV-03055 (C.D. Cal. 1997).

[41] Playboy Enterprises, Inc. v. Calvin Designer Label, 985 F.Supp. 1220 (N.D. Cal. 1997).

of transferring whole blocks of creative content from another site into your own, should be avoided as well.[42] These actions could have very undesirable results for blogs. Conversely, blogs that use another's trademark in the context of a discussion of ideas, commentary, and/or criticism will probably be able to enjoy a broader trademark "fair use" defense for parody and comment than websites have experienced so far. For instance, in Jews for Jesus v. Google,[43] Google was accused by the religious group of allowing a hosted blogger on Google's *Blogspot* to infringe by using the group's name as a URL, http://jewsforjesus.blogspot.com. In this pending New York case, the plaintiffs asserted the possibility of confusion and damage to its trademark and are seeking an injunction and damages. The blogger has argued fair use and the right to comment on religious issues.

B. Copyright

The exclusive rights of the owners for their creative works are protected by copyright law. Copyright protection now applies to the Internet in most of the industrial nations through several treaties like the Berne Convention.[44] In the U.S., Congress' 1998 passage of the Digital Millennium Copyright Act (DMCA)[45] made it emphatic that the full force of copyright applies to Internet users and marketing websites. U.S. courts have generally enforced the copyright law in favor of the copyright owner against de-encryption and music file sharing software providers and networks, and against online marketers as well.

Because creative expressions on blogs are clearly within the scope of copyright protection, use of copyright registration to protect creative aspects of the blog should considered just as website marketers have done. Similarly, bloggers will be answerable for infringement challenges. Two recent challenges have been made against blogs that involve the DMCA's "safe harbor" for ISP's and other interactive service providers.[46] The DMCA safe harbor provides immunity for copyright infringement arising by third-party postings. But unlike the safe harbor immunity provision of the CDA, the DMCA safe harbor

[42] Washington Post Co. v. Total News, Inc., Case No. 97 (S.D. N.Y. 1997).

[43] Jews for Jesus v. Google, Inc., 05-CU-10684 (S.D. N.Y. Dec. 21, 2005).

[44] Berne Convention [http://www.wipo.int/clean/docs/eu/wo/wo 001en.htm], Accessed 18 July 2006.

[45] DMCA, Pub. L. No. 105-304, 112 Stat. 2860 (Oct. 28, 1998), 17 U.S.C. § 512, *et seq.*, amending 17 U.S.C. § 101-810 (2006).

[46] 17 U.S.C. § 512(a)-(n).

requires the service provider to delete the infringing material after appropriate notice by the copyright owner.

In 2003, Diebold, maker of electronic voting machines, sent DMCA cease- and-desist letters to two blogging Swarthmore College students and an online newspaper. Diebold demanded that these parties remove posted internal Diebold e-mail that contained descriptions of copyrighted source codes and acknowledged problems with its voting machines. The Electronic Frontier Foundation, a non-profit Internet free speech group, joined in and filed suit on behalf of the students and the newspaper, seeking both a dismissal of Diebold's suit and a declaratory judgment that the postings were part of protected First Amendment speech rights of free comment and criticism.[47] Diebold settled the matter, stating that the information they sought to protect was already too widespread to justify further litigation expense. Bloggers proudly point to the settlement's requirement that Diebold sent bloggers individual retractions of previous cease-and-desist letters. On the other hand, Jason Kottke, a well known blogger, posted a video clip he received showing the surprise defeat of the famous Jeopardy champion, Ken Jennings, one day before the show was to air. Attorneys from Sony Pictures contacted Kottke and demanded he remove the copyright protected clip from his blog, which he ultimately did.[48]

Regardless of the outcome of these initial matters, they show a readiness to use copyright to restrict bloggers who allow postings of copyrighted or other restricted material without permission. And though the safe harbor is being applied to blogs, it must be understood that it will not provide complete immunity for infringements originated by the blogger.

C. Trade Secrets

Many online marketers have turned to trade secrets in lieu of patents as a means to protect proprietary information and ways to conduct online business.[49] Trade secrets require no registration and can

[47] Online Policy Group, *Nelson Chu Pavlosky and Luke Thomas Smith v. Diebold, Inc. and Diebold Election Systems, Inc.*, Case. No. C 03-04913-JF (N.D. Cal. Sept. 30, 2004).

[48] William Smith, *In House Counsel, Fighting Intellectual Property Theft*, Vol. 27, No. 40, NAT'L L. J., at 8, June 13, 2005. For additional inquiry, see the synopsis of events as related by Kottke and other bloggers at Kottke's web log [kottke.org/04/12/sony-ken-jennings-and-me], Accessed 17 July 2006.

[49] Michael T. Zugelder, *Trade Secrets and the Internet: A Legal Review and Management Considerations*, 18 MIDWEST L. REV. 79 (2002); L. BURGUNDER, *LEGAL ASPECTS OF MARKETING TECHNOLOGY*, Ch. 4, pp. 193-96 (2d ed. 2001).

last as a protected property interest indefinitely up until they are lost to the public through carelessness, failures in security, or intentional misconduct by competitors or departing employees.[50] Loss without legal recourse can occur especially when trade secrets make their way onto the Internet, as was the case of Religious Technology Center v. Netcom On-Line Communications Services Inc.,[51] where a disgruntled employee placed secrets of the Church of Scientology on a listserv which sent them to websites that broadly disseminated them before suit was brought. In Ford Motor Co. v. Lane,[52] First Amendment rights provided website operator Lane with a shield for trade secret misappropriation liability when unidentified Ford Motor employees forwarded company secrets he posted to his website which commented on and criticized Ford's safety record.

However, this not always the case, and courts have come down on the side of the trade secret owner against websites and bloggers alike who post secrets obtained from third parties. Such was the result in several federal court actions filed by Apple Computer in the winter of 2004 to force bloggers to take down trade secrets and obtain the names of 25 unidentified "John Doe" employees who forwarded them for posting. In one of the cases, Apple Computers Inc. v. Doe 1,[53] the trial court held the postings violated Apple's rights under California's Trade Secret Act and that the bloggers had to disclose the employees' identities. The Court specifically found that neither the First Amendment nor California's Shield Law protecting professional journalists' confidential sources could be used by web sites or bloggers as a basis to refuse disclosure. These cases underscore the potential for litigation and liability for bloggers and others who post the trade secrets of others.

IV. EMPLOYEE'S PERSONAL BLOGS

In light of the legal concerns and loss of company control posed by blogs, employee blogging presents new employee relations

[50] Victoria Cundiff, *Trade Secrets and the Internet: A Practical Perspective*, 14 No. 8, COMPUTER L. 6 (1997).

[51] Religious Technology Center v. Netcom On-Line Communications Services, Inc., 923 F.Supp. 1231 (N.D. Cal. 1995).

[52] Ford Motor Co. v. Lane, 67 F.Supp.2d 745 (E.D. Mich. 1999).

[53] Apple Computers, Inc. v. Doe, No. 1-04-CV-032178, 2005 WL 578641 (Cal. Sup. Ct. Mar. 11, 2005).

challenges to many organizations.[54] Most companies have concern regarding damage by employees posting negative or confidential information about the company.[55] As such, employers must clearly delineate between acceptable and unacceptable content on blogs.[56] Firms have taken varied approaches to employee blogging and range from cautious tolerance to that of encouraging employees to blog. High tech companies in the software and hardware industry are more apt to see the marketing advantages and encourage employees to maintain blogs. For example, Microsoft has nearly 2,000 employee bloggers on company-hosted blog sites.[57] Sun Microsystems has likewise established a publicly accessible site with 1,300 employee maintained blogs.[58]

While there have been 11 reported employee terminations for blog-related activities in 2005, the number is bound to grow due to the blogging explosion and the prevailing "employment at will" doctrine in the U.S. private sector that allows employers to terminate employees for nearly any reason. Perhaps the most famous case to date was Delta Flight attendant Ellen Simonetti,[59] fired by the airline after she posted photos of her posing in a Delta plane in her fight attendant's uniform. She later filed suit for sex discrimination, claiming Delta did not fire male employees for similar offenses.[60] Simonetti now maintains a blog called "Diary of a Fired Flight Attendant"[61] and is about to publish a book about her experience. More common termination cases involve

[54] *EMARKETER, Business Blogging Still Bogged Down*, July 7, 2006 [http://www.emarketer.com/Article.aspx?1004049], Accessed 7 July 2006; Meryl K. Evans & Hank Stroll, *Marketing Challenge: When It's Best NOT to Blog*, MARKETINGPROFS.COM, Jan. 17, 2006.[http://www.marketingprofs.com/6/stroll102.asp?f=evrl], Accessed 17 January 2006.

[55] Amy Rosewater, *Dear Blog: Wow, the Boss Sure is Mad*, THE VIRGINIAN-PILOT, Jan. 8, 2006, at D6.

[56] Flahardy, Cathleen, *Employees Fired Over Personal Blog Fight Back — Companies Implement Blogging Policies to Avoid Legal Pitfalls*, CORP. LEGAL TIMES, May 5, 2005, 26.

[57] *Id.* at n.55.

[58] Benjamin Pimentel, *Writing the Codes on Blogs — Companies Figure Out What's OK, What's Not, in Online Realm*, SAN FRANCISCO CHRONICLE, June 13, 2005 [http://www.sfgate.com/cgi-bin/article.cgi?file=/chronicle/archive/2005/06/13BU6OMD64], Accessed 19 July 2006.

[59] Jo Twist, *Blogger Grounded by Her Airline*, BBC News, 3 Nov. 2004 [http://www.news.bbc.co.uk/1/hi/technology/3974081.stm], Accessed 19 July 2006.

[60] Simonetti v. Delta Air Lines, Inc., Case No. 1:05-CU-2321 (N.D. Ga. Sept. 7, 2005).

[61] *"Queen of the Sky" Announces Upcoming Release of her Blog-Based Book*, press release, Feb. 15, 2005 [http://www.prweb.com/releases/2006/2/ prweb346908.htm], Accessed 19 July 2006.

employees who comment on activities at work, such as former Google programmer Mark Jen, who was fired for posting stories he wrote about his life at the company. While he believed such stories would be interesting to the public, Google thought otherwise.[62] Employees maintaining a blog about company must clearly understand what information can and cannot be included in the blog.[63]

V. CONCLUSION

This article examined the marketing and business environment of blogs in order to provide a descriptive analysis of legal concern. For companies and individuals involved with blogs, there are various rights and responsibilities associated with defamation and jurisdictional issues, intellectual property rights, and employment law concerns. Concluding comments about each of these main areas is provided below.

Blogs that contain damaging false statements will continue to be challenged in courts. While U.S. cases extend free speech protection to blogger criticism and opinion and even CDA immunity from liability for third-party posts that defame an individual or disparage a firm or product, courts elsewhere may not agree. Even in the U.S., bloggers can face liability for their own defamatory comments. Care therefore must be taken. Bloggers should avoid any false statements and disclaim affiliation with and responsibility for third-party comments. A policy of filtering should be also considered. Bloggers should never target their blog to a jurisdiction unless they are ready for the possible consequences.

To avoid problems associated with intellectual property loss, there are several steps that marketing bloggers should take. First, protect the blog's branding slogans, brand marks, and/or logos with trademark registration. Second, creative expressions and layout of blog designs should be protected with appropriate copyright registration. Finally, infringement is another serious concern. Bloggers should refrain from using or allowing others to post valuable trademarks, copyright-protected materials, or trade secrets without the owner's

[62] Anick Jesdanun, *Most Companies Lack Policies for Governing Employee Blogs*, THE VIRGINIAN-PILOT, March 7, 2005, A1.

[63] Bart A. Lazar, *Marketing Blogs Present New Legal Issues*, MARKETING NEWS, at 6, 6 (2005); Daniel Terdiman, *Why Companies Monitor Blogs*, *CNET NEWS.COM*, Jan. 3, 2006.

permission because the same legal scrutiny and liability imposed on web sites is beginning to be imposed on blogs.

Blogging is now creating a number of employment law concerns. In addressing these issues, it is worth noting that company employee blogging policies vary from the general, sometimes as a part of an electronic communications policy, to separate and more specific guidelines. IBM, a firm that has long encouraged employees to utilize the Internet, has a separate policy with extensive guidelines and an 11-point executive summary.[64] Sun Microsystem's extensive policy[65] emphasizes that ". . . it's all about judgment" and asks employees not to tell lies or embarrass the company. Most policies stress employees' personal responsibility, honesty, and loyalty to the firm and its products. They often warn employee bloggers to respect copyright laws as well as confidential and proprietary information. However versed, a policy is a must for firms that know its employees are blogging and especially for firms that encourage employee blogs.

[64] IBM Blogging Policy and Guidelines, (2005), [http://www.snellspace.com/IBM_Blogging_Policy_and_Guidelines.pdf], Accessed July 18, 2006.

[65] SUN NEWS (2006), Sun Blogs, [http://www.sun.com/aboutsun/media/blogs/policy.html], Accessed 19 July 2006.

I.R.C. § 179, Hybrid Cars & Sport Utility Vehicles: The Counterproductive Income Tax Treatment of Certain Vehicles under the Internal Revenue Code and a Proposed Solution

Brian J. Halsey*

I. Introduction

This is an era of great change in the automobile industry. It is also an era characterized by a sort of schizophrenia. The most popular class of vehicle on the market in the United States in 2002 was the sport utility vehicle ("SUV").[1] At the same time, there has been growth at the opposite end of the market, where small cars with the first viable alternative propulsion systems to the traditional internal combustion engine in a century are coming to market.[2]

The Internal Revenue Code, in its current form and under some proposals that are due before the Congress, treats each class of vehicle very differently for income tax purposes.[3] SUVs are strongly favored under the tax code, especially under Section 179. The new alternative powered automobiles ("Hybrids"), despite limited government support of the basic concept,[4] are given a much harsher tax treatment. This disparity works to the determent of: businesses on an individual level; national security; the environment; and the long term competitiveness of the American automobile industry.

This article begins with a review of the basic technology available today. It then reviews the current tax treatment of SUV's and Hybrids. Next, it examines the consequences of the current proposed and existing tax policies, and lastly the article presents a proposed

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[1] *Storm Clouds over Detroit*, THE ECONOMIST, Nov. 16, 2002, at 55.

[2] *See,* Bob Gritzinger, *GM Announces Hybrid Future,* AUTOWEEK, Jan.13, 2003, at 4; Chester Dawson, *Fuel Cells: Japan's Carmakers Are Flooring It,* BUS. WK., 12/23/2002, at 50; Hakim, Danny, *Automakers Look Beyond Electric.*, N.Y. TIMES, Sept. 22, 2002, at 12-1.

[3] *See,* I.R.C. § 179 and I.R.C. § 179A.

[4] *See,* I.R.C. § 179A. *See generally,* Harry Stoffer, *Unmoved by hydrogen, critics seek higher CAFE,* AUTOMOTIVE NEWS, Jan. 21, 2002, at 3; Jon Lowell, *Supercar to identify research priorities*, WARD'S AUTO WORLD, Feb. 1994, at 33; Bob Davis, *SUVs May Be Added to Supercar Project*, WALL ST. J., May 5, 1999, at B4; Harry Stoffer, Despite *PNGV's efforts, Ford outsources to Japan*, AUTOMOTIVE NEWS, Aug. 20, 2001, at 1.

solution that could result in palpable benefits for business and the society as a whole.

II. The Vehicles and Technology

A, Sport Utility Vehicles

The SUV is the current superstar of the automotive world. The SUV's popularity is evidenced by soaring sales,[5] massive increases in market share vis-à-vis automobiles,[6] and near total saturation of the market.[7] The SUV is essentially a light truck that has passenger car attributes, so although it is sold and perceived as an automobile replacement, it is governed by the federal government's truck standards for safety, emissions and CAFÉ fuel economy standards.[8]

The technologies utilized by SUV are, to date, standard systems that offer no great innovations in either safety[9] or, for our purposes here, fuel economy. The vehicles use large versions of the internal combustion engines that have powered the automobile industry for better than a century.[10]

Sport utility vehicles are generally larger, have bigger engines and are far less aerodynamic than traditional automobiles. As a consequence, virtually all of these vehicles have greater fuel

[5] Lora J. Bingham, *Compact Market Continues Growth*, AUTOMOTIVE INDUSTRIES, October 2001, at 39.

[6] *See* Kathleen Kerwin, *Autos.*, BUS. WK., Jan. 10, 2000, at 118.

[7] Mark Dolliver, *It couldn't happen to a nicer category*, ADWEEK, Jan. 17, 2000, at 37; Matt Nauman, *SUV Sales Continued to Grow in California Last Year*, SAN JOSE MERCURY NEWS, Feb. 7, 2003.

[8] 49 CFR § 533.5; *See* Proposed Rules Department Of Transportation, National Highway Traffic Safety Administration (NHTSA) 49 CFR Part 533, Light Truck Average Fuel Economy Standards Model Years 2005-07 Monday, Dec. 16, 2002, 67 FR 77015-01, 2002 WL 31784922 (F.R.); *see also* 49 U.S.C. 32904(a)(2); *see generally New Suv Mileage Ratings Discourage Fuel Efficiency*, NEWS & RECORD (Greensboro, NC), Dec. 16, 2002.

[9] *See* Cindy Skrzycki, *Regulator Assails Safety Of SUVs; Blunt Talk Is Unusual In Runge's Position*, THE WASHINGTON POST, Jan. 16, 2003, at E01; *See* Terril Yue Jones, *U.S., Foreign Automakers Agree to Improve SUV Safety Standards Los Angeles Times*, February 14, 2003 at 32; For an interesting overview of the innovation staking place in small car design, *see Product Design & Development*, Jan. 2003, Vol. 58, No. 1 at pg. 36.

[10] *See The next Apollo mission?*, THE ECONOMIST, Feb. 1, 2003; *See also* Woodrow W. Clark & Emilio Paolucci, *Commercial development of environmental technologies for the automotive industry towards a new model of technological innovation*; INT'L J. ENTL .TECH. AND MGMT., 2001, at 363, 363-383.

requirements than automobiles[11], greater emission of wastes, and in many ways pose a greater threat on the road than their smaller cousins.[12] For instance, the 2003 Dodge Durango weighs 6400 pounds and returns between 12 and 17 miles per gallon.[13] The 2003 Ford Expedition weighs 7,300 pounds and returns 14 miles per gallon.[14] The 2003 Hummer H2 weighs 8600 pounds and has its fuel economy listed as "[o]ut of regulated fleet requirements".[15] None of these vehicles are certified as clean burning.

Because these vehicles are perceived as automobile replacements, they take the place of a smaller, more traditional automobile in many households. That behavior, multiplied over millions of households and many years, gives the SUV a profound impact on the society as a whole.

B. Hybrid Cars

The opposite end of the automobile spectrum from the SUV is occupied by the hybrids. After years of failed U.S. government-industry cooperation in an attempt to develop a hybrid vehicle that could maintain 80 miles per gallon,[16] several companies that have worked outside of the government sponsored programs have brought viable and attractive hybrid vehicles to the American market.[17]

> Automakers have finally combined the best of two cars-the electric and the gasoline powered-into one fuel-efficient hybrid. The Honda Insight and the Toyota Prius . . ., which arrived in U.S. showrooms in 1999 and 2000, respectively, rely primarily on gasoline, switching to electricity under light loads, or use both types of energy simultaneously when the

[11] *See also* Bart Jansen, *Maine's Senators Renew Push for Better SUV Mileage*, Portland Press Herald, Jan. 31, 2003.

[12] *See* Transcript Frontline, *Rollover: The Hidden History of the SUV* Program #2013, Original airdate: Feb. 21, 2002.

[13] Edmunds.com; 2003 Dodge Durango Specifications http://edmund.com/new/2003/dodge/durango/100169637/specs.html?tid=edmunds.n.prices.leftsidenav..9.Dodge* (visited Mar. 5, 2003)

[14] *Ford Truck Enthusiasts* 2003 Ford Expedition Technical Specifications http://www.ford-trucks.com/specs/2003/2003_expedition_1.html (visited Mar. 5, 2003)

[15] 2003 HUMMER H2 SPECIFICATIONS http://media.gm.com/division/hummer/products/03_HUMMER_H2/specifications.html (visited on March 5, 2003).

[16] Mark Schrope, *New-Generation Cars Become Old Hat As US Changes Course*, NATURE, Jan. 17, 2002, at 248.

[17] Danny Hakim, *The Hybrid Car Moves Beyond Curiosity Stage*, N. Y. TIMES, Jan. 28, 2003, at A1.

> vehicle needs a boost of power. Sensors placed throughout the car monitor conditions such as throttle position, vehicle speed, and battery charge, and relay the readings to a computer that decides how to optimally divide the load between the gasoline engine and electric motor.[18]

Hybrids provide several benefits as opposed to the ubiquitous SUV. First, the fuel mileage achieved by these types of vehicles is far greater than SUV's (the three models available to the general market as of this writing, the Honda Civic and Insight, and the Toyota Prius, all achieve greater than 40 miles per gallon on the EPA highway cycle). Second, these vehicles are all certified low emissions vehicles, unlike virtually all SUV's. Third, hybrids are, at present, far more compatible from a safety standpoint with other vehicles on the road. Fourth, although all hybrid vehicles are today small cars, the technology is easily transferable to any vehicle type – large car, minivan, pickup truck, or even SUV (indeed, some manufacturers have such plans today).

III. Current Tax Treatment of SUV's and Hybrids

A. I.R.C. § 179

The normal depreciation schedules under the Internal Revenue Code are well known.

1. The Present Law

Equally well known amongst the business community is the Section 179 accelerated deduction.[19]

> Section 162 of the Internal Revenue Code ("Code" or "I.R.C.") allows a deduction for the ordinary and necessary business expenses incurred in carrying on a trade or business. In contrast, section 263 of the Code allows no deduction for a capital expenditure. "The primary effect of characterizing a payment as either a business expense or a capital expenditure concerns the timing of the taxpayer's cost recovery: While business expenses are currently deductible, a capital expenditure usually is amortized and depreciated over the relevant life of the asset." *INDOPCO, Inc. v.*

[18] Tracy Staedter, *Hybrid Cars*, TECH. REVIEW, Nov. 2002.
[19] I.R.C. §179.

> *Commissioner*, 503 U.S. 79, 83- 84, 112 S.Ct. 1039, 117 L.Ed.2d 226(1992). Under section 179 of the Code, however, a taxpayer may elect (subject to certain limitations) to treat the cost of any "section 179 property" as a current expense in the year such property is placed in service, rather than depreciating the cost of the property over a number of years.[20]

Section 179 property is "[a]ny tangible property (to which section 168 applies) which is Section 1245 property (as defined in section 1245(a)(3))[21] and which is acquired by purchase for use in the active

[20] *Hayden v. C.I.R.*, 204 F.3d 772, 773 (C.A.7, 2000). The Section 179 deduction provides that:

> (a) Treatment as expenses.--A taxpayer may elect to treat the cost of any section 179 property as an expense which is not chargeable to capital account. Any cost so treated shall be allowed as a deduction for the taxable year in which the section 179 property is placed in service.

[21] I.R.C. § 1245(a)(3) provides: "Section 1245 property.--For purposes of this section, the term "section 1245 property" means any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either--

> (A) personal property,
>
> (B) other property (not including a building or its structural components) but only if such other property is tangible and has an adjusted basis in which there are reflected adjustments described in paragraph (2) for a period in which such property (or other property)--
>
> (i) was used as an integral part of manufacturing, production, or extraction or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services,
>
> (ii) constituted a research facility used in connection with any of the activities referred to in clause (i), or
>
> (iii) constituted a facility used in connection with any of the activities referred to in clause (i) for the bulk storage of fungible commodities (including commodities in a liquid or gaseous state),
>
> (C) so much of any real property (other than any property described in subparagraph (B)) which has an adjusted basis in which there are reflected adjustments for amortization under section 169, 179, 179A, 185, 188 (as in effect before its repeal by the Revenue Reconciliation Act of 1990), 190, 193, or 194
>
> (D) a single purpose agricultural or horticultural structure (as defined in section 168(i)(13)),

conduct of a trade or business."[22] Section 168 provides the general rules for depreciation. [23]

The beauty of the Section 179 expense allowance is that it allows business owners to expense against income the cost of qualifying property, instead of capitalizing that property and spreading the resulting deduction over several years. Therefore, it is in the owner's interest to classify as much acquired property under Section 179 as possible in order to gain the present deduction.

There are limitations to the usefulness of Section 179. For instance, there are dollar limitations ($25,000 in 2003) on the amount that may be taken as a present expense deduction under Section 179.[24] In addition, the deduction "[s]hall not exceed the aggregate amount of taxable income of the taxpayer for such taxable year which is derived from the active conduct by the taxpayer of any trade or business during such taxable year."[25]

Mitigating some of these limits are short term additional deductions that were passed after the terrorist attacks on September 11, 2001 and that were intended to add an additional economic boost to the nation's economy in the economically turbulent period that was intensified by those attacks.[26] For instance, there is a provision that

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(E) a storage facility (not including a building or its structural components) used in connection with the distribution of petroleum or any primary product of petroleum, or

(F) any railroad grading or tunnel bore (as defined in section 168(e)(4))."

I.R.C. § 1245(a)(3).

[22] I.R.C. § 179(d)(1).

[23] I.R.C. § 168.

[24] I.R.C. § 179(b)(2) provides as follows:

"(b)Limitations.--

(1) Dollar limitation.--The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

If the taxable year Begins in:	The applicable amount is:
1997	18,000
1998	18,500
1999	19,000
2000	20,000
2001 or 2002	24,000
2003 or thereafter	25,000.

[25] I.R.C. §179 (3)(A).

[26] *See* I.R.C. § 198(k).

now permits a new additional first-year depreciation deduction.[27] This provision provides an "[a]dditional 'bonus' depreciation allowance of

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[27] See Joint Committee on Taxation, *Technical Explanation of the "Job Creation and Worker Assistance Act of 2002"* (JCX-12-02), March 6, 2002. The relevant text of the Joint Committee's technical explanation is as follows:

"The provision allows an additional first-year depreciation deduction equal to 30 percent of the adjusted basis of qualified property. The additional first-year depreciation deduction is allowed for both regular tax and alternative minimum tax purposes for the taxable year in which the property is placed in service. The basis of the property and the depreciation allowances in the year of purchase and later years are appropriately adjusted to reflect the additional first-year depreciation deduction. In addition, the provision provides that there would be no adjustment to the allowable amount of depreciation for purposes of computing a taxpayer's alternative minimum taxable income with respect to property to which the provision applies. A taxpayer is allowed to elect out of the additional first-year depreciation for any class of property for any taxable year. In order for property to qualify for the additional first-year depreciation deduction it must meet all of the following requirements. First, the property must be property to which the general rules of MACRS apply with (1) an applicable recovery period of 20 years or less, (2) water utility property (as defined in section 168(e)(5)), (3) computer software other than computer software covered by section 197, or (4) qualified leasehold improvement property. Second, the original use of the property must commence with the taxpayer on or after September 11, 2001. Third, the taxpayer must purchase the property within the applicable time period. Finally, the property must be placed in service before January 1, 2005. An extension of the place in service date of one year (i.e., January 1, 2006) is provided for certain property with a recovery period of ten years or longer and certain transportation property. Transportation property is defined as tangible personal property used in the trade or business of transporting persons or property. The applicable time period for acquired property is (1) after September 10, 2001 and before September 11, 2004, and no binding written contract for the acquisition is in effect before September 11, 2001 or (2) pursuant to a binding written contract which was entered into after September 10, 2001, and before September 11, 2004. With respect to property that is manufactured, constructed, or produced by the taxpayer for use by the taxpayer, the taxpayer must begin the manufacture, construction, or production of the property after September 10, 2001, and before September 11, 2004. Property that is manufactured, constructed, or produced for the taxpayer by another person under a contract that is entered into prior to the manufacture, construction, or production of the property is considered to be manufactured, constructed, or produced by the taxpayer. For property eligible for the extended placed in service date, a special rule limits the amount of costs eligible for the additional first year depreciation. With respect to such property, only the portion of the basis that is properly

30% of the adjusted basis of qualified property, for the year in which the property is placed in service. This 30% is in addition to the usual annual depreciation allowance that applies to the remaining 70% of the property's adjusted basis . . . ."[28]

2. Proposed Changes to the Present Law

The Bush Administration has recently proposed to raise the current $25,000 annual limitation under section 179 to $75,000. The proposal is explained well in the *General Explanations of the Administration's Fiscal Year 2004 Revenue Proposals* published by the Department of the Treasury in February 2003. Because of the brevity of the relevant section of this report it is reproduced here in its entirety:

INCREASE EXPENSING FOR SMALL BUSINESS

Current Law

Section 179 provides that, in place of depreciation, certain taxpayers may elect to deduct up to $25,000 of the cost of qualifying property placed in service each year. In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. Off-the-shelf computer software generally does not qualify for the Section 179 deduction because it is intangible property. The $25,000 amount is reduced (but not below zero) by the amount by which the cost of qualifying property exceeds $200,000. More generous incentives are provided for investment in the New York Liberty Zone or in an empowerment zone or renewal community. An election for the Section 179 deduction must generally

attributable to the costs incurred before September 11, 2004 ("progress expenditures") shall be eligible for the additional first year depreciation. The limitation on the amount of depreciation deductions allowed with respect to certain passenger automobiles (sec. 280F of the Code) is increased in the first year by $4,600 for automobiles that qualify (and do not elect out of the increased first year deduction). The $4,600 increase is not indexed for inflation ... [and] the provision applies to property placed in service after September 10, 2001 (footnotes omitted)."

Id. at 2.

[28]Smith, Annette B., *Depreciation*. Tax Adviser, July 2002 at 426.

be made on the taxpayer's initial tax return to which the election applies. The election can be revoked only with the consent of the Commissioner.

Reasons for Change

Expensing encourages investment by lowering the after-tax cost of capital purchases, relative to claiming regular depreciation deductions. Expensing is also simpler than claiming regular depreciation deductions, which is particularly helpful for small businesses. Raising the amount of total investment at which the phase-out begins would increase the number of taxpayers eligible for Section 179 expensing.

The exclusion of off-the-shelf computer software from Section 179 is confusing to many taxpayers and puts purchased software at a disadvantage relative to developed software (for which development costs can generally be expensed as incurred).

Small business taxpayers may not always be aware of the advantages or disadvantages of Section 179 expensing. For example, a taxpayer may want to make an election on an amended return if the taxpayer was not aware of the Section 179 election or if changes on an amended return make the taxpayer eligible for the election. Alternatively, a taxpayer may want to revoke a previous Section 179 election if the taxpayer determines that it was not to the taxpayer's advantage. However, a taxpayer is precluded from revoking a Section 179 election on an amended return without incurring the expense and uncertainty of requesting the consent of the Commissioner.

Proposal

The proposal would increase the maximum amount of qualified property that a taxpayer may deduct under Section 179 to $75,000. The proposal would raise the amount of total qualifying investment at

> which the phase-out begins to $325,000 per year and include off-the-shelf computer software as qualifying property. Both the deduction limit and phase-out threshold would be indexed annually for inflation. Additionally, the Administration proposes to allow expensing elections to be made or revoked on amended returns.
>
> The proposal would be effective for taxable years beginning on or after January 1, 2003.[29]

While this proposal is innocuous on its face and may even be laudable in some respects, the ancillary and probably unintended effects of increasing the §179 deduction to $75,000 could be profound.[30] To understand the implications, this article will next discuss the basic depreciation rules for automobiles, and then the tax rules regarding SUV's.

3. Depreciation of Automobiles in General

There are other restrictions on deductions that affect businesses. One of the most widely applicable relates to the tax treatment of automobiles. Automobiles generally are subject to specific rules that limit their deductibility.[31] These rules, tellingly, apply to "any 4-wheeled vehicle – (i) which is manufactured primarily for use on public streets, roads, and highways, and (ii) which is rated at 6,000 pounds unloaded gross vehicle weight or less."[32]

Generally, the purchase costs of automobiles are deducted over a five year period.[33] For lower priced automobiles, the entire car, over a period of years, can be amortized. But, there is a limitation on

[29] *General Explanations of the Administration's Fiscal Year 2004 Revenue Proposals*, Department of the Treasury, Feb. 2003, at page 23.

[30] It is important to note that raising the deduction limit to $75,000 (or whatever dollar number that is eventually passed and signed into law) will affect all types of property acquired by business, not just automobiles. The point of this article is to illustrate how these unintended consequences in seemly minor areas of tax policy may compound upon themselves to create large disparities between segments of entire industries (Hybrids and SUV's here). Therefore, this article offers no opinion on the current tax proposals before Congress, excepting where they are specifically addressed herein.

[31] Treas. Reg. § 1.280F-2T.

[32] I.R.C. 280(F)(5)(A). It should be noted that the restriction to "unloaded gross vehicle weight" prevents the shifting of a vehicle form one category to another by changing it's passenger load.

[33] I.R.C. § 168 (3)(D).

this deduction that suppresses its use for higher priced cars – luxury vehicles.[34]

By way of example, the limitations on an automobile first placed in service in 2002 are: $7,603 for the first tax year in its recovery period (2002); $4,900 for the second tax year in its recovery period (2003); $2,950 for the third tax year in its recovery period (2004); and $1,775 for each succeeding tax year in its recovery period (2005 and on).[35]

These limits make higher priced automobiles only partially deductible, and therefore limit their attractiveness as a business purchase. They are coordinated with section 179, so that "[a]ny deduction allowable under section 179 with respect to any [automobile] shall be subject to the limitations of subsections (a) and (b), and the limitation of paragraph (3) of this subsection, in the same manner as if it were a depreciation deduction allowable under section 168."[36]

4. The Intersection of Section 179 and SUV's

In order to understand the way Section §179 relates to SUV's, one must understand the origins of the 6,000 pound vehicle limitation that allows the accelerated expense deduction of §179 to apply to those vehicles that weigh over 6,000 pounds, while restricting more common lighter automobiles to the scheduled depreciation discussed *supra*.[37]

"The tax code defines industrial vehicles by weight instead of function. The parameter that the vehicle must be over 6,000 pounds fits

[34] Rev. Proc. 2002-14, Sec. 4.02(2), 2002-5 IRB 450.

[35] *Id.*; *But see* I.R.C. § 280F(a)(1)(C)(ii) (providing in pertinent part that the annual limitations are tripled for certain electric vehicle as discussed *infra*.). Also note that the first year deduction was $3,060 until the implementation of I.R.C. § 198(k) (the *Job Creation and Worker Assistance Act of 2002* discussed *supra*) that allows an additional 30% first year deduction. Vehicles that do not qualify under I.R.C. § 198(k) still are subject to the $3,060 limit.

[36] I.R.C. § 168 (3)(D).

[37] There may be some confusion regarding the calculation of the 6,000 pound number when determining if a vehicle qualifies for either the Section 179 deduction or Section 280(F) annual depreciation limitations. Automobiles are "[r]ated at 6,000 pounds unloaded gross vehicle weight or less." In the case of trucks, vans or sport utility vehicles, the "unloaded gross vehicle weight" is ignored and "gross vehicle weight" (GVW) is used instead. For trucks, vans and sport utility vehicles, gross vehicle weight means the fully loaded rating assigned to a particular vehicle by the manufacturer, based on chassis, engine and drivetrain capabilities. This means the weight of the vehicle itself and all the stuff it is designed to carry, such as people and cargo." ANNUAL DEPRECIATION LIMITS AND GROSS VEHICLE WEIGHT RATINGS for Trucks, Vans & Sport Utility Vehicles by Bill Sanders, http://www.biz.colostate.edu/faculty/cherieo/GrossVehicleWeights.doc (visited Mar. 6, 2003).

the original intent of the legislation to help small family farmers."[38] In the 1970's, when the current 6,000 pound cut off was instituted, SUV's did not exist as a viable passenger car alternative.[39] The Congress, in exempting these larger vehicles, expected that farmers would be able to purchase work pick-up trucks, tractors, and other workhorse vehicles with an immediate tax benefit. At the same time, those vehicles that weighed under 6,000 pounds (basically every passenger vehicle at the time) would not be afforded the same luxury. As this article has illustrated in Section II.A., *supra,* since the initial promulgation of the law the sport utility market has exploded, with interesting and unintended effects.[40]

As massive luxury SUV's have become the rage, they have replaced luxury automobiles in many garages. An increasing number of these SUV's have another defining characteristic – they cross the 6,000 pounds unloaded gross vehicle weight threshold set forth in Section 179. There are currently *at least* 34 sport utility vehicles that meet that test. Although some may be pick-up trucks, not one of them is a workhorse vehicle that a farmer or tradesman would reasonably use to haul crops, transport livestock, or to move tools and inventory. The law has not changed to meet that dynamic in the automobile industry.

The result is that business owners – those persons who can place in service an SUV weighing more that the 6,000 pound limit and still meet the business use requirements of the Internal Revenue Code – have an unexpected windfall wholly unintended by Congress. For example, a business owner can purchase a large luxury SUV (many of these SUV's are actually marketed as "luxury"), use it for some business purposes – enough to meet the requirements of the statute, enjoy the perceived power and prestige of these new style luxury vehicles, and deduct immediately $25,000 of the purchase price against their income attributable to their active pursuance of their trade or business. The equation becomes even more stark when one considers the ramifications an "[i]ncrease [in] the maximum amount of qualified property that a taxpayer may deduct under Section 179 to $75,000."[41] In essence, business owners will be able to buy all but the most expensive luxury SUV's, document that they meet the business usage tests (a minor matter) and expense the entire purchase price in the year

[38] Aileen Roder & Lucas Moinester, *A Hummer Of A Tax Break*, Taxpayer's for Common Sense White Paper, Jan. 23, 2003.

[39] *See generally* Peter Passell, *How G.I. Joe's Little Jeep Grew Into A Yuppie Hunk*, NEW YORK TIMES, Oct. 16, 1997, at G7.

[40] *See also* Jeffrey Ball & Karen Lundegaard, *Quirk in Law Lets Some SUV Drivers Take Big Deduction*,, WALL ST. J., Dec, 19, 2002, at D1.

[41] Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2004 Revenue Proposals*, Feb. 2003, at 23.

of purchase. That, by any measure, is a tremendous tax windfall.

B. State and Federal Laws Pertaining to Hybrids

1. Section 179A and the Relevant Federal Law

As this article discussed *supra*, Hybrids are the most viable new automobile technology to date. The tax treatment of Hybrids is starkly different than the tax treatment afforded SUV that qualify for the Section 179 treatments described *supra.* The Federal and state governments do provide some tax relief to hybrids, but that relief is paltry and should be increased to meet or exceed the tax benefits provided to qualifying SUV's.

Section 179A.provides a "[d]eduction for clean-fuel vehicles and certain refueling property"[42] The deduction is provided for "[an]y qualified clean-fuel vehicle property."[43] The deduction is limited to the cost of the vehicle,[44] or $2,000, whichever is less.[45] Finally, the tax benefit is limited so that it "[s]hall be allowed [only] for the taxable year in which such property is placed in service."[46]

There is a larger deduction under Section 179A available as follows:

> **(ii)** in the case of any truck or van with a gross vehicle weight rating greater than 10,000 pounds but not greater than 26,000 pounds, $5,000, or
> **(iii)** $50,000 in the case of—
> (I) a truck or van with a gross vehicle weight rating greater than 26,000 pounds, or
> **(II)** any bus which has a seating capacity of at least 20 adults (not including the driver).[47]

As a practical matter, this means that on the federal level the vast majority of clean-fuel vehicles (like Hybrids) are limited to a one-time $2,000 deduction. Currently, only the Honda Civic and Insight, and the Toyota Prius qualify for the Section 179A deduction.

Note that there is additional relief for electric cars (but not Hybrids) in the form of Section 280F(a)(1)(C)(ii). That provision allows the annual limitations under the standard automobile deprecation rules of Section 280F to be tripled.[48] This provision is of

[42] I.R.C. § 179A.
[43] *Id.* § 179A(a)(1)(A).
[44] *Id.* § 179A(a)(1).
[45] *Id.* § 179A(b)(1)(A)(i).
[46] *Id.* § 179A(a).
[47] *Id.* § 179A(b)(1)(A)(ii); *Id.* § 179A(b)(1)(A)(iii).
[48] "Congress believed that the price of an electric vehicle doesn't necessarily

little use, because there are no commercially viable electric cars planned or in continuing mass production.

2. *A Brief Survey of State Laws*

Many states have tax or financial incentive programs that mitigate the cost to business (and individuals as well) of a Hybrid purchase. Some states provide a direct tax credit or deduction to the taxpayer, regardless of whether they are a private individual or a business owner.[49] Others provide grants to specific entities (public transportation agencies, schools, etc.) to purchase Hybrid vehicles.[50] Still others have attempted to provide discounts on registration or other administrative costs that are usually required to maintain an automobile.[51] Others allow Hybrid owners to use High Occupancy Vehicle Lanes without the usual two passenger requirements.[52]

While it is clear that this type of state level incremental tax and administrative fee relief is a boon to the adoption of hybrid cars, these tools, even when combined with the $2,000.00 tax credit provided by the Federal government, are paltry when compared to the Section 179 provisions discussed *supra* that benefit the large SUV's.

represent the purchase of a luxury. Rather, the higher price of those vehicles often represents the cost of the technology required to provide an automobile designed to provide certain environmental benefits. Therefore, for electric vehicles, Congress believed it appropriate to modify the limitation on depreciation that applies to passenger automobiles" FTC P L-10004.1 (citing I.R.C. § 280F(a)(1)(C)(ii) and H. Rep. No. 105-148 (PL 105-34), at 427).

[49] *See* GA ST § 48-7-40.16(7)(b) ("[A] tax credit is allowed against the tax imposed under this article to a taxpayer for the purchase or lease of a new low-emission vehicle or zero emission vehicle that is registered in the State of Georgia. The amount of the credit shall be $ 2,500.00 per new low-emission vehicle and $ 5,000.00 per new zero emission vehicle."); *See* also K.S.A. § 79-32,201(a); OR ST § 316.116.

[50] *See*, 75 Pa.C.S.A. § 7202.

[51] *See also,* 72nd Oregon Legislative Assembly--2003 Regular Session Senate Bill 312(Eliminates the registration fee for hybrid vehicles.)

[52] *See* California Motor Vehicle Code §§5205.5 and 21655.9 (21655.9 provides that "[w]henever the Department of Transportation authorizes or permits exclusive or preferential use of highway lanes or highway access ramps for high-occupancy vehicles pursuant to Section 21655.5, the use of those lanes or ramps shall also be extended to vehicles that are issued distinctive decals, labels, or other identifiers [as hybrid cars] regardless of vehicle occupancy or ownership."); *See also* AZ ST § 28-737, (providing that "[a] person may drive a hybrid vehicle with alternative fuel vehicle special plates, or an alternative fuel vehicle sticker, and a hybrid vehicle sticker issued pursuant to § 28-2416 in high occupancy vehicle lanes at any time, regardless of occupancy level, without penalty.").

IV. *Consequences of Current Proposed and Existing Tax Policies*

A. *Current Policies*

The SUV provisions in the current tax code (express or implied) at present have several impacts on American industry and American highways.

1. *SUV's*

The tax loophole encourages manufacturers to build larger and larger SUV's, and it conversely prods business owners who qualify for the business use provisions discussed *supra* to purchase larger SUV's that they would otherwise not purchase.

This is an artificial distortion of the market. Although that distortion benefits American automobile manufacturers because they build and sell the vast majority of the 6,000 pound SUV's, it makes those manufacturers dependent on an artificial market at the expense of innovation and market growth in the new technologies of Hybrids. Manufacturers that offer limited choices in the large SUV market, like Honda and Toyota, have moved beyond these older technologies in order to innovate in the Hybrid arena.

We have seen this situation before. In the late 1970's restrictive import tarrifs on foreign cars brought to the United States was essentially a subsidy to domestic manufacturers. This import tariff on foreign content forced Japanese automakers to innovate in manufacturing techniques, in technology, and in their approach to the business and legal environment of the times (including opening plants in the United States in order to skirt the tariff provisions). American automobile companies failed to innovate in part because of those protections, with a well-known loss in market share.

Today, American auto manufacturers are in danger of a similar fate. Their emphasis on temporarily popular large SUV's is partially fueled by the artificial demand generated under the Section 179 rules. What this artificial market succeeds in doing is diverting resources and innovation away from the emerging vehicle technologies. This diversion occurs at the very time that other companies that are not dependent on the large SUV are forging ahead with little or no government support. An additional danger exists – it stands to reason that other automobile manufacturers that do not participate heavily in the large SUV category could join the fray, moving resources away

from technologies with social utility (like Hybrids) and into those technologies with less of a benefit (like the large SUV's).

2. *Hybrids*

This article has discussed the technology and tax treatment of Hybrids at length. The Federal government has provided the Section 179A deduction for hybrid purchases, but that $2,000 one time deduction together with the relevant state incentives, is significantly lacking when it is compared to the Section 179 $25,000 deduction (Note again the possibly that this deduction may become a $75,000 deduction if the Bush Administration proposal becomes law in its current form[53]).

The Federal government has invested significant resources in Hybrid technologies before. The Clinton era Partnership for a New Generation of Vehicles ("PNGV"), concentrated on hybrid car technologies to achieve a family car that could consistently perform at 80 miles per gallon.[54] The PNGV fell by the wayside in favor of the Bush Administration's "Supercar" project that aims to bypass hybrid technologies in favor of developing fuel cell powered vehicles that will operate on hydrogen fuel and emit only water as a waste product.[55] The Supercar project aims to begin mass production of these fuel celled cars in about a generation.[56]

This redirection of resources from Hybrids to fuel cell research is a tremendous gamble. If the technology works, it will provide tremendous benefits in reduced dependence on fossil fuels and political stability in oil producing regions. However, it avoids a technology (hybrid technology) that works in the present, shows tremendous promise, and is dominated by foreign automakers. To concede that market is a calculated risk that may have serious long term consequences in reduced competitiveness by American companies in the Hybrid market.

B. *Proposed Policies*

1. *SUV's*

The 179 loophole has not gone unnoticed. In the Congress, there are two companion bills, House Resolution 727, introduced in the

[53] *See supra* note 29.
[54] *See supra* note 6.
[55] *Id.*

House on February 12, 2003[57] and S 265, introduced in the Senate on January 30, 2003.[58] The bills propose to "[t]o include sports utility vehicles in the limitation on the depreciation of certain luxury automobiles"[59] This "SUV Business Tax Loophole Closure Act"[60]

[57] H.R. 727, 108th Cong., 1st Sess. (2003).
[58] S. 265, 108th Cong., 1st Sess. (2003).
[59] *Id.* The relevant text of the Senate bill reads as follows:
"A Bill ... [t[o amend the Internal Revenue Code of 1986 to include sports utility vehicles in the limitation on the depreciation of certain luxury automobiles.
Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the 'SUV Business Tax Loophole Closure Act'.
SEC. 2. INCLUSION OF SPORTS UTILITY VEHICLES IN LIMITATION ON DEPRECIATION OF CERTAIN LUXURY AUTOMOBILES.

(a) IN GENERAL- Section 280F(d)(5)(A) of the Internal Revenue Code of 1986 (defining passenger automobile) is amended by striking clause (ii) and all that follows and inserting the following new clause:
'(ii)(I) except as provided in subclause (II) or (III), which is rated at 6,000 pounds unloaded gross vehicle weight or less,
'(II) in the case of a truck or van, which is rated at 6,000 pounds gross vehicle weight or less, or
'(III) in the case of a sports utility vehicle not described in subclause (I), which is rated at more than 6,000 pounds but not more than 14,000 pounds gross vehicle weight.'.

(b) DEFINITION- Section 280F(d)(5) of the Internal Revenue Code of 1986 is amended by adding at the end the following new subparagraph:
'(C) SPORTS UTILITY VEHICLES- The term 'sports utility vehicle' does not include any vehicle which--
'(I) does not have the primary load carrying device or container attached,
'(II) has a seating capacity of more than 12 individuals,
'(III) is designed for more than 9 individuals in seating rearward of the driver's seat,
'(IV) is equipped with an open cargo area, or a covered box not readily accessible from the passenger compartment, of at least 72.0 inches in interior length, or
'(V) has an integral enclosure, fully enclosing the driver compartment and load carrying device, does not have seating rearward of the driver's seat, and has no body section protruding more than 30 inches ahead of the leading edge of the windshield.'.

(c) EFFECTIVE DATE- The amendments made by this section

essentially would remove SUV's "[r]ated at more than 6,000 pounds but not more than 14,000 pounds gross vehicle weight"[61] from the control of Section 179. Therefore, essentially every luxury SUV on the market today would lose the special tax treatment previously afforded them.

While this proposal on its face makes eminent sense, it fails to do much to encourage the growth of Hybrid technology. While passage of this bill would result in an immediate demand drop for SUV's because of the increased financial costs associated with their business purchase, Hybrids, the manifestation of a new and promising emerging technology, will not be impacted.

2. Hybrids

There are no real proposals to date to either increase incentives or decrease government credits on the Federal level for the purchase or development of Hybrids.

V. A Proposal to Equalize the Tax Treatment of SUV's and Hybrid Cars

A. The Terms of the Equalization Proposal

This article attempts to illustrate the disparity between Hybrids and SUV's treatment under the tax code. Although the solutions currently before the Congress provide some relief from this disparity,[62] there is a further solution that could have much better long term consequences. Hybrids that qualify for the business use treatment under this plan will be initially granted the same benefits under the Internal Revenue Code rubric as massive SUV's. Later, the current Section 179 provisions relating to SUV's would begin a slow phase out to allow manufacturers to modify the plans to account for the shifted market conditions.

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shall apply to property placed in service after the date of the enactment of this Act.

S. 265, 108th Cong., 1st Sess. (2003).

[60] *Id.*

[61] *Id.* at a(III).

[62] *Id.*

1. Costs of the Equalization Proposal

The costs of the equalization proposal are difficult to quantify. However, it is reasonably expected that there will be a short term increased drain on the treasury when both Hybrids and SUV qualify for the accelerated deductions. As the incentives for SUV's are removed, the cost may actually be less to the treasury because businesses claiming the deduction for Hybrids will likely be claiming inherently smaller deductions for lower priced hybrids, rather than higher priced luxury heavy SUV's.

Of course, there will be the additional loss of the artificial market for massive SUV's which will in the short term harm those automakers that are currently benefiting from it. As they bring further Hybrids to market, they will reap the corresponding rewards.

2. Benefits of the Equalization Proposal

Aside from the many benefits discussed *supra* if the SUV loophole is removed and if Hybrids are preferentially taxed, it is reasonable to foresee several other marked benefits. First, there will be increased competitiveness by domestic industry in future technologies that are available now (as opposed to fuel cell powered vehicles that are at least a decade and probably a generation away). Second, there will be reduced or at least more managed growth in our oil dependence because Hybrids by their nature consume far less petroleum than do the large SUV's. Third, there will be the concurrent environmental benefits of reduced smog and pollution that are part and parcel of a policy favoring lesser polluting vehicles over those with a greater environmental impact. Finally, there are safety benefits that flow from having smaller Hybrids on the road instead of large SUV's that are not as compatible with standard automobiles.

VI. Conclusion

It is clear that the unintentional tax loophole provided by Section 179 to massively sized business use SUV's has only two real benefits. It is a direct subsidy to American auto manufacturers that produce these vehicles, and it is nothing less than a tax windfall to the SUV buyers with little or no benefits to the society as a whole. Hybrid cars, which promise far more in performance, competitiveness, and resource management, are given short shrift under the current laws.

It stands to reason that the Federal government should at a minimum close the Section 179 loophole. Ideally, it will subsidize the beneficial emerging technology of the Hybrids in order to encourage its adoption while phasing out the unwarranted SUV deduction. For all the reasons *supra* the benefits of such a policy are profound. Manufacturers and consumers all will benefit from this move from a subsidy of the old technologies to a subsidy of the new.

Where Have All the Horses Gone? Driving Forces Behind the Underground Horse Industry in Connecticut

Donna L. Sims*

I. Introduction

Connecticut has a long and powerful relationship with agriculture and its implements. Quinnehtukqut or "beside the long tidal river"[1] is the state's Native American name and has been in use since the 1600's for both the region and the river to which it is associated. The Connecticut River, like the Nile, regularly floods the Connecticut River Valley, making the area one of the most fertile and rich agricultural regions in New England.

Today the state struggles with its almost suburban status as a desirable residential locale: conveniently located between the busy metropolitan areas of Boston and New York City, and its rural and agricultural past. The horse as a tool of agriculture in the state has its own intertwining history, yet today the horse industry in Connecticut remains vibrant, despite the inevitable decline of agriculture in the state. The difficulty for the horse industry lies in its relatively secretive status as a result of local and state taxation and public policy issues concerning zoning and nuisance in an urban/suburban environment.

II. Background

Connecticut horse owners have been known frequently to state that "there are more horses today in Connecticut than there were in Colonial times." This declaration, while intriguing, does not lend itself to support from any data supported by historic record. Indeed, comparative details and statistics of colonial life are difficult to discover, in great part because of the national view that has taken precedence. "The period of our history before 1783 has been construed as merely the ante-chamber to the great hall of our national development. In doing so, writers have concerned themselves not with

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[1]. State History Guide, LLC (2003), http://www.sghresources.com/ct/symbols/names/.

colonial history as such, but rather with the colonial antecedents of our national history."[2]

We can, however, make an attempt at interpolating an estimate of colonial horse ownership in Connecticut by looking at approximations of populations at points close in time. Historian, Jackson Turner Main estimates that in the year 1730 the colony of Connecticut had a population of about 38,000.[3] Since it is hardly likely that each person owned a horse, but also possible that some part of the population owned multiple horses for agricultural and transportation purposes, an estimate of 38,000 colonial horses is not beyond reason. Therefore based on estimates discussed later in this analysis of current horse populations, we most probably do have more horses in Connecticut today than in colonial times.

That horses played an important role in the commerce between the colonies and the development of transportation systems is relatively well documented through the evolution of our public modern highways. This may have been the basis for the later establishment of the personal property tax on motor vehicles which residents of Connecticut still enjoy. Municipalities assess and collect the tax today on motor vehicles owned and maintained in their jurisdiction.

Interestingly, responsibility for the highways gave rise to control over the methods of their use. The first statutory regulation giving towns the authority over railroad companies was "An Act Relating to Horse Railroads" adopted in 1864 and was later revised in 1866.[4]

III. The Relevant History of Horse Taxation

The adoption of the "Fundamental Orders of 1639"[5] allowed the colony some degree of independent governance: establishing democratic principles based on popular approval of "admitted freemen"[6], establishing the first local authority to fine, make or repeal laws, and grant levies. The Fundamental Orders are considered by

[2]. Charles M. Andrews, *Colonial Commerce*, 20 AM. HIST. REV. 43, 43-63 (Oct. 1914).

[3]. JACKSON TURNER MAIN, SOCIETY AND ECONOMY IN COLONIAL CONNECTICUT, Princeton University Press, (1983) at 177.

[4]. 1864, Conn. Pub. Acts, page no 37, Chap. 21, Rev. 1866, page no. 181, 206.

[5]. *The Federal and State Constitutions Colonial Charters, and Other Organic Laws of the States, Territories, and Colonies Now or Hereafter Forming the United States of America*, Compiled and Edited Under the Act of Congress of June 30, 1906, Francis Newton Thorpe, Washington, DC: Government Printing Office, 1909.

[6]. *Id.* at 1.

many to represent the first written constitution of a democratic government in our nation's history. The document, however, fails to establish any attempt to regulate business, agriculture or commerce as do later iterations of constitutional documents.

One of the earliest indications that horses enjoyed a favored status in the Connecticut economy was the enactment in 1672 by the General Court of Assemblies of the Connecticut Colony of a statute requiring towns to construct and maintain roads and bridges. It additionally imposed liability on towns for injuries to people and injuries to horses, if the injuries were from the failure to sufficiently maintain the roads and bridges.[7]

The property tax, as a tool for government generation of revenue has been used for thousands of years. As imposed by the British it was originally contemplated as a tax that used "ownership or occupancy of a property to estimate a taxpayer's ability to pay."[8] Over time the tax came to be regarded as in rem or a tax on the property itself. [9] "In the strict sense of the term, a proceeding "in rem" is one which is taken directly against the property or one which is brought to enforce a right in the thing itself."[10] By the time of the Revolutionary War, each of the colonies had systems in place to levy and collect taxes for a variety of purposes: capitation or poll tax, faculty taxes levied on certain trades, tariffs were levied on goods, excises were levied on consumption of goods and not the least of which, the property tax was generally levied on specified items, sometimes at fixed rates and sometimes according to its value, or ad valorem.

[7]. The Laws of Connecticut Colony, (1672), 7."This Count considering the great danger that persons Horses and Teams are Exposed unto, by reason of defective Bridges, and county High-ways in this Jurisdiction; Do Order; That if any person of any time loose his life through defect or insufficiency of such Bridges, in passing any such Bridge or High-way after due warning given unto any the Selectmen of the Town in which such defect is, in writing under the hand of two witnesses, or upon presentment to the County Court of such defective Wayes and Bridges, that then the County or Town which ought to secure such wayes or bridges, shall pay a fine of one hundred pounds to the Parents, Husband, Wife, or Children, or next of Kin to the party deceased. And if any person loose a Limb, break a Bone, or receive any other Bruise, or breach in any part of his body through such defect aforesaid, the County or Town through whose neglect such hurt is done shall pay to the party so hurt Double Damage; the like satisfaction shall be made to any Team, Cart or Carriage Horse of other Beast, or loading proportionable to the Damage sustained aforesaid."

[8]. Glenn W. Fisher, *History of the Property Tax in the United States*, EH. NET ENCYCLOPEDIA, edited by Robert Whaples, (Oct. 1, 2002), http://eh.net/encyclopedia/article/fisher.property.tax.history.us.

[9]. BLACK'S LAW DICTIONARY, 900-901, (4th ed. rev.1973).

[10]. Austin v. Royal League, 316 Ill. 188, 147 N.E. 106, 109.

Horses were considered valuable property to the colonists. Their use was varied, ranging from a tool for agriculture production to a means of transportation. Although horse racing existed in the colonies from as early as 1665 on Long Island: home to the first recognized race track, organized racing was not developed until after the Civil War when the American Stud Book was begun in 1868.[11]

Connecticut's statutory authority specifically authorizing the property tax on horses is enumerated as early as 1821 where the statute provided that ". ... all horses, asses and mules, one year old, or more, shall be valued, and set in the list at 10 percent of such value..."[12] While the underlying dispute in *Ingraham* had its foundation in the authority of local assessors to place varying percentage valuations on different types of taxable property, the court confirmed the authority of the state to authorize assessment of all forms of personalty and the court held that the present statutory authority required one hundred percent valuation. Later with the adoption of the Public Acts of 1860, the valuation practice was clarified stating that, "all property on which, by the laws of this state, taxes may be laid, shall be set in the list at its actual valuation...".[13]

One of the earliest cases of Connecticut's highest court acknowledging horses as taxable property relates primarily to a writ of attachment to secure a debt.[14] Defendant Dunn owed $600 to Enscoe who obtained a writ to attach the property of Dunn. Dunn owned five horses, six carts and six harnesses and when Enscoe attempted to seize the property as security for the debt, Dunn claimed that since he used the property as implements of his trade, he was exempted from seizure. The court opined that while the referenced exemption existed, it was strictly construed to relate to the business of a "carpenter, blacksmith, silversmith, printer, or the like,"[15] and did not relate to the business of transportation of merchandise, which was Dunn's business. The court further clarified the limited specificity of horses exempted from statutory judgment or taxation by referring to a specific exemption given to a physician for a horse for a value up to $200.

[11] *The History of Horse Racing*, ¶ 9 (1998), http://www.mrmike.com/explore/hist.htm.
[12] Ingraham v. Bristol, 144 Conn. 378 (1957).
[13] 1860 Conn. Pub. Acts, Ch. 15, 1.
[14] Encsoe v. Dunn, 44 Conn. 93 (1876).
[15] *Id.* at 99.

IV. Current Statutory Environment

Taxation of Connecticut horses, with minor modifications has remained remarkably unchanged since the nineteenth century. Horses and ponies used exclusively in farming operations are exempt from taxation.[16] There is value to the farmer who pulls their product to market in horse drawn wagons, plows the farm fields and performs other farming and agricultural tasks using horses, however for the vast majority of horse owners there is little practical benefit to this provision of the statutes.

Horses and ponies are also addressed under the general section of exemptions,[17] and although livestock is totally exempt, horses and ponies are exempt only up to a value of one thousand dollars each. Provided you have sufficient property to accommodate local zoning requirements, a resident of Connecticut could own many kinds of livestock (which might include cattle, dairy cows, sheep or goats, etc.) and not be required to pay personal property tax on them but would pay property tax on a horse with a value in excess of one thousand dollars.

After examining the personal property tax and its development in Connecticut, it seems a logical conclusion that the tax on horses is a relic from a time when horses and carts used the highways and byways and local towns needed taxes for maintenance costs and other costs of liability. In other ways the holdover has been passed on to motor vehicles, which do actually use and wear the streets and roads.

Of recent interest concerning the automobile tax is a proposal by Governor M. Jodi Rell to eliminate the local personal property tax on automobiles.[18] Although the proposal has undergone recent iterations, the possibility of success for this legislative session is unlikely. Municipalities are lobbying strongly against this change since the assurance of alternate revenues transmitted by the state is not a certainty.

Horse owners are also required by statute to declare the value of their personal property, including horses to the assessor annually as of the assessment date of October 1st.[19] If the property owner fails to declare the value by the return date of November 1st the assessor is required to place a value on the property and adds a penalty of 25 percent of the value for failing to report.[20]

[16]. Conn. Gen. Stat. § 12-91 (a) (2004).
[17]. *Id.* at § 12-81 (68) (2005).
[18]. Conn. HB 05550 (2006).
[19]. Conn. Gen. Stat. § 12-40, (2005).
[20]. *Id.* at § 7-568, (2005).

The assessor in each town and city gathers all of the declared information annually and reports to the Office of Policy and Management where statewide statistics are compiled. The following table represents statewide totals of horses and ponies declared over the last ten years.[21]

Table I.

Year	*# Horses*	*Year*	*# Horses*
1995	2443	2000	2187
1996	1634	2001	1797
1997	1834	2002	1803
1998	1729	2003	1857
1999	2886	2004	1876

While these statistics may not seem unusual to many, to members of Connecticut's horse community the numbers represent a pittance of rule followers. Where are all of the horses and why are their owners so reluctant to report to the state?

V. Who Is Counting Anyway?

The American Horse Council Foundation commissioned the firm of Deloitte Consulting LLP in 2004 to conduct a study on the economic impacts of the U.S. horse industry. The results of the study were completed and issued in 2005.[22] This study has important implications for the Connecticut horse industry because it demonstrates the significant disparity between reported ownership and actual

[21]. Office of Policy and Management, Municipal Statistics (2006).

[22]. American Horse Council Foundation, "*The Economic Impact of the Horse Industry on the United States*" 2005. "As a large, economically diverse industry, the United States horse industry contributes significantly to the American economy. Horse owners and industry suppliers, racetracks and off-track betting operations, horse shows and other competitions, recreational riders and other industry segments all generate discrete economic activity contributing to the industry's vibrancy. The spending generated within the horse industry, and the subsequent spending between co-dependent industries, contributes hundreds of thousands of jobs and billions of dollars to the economy on an annual basis." American Horse Council Foundation, *supra*.

ownership. The study designed a sampling methodology which was used to estimate the numbers of horses in each state. Of the nine million horses estimated in the United States today, Connecticut ranked 41st. This is how the state compared to the top five states.

Table II.

State	*# Horses*	*State*	*# Horses*
Texas	978K	Oklahoma	326K
California	698K	Kentucky	320K
Florida	500K	**Connecticut**	**52K**

The University of Connecticut, Department of Animal Science and Department of Agriculture and Resource Economics conducted a survey relating to the industry and preliminary results indicate a more conservative estimate extrapolated from the survey results.[23] While the scope of the survey encompassed a number of quantitative and qualitative issues relating to horse ownership, the number of horses actually reported was approximately three thousand in the state.

VI. Conclusion

Why are Connecticut horse owners so reluctant to let the regulatory world know about the existence of their horses? One can only presume that the orneriness is derived from a natural Yankee disinclination to report anything to the tax assessor. The reality of failing to report is at least statutorily more punitive than disputing the value with the assessor, particularly when one recognizes the ability to assess a 25 percent penalty, plus the potential to back-assess the undeclared horse for up to three years.

Archaic personal property tax laws designed for the horse and buggy still plague the horse owner in Connecticut today and although many sources indicate a vibrant industry, outdated property tax laws have resulted in a secretive and undervalued industry.

[23]. Jennifer Nadeau, Farhad Shah, Anita Chaudhry, Jose Maripani, "*Connecticut's Horse Industry: A Demographic and Economic Analysis,* College of Agriculture & Natural Resources, University of Connecticut (2005).

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