PETITION FOR REHEARING WITH SUGGESTION FOR REHEARING *EN BANC*

STATEMENT OF COUNSEL

Defendant-Appellant Linda Vaughey, the Montana Commissioner of Political Practices,[1] Defendant-Cross-Appellant Mike Cooney, the Secretary of State of Montana, and Defendant-Intervenor-Appellants League of Women Voters of Montana, *et al.*, respectfully submit this joint petition for rehearing and suggestion for rehearing *en banc* pursuant to Rules 35 and 40 of the Federal Rules of Appellate Procedure. In the judgment of counsel, this case meets the appropriate standards for rehearing and/or rehearing *en banc*, as provided in the Local Rules of this Court and F. R. App. Pr. 35 and 40, for several reasons.

First, this case presents a question of exceptional importance on which, as the dissenting opinion of Circuit Judge Hawkins recognizes, the decision of the panel majority conflicts with the decisions of the United States Supreme Court in *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990), and *FEC v. Massachusetts Citizens for Life*, 479 U.S. 238 (1986). The majority decision strikes down Montana's I-125, which was enacted by the people of Montana in 1996 to limit what the Supreme Court has termed "the corrosive and distorting

[1] During the pendency of this appeal, former Montana Commissioner of Political Practices Ed Argenbright was succeeded in office by Linda Vaughey, the current Commissioner.

effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public's support for the corporation's political ideas." *Austin*, 494 U.S. at 660. I-125 furthers this compelling state purpose by prohibiting the use of corporate general treasury funds to promote the enactment or defeat of ballot initiatives, while permitting corporations to participate in ballot initiative campaigns through expenditures from segregated funds collected from employees, members and shareholders of the corporation who wish to support the corporation's political activities. Under the Supreme Court's *Austin* decision, which upheld a Michigan statute imposing a segregated fund requirement for corporate independent expenditures, I-125 "is justified by Montana's asserted interest in eliminating what its people have determined to be distorting effects of corporate wealth on the electoral process." Slip Op. at 12351 (dissenting opinion of Judge Hawkins). Rehearing or rehearing *en banc* is warranted to correct the majority's misapprehension of Supreme Court precedents in striking down a statute of great importance to Montana's political process.[2]

This Court's ruling on the constitutionality of I-125 under the First Amendment, moreover, is of great significance not only for the State of Montana,

[2] This petition addresses only the ruling that I-125 is unconstitutional, and does not take issue with the ruling rejecting plaintiffs' challenge to I-137.

but for the other 26 states across the country that employ initiatives or referenda. *See* Thomas E. Cronin, DIRECT DEMOCRACY: THE POLITICS OF INITIATIVE, REFERENDUM AND RECALL 2-3, 51 (1989) (summarizing states that provide for referendum, initiative and/or recall). The distorting effect of corporate political expenditures has dramatically affected the initiative process in many such states,[3] and Montana's I-125 is the first law of its kind to be the subject of federal appellate review. The majority's ruling will discourage any other state from enacting similar provisions. It is imperative that states within this Circuit and across the country have the ability to protect their states' democratic processes by enforcing reasonable, carefully drawn limitations such as I-125.

Further, rehearing or rehearing *en banc* is warranted because the panel majority failed to apply the proper *de novo* standard of review to the district court's mixed conclusions of law and fact, in conflict with the precedents of this Court. *National Association of Radiation Survivors v. Derwinski*, 994 F.2d 583, 587 n.6 (9th Cir. 1993) (en banc), *cert. denied*, 510 U.S. 1023 (1993); *Bay Area Peace Navy v. U.S.*, 914 F.2d 1224, 1226-1227 & n.1 (9th Cir. 1990). Thus, for example, the panel majority applied the deferential "clear error" standard of review to the district court's finding "that there was no imminent threat to the democratic

[3] David R. Lagasee, *Undue Influence: Corporate Political Speech, Power and the Initiative Process*, 61 Brook. L. Rev. 1347, 1347-49 (1995).

process" that would justify a restriction on corporate general treasury spending in initiative elections. Slip Op. at 12342. The district court's findings, however, were premised on an incorrect understanding of the governing legal standards, including its belief that a showing of *quid pro quo* financial corruption is necessary to demonstrate a compelling state interest, *see* CR 186 at 15, 21, and its belief that defendants were required to prove that money has been the sole variable in initiative elections in order to sustain I-125, *id*. at 21. These and other critical legal assumptions underlying the district court's findings are incorrect under *Austin*, which expressly rejected any reliance on proof of *quid pro quo* financial corruption, and instead held that "the *potential* for distortion" presented by the use of the corporate structure was sufficient to justify special restrictions on the use of corporate general treasury funds. *Austin*, 494 U.S. at 661 (emphasis added). Under this Court's precedents, the majority's deference to such legally flawed findings was improper, particularly when the constitutionality of a state statute is at stake. Review by the full Court is therefore necessary to maintain uniformity of the Court's decisions.

ARGUMENT

I. The Majority Opinion Misapprehended the Supreme Court's Decisions in *Austin* and *MCFL*, and the Exceptional Importance of the Case Warrants Rehearing or Rehearing En Banc to Affirm the Constitutionality of Montana's I-125.

Montana's I-125 is designed to insure that corporate participation in ballot initiative campaigns reflects actual public support for the corporation's political views, rather than merely the sheer economic power that corporations derive from the state-created advantages of the corporate form. As the Supreme Court has noted:

> [t]he resources in the treasury of a business corporation . . . are not an indication of popular support for the corporation's political ideas. They reflect instead the economically motivated decisions of investors and customers. The availability of these resources may make a corporation a formidable political presence, even though the power of the corporation may be no reflection of the power of its ideas.

MCFL, 479 U.S. at 258. I-125 therefore prohibits the use of corporate general treasury funds in ballot initiative campaigns, while permitting corporations to participate in such campaigns through the use of segregated funds collected from employees, members and shareholders who wish to support the corporation's political activities. Mont. Code Ann. § 13-35-227.[4]

The decision of the panel majority, which would establish an insuperable bar to regulations such as I-125, cannot be squared with the Supreme Court's decision

[4] The text of I-125 is reproduced in the Slip Opinion at n.4.

in *Austin v. Michigan Chamber of Commerce.* In *Austin*, the Supreme Court upheld the constitutionality of a Michigan statute prohibiting corporations from using general treasury funds to make independent political expenditures and requiring all such expenditures instead to be made from segregated funds raised from individual officers, employees or shareholders of the corporation. The same interests that the Supreme Court found compelling in *Austin* – protecting the electoral process from the distorting influence of corporate wealth, and protecting the rights of shareholders who may not subscribe to the corporation's political goals, are served by I-125. After *Austin*, "'[t]he conclusion is inescapable that legislatures are now free to restrict corporations to spend only from separate political funds *in ballot measures as well as candidate elections.*'" *See* Slip Op. at 12348 (dissenting opinion of Judge Hawkins, *quoting* Gerald G. Ashdown, *Controlling Campaign Spending and the New Corruption: Waiting for the Court*, 44 Vanderbilt Law Review 767, 779 (1991) (emphasis added by dissenting opinion)).

The panel majority opinion attempted to distinguish *Austin* by asserting that *Austin* turned on "the difference between expenditures for candidate elections and ballot issues." Slip Op. at 12340-41. But this disregards the critical passage in *Austin* in which the Supreme Court *expressly declined* to place any weight on the

traditional state interest in protecting candidate elections from the risk of *quid pro quo* financial corruption:

> *Regardless of whether* this danger of "financial *quid pro quo*" corruption may be sufficient to justify a restriction on independent expenditures, Michigan's regulation *aims at a different type of corruption* in the political arena: the corrosive and distorting effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public's support for the corporation's political ideas.

Id. at 659-660 (emphasis added). The Supreme Court thereby recognized a new compelling interest in controlling the distorting effects of corporate wealth on the political process that turns not on the *object* of the spending (candidate elections or referenda), but on the *source* of the spending (corporate general treasury funds not raised for political purposes). As Judge Hawkins' opinion points out, "*Austin* identified a new rationale for limiting corporate campaign spending that does not turn on whether candidate elections or ballot initiatives are at issue." Slip Op. at 12351. "Once *Austin* was decided, therefore, the natural conclusion was that a similar restriction on corporate spending in state referenda would be upheld . . . ." Slip Op. at 12348 (dissenting opinion of Judge Hawkins).

Corporations, unlike individuals and non-incorporated entities, enjoy state-created rights that enhance their profit-making ability. *Austin* explains this as follows: "State law grants corporations special advantages – such as limited liability, perpetual life, and favorable treatment of the accumulation and

distribution of assets – that enhance their ability to attract capital and to deploy their resources in ways that maximize the return on their shareholders' investments." 494 U.S. at 658-659; *see also MCFL*, 479 U.S. at 258 n.11 (corporations are "by far the most prominent example of entities that enjoy legal advantages enhancing their ability to accumulate wealth.") *Austin* and *MCFL* recognize that states have a compelling interest in assuring that these state-created advantages do not provide corporations with unfair leverage in the electoral arena. *Austin*, 494 U.S. at 659-660; *MCFL*, 479 U.S. at 258.

A business corporation seeking to control the outcome of a ballot initiative election in Montana enjoys precisely the same state-created advantages that the Court described in *Austin* and *MCFL*. There exists no inherent right to the state's assistance in securing an artificial advantage over other speakers in the marketplace of ideas. Montana thus has a compelling interest in requiring corporate spending in initiative campaigns to be conducted through segregated PAC funds raised specifically for use in the electoral arena.

Montana's I-125 also protects the political rights of shareholders by assuring that corporate expenditures in the political process are made from funds raised specifically for that purpose. Again, both *MCFL* and *Austin* recognize this as a compelling state interest supporting a segregated fund requirement. *MCFL*, 479 U.S. at 258; *Austin*, 494 U.S. at 659. *See also FEC v. National Right to Work*

Committee, 459 U.S. 197, 207-08 (1982) (noting that regulation of corporate solicitations for PAC fund served goal of protecting shareholders whose investments were not made for political purposes).[5]

Contrary to the reasoning of the panel majority, Slip Op. at 12341, the important constitutional question presented by this case cannot be resolved by asserting that the Supreme Court must first overrule its decision in *First National Bank of Boston v. Bellotti*, 435 U.S. 765 (1978), before an appellate court may uphold a regulation such as I-125. As the dissent points out, the holding of *Bellotti* does not dispose of this case, because the statute struck down in *Bellotti* banned *all* corporate spending in initiative elections, and made no provision allowing for corporate expenditures from segregated funds as does I-125. Thus, to assert that *Bellotti* has not been overruled simply "begs the question", as Judge Hawkins noted, since *Austin* has not been overruled, either:

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[5] The record contains specific, undisputed testimony by corporate shareholders that their own political beliefs were violated by the corporation's spending on initiative campaigns in Montana. Testimony of Tony Jewett, RT 645-646 (ER 55-56); Deposition of Joseph M. McNulty, Ex. 736 at 30-31. Further, a professional survey of Montana residents showed that owners of corporate shares or mutual funds overwhelmingly believe that corporate spending on initiative campaigns reflects only the views of a few corporate officers rather than the views of shareholders. Ex. 580A at 5. As *Austin* and *MCFL* recognize, it is no answer to say that shareholders who disagree with a corporation's political expenditures may simply liquidate their holdings, because they may face serious economic disadvantages for doing so – such as unfavorable market conditions, tax consequences, or other economic disincentives. *MCFL*, 479 U.S. at 264; *Austin*, 494 U.S. at 663.

> In such a situation, we should not simply assert that one case directly applies and then ignore the other. We must do our best to reconcile the two. And in my opinion, the best way to reconcile these cases is to acknowledge that *Austin* identified a new rationale for limiting corporate campaign spending that does not turn on whether candidate elections or ballot initiatives are at issue. In addition, the statute in *Austin* was less objectionable than the statute in *Bellotti* because it allowed for corporate spending through a segregated fund. Because the [Montana] initiative also allows for corporate spending through a segregated fund, I think it is justified by Montana's asserted interest in eliminating what its people have determined to be distorting effects of corporate wealth on the electoral process.

Slip Op. at 12351 (dissenting opinion of Judge Hawkins).

The Supreme Court's 1986 opinion in *FEC v. MCFL* further demonstrates that I-125's provision for corporate spending through a segregated fund is a critical distinction that renders *Bellotti* inapposite. The *MCFL* opinion, joined by a majority of the Supreme Court, noted that requiring corporations to use segregated funds instead of their general treasury funds "is of course distinguishable from the complete foreclosure of any opportunity for political speech that we invalidated in the state referendum context in *First National Bank of Boston v. Bellotti.*" *MCFL*, 479 U.S. at 259 n.12. Accordingly, the key factor in determining the constitutionality of a restriction on corporate spending is whether the restriction leaves open an avenue of expression for the corporation, as does Montana's I-125, or instead "completely foreclos[es]" any such opportunity. *Id*.; *see also Austin*, 494 U.S. at 660 (noting that Michigan's statute "does not impose an absolute ban

on all forms of corporate political spending but permits corporations to make independent political expenditures through separate segregated funds").

II. The Majority Opinion Conflicts with Controlling Ninth Circuit Precedent Requiring *De Novo* Review of Mixed Findings of Fact and Law, Particularly in Cases Addressing the Constitutionality of State Statutes.

The majority improperly deferred to district court findings that constituted mixed findings of fact and law and were based on an incorrect understanding of the governing legal principles. The majority stated:

> As there was evidence pointing in each direction, we cannot say the court clearly erred in finding that there was no imminent threat to the democratic process.

Slip Op. at 12342. This deferential review conflicts with the precedents of this Circuit, which require *de novo* review of mixed findings of fact and law, particularly when they involve questions of constitutional law. As this Court held in an *en banc* decision reviewing a district court judgment in another First Amendment case, "precedent establishes that the de novo standard of review is appropriate for mixed questions involving constitutional issues." *National Association of Radiation Survivors v. Derwinski*, 994 F.3d 583, 587 n. 6 (9th Cir.) (*en banc*), *cert. denied*, 510 U.S. 1023 (1993). Similarly, in *Bay Area Peace Navy v. United States*, 914 F.2d 1224, 1227 n.1 (9th Cir. 1990), this Court stated that "the appropriate standard of review is *de novo* because the application of constitutional law to the facts of this case 'requires us to consider legal concepts in

the mix of fact and law and to exercise judgment about the values that animate legal principles.'" (quoting *ACORN v. City of Phoenix*, 798 F.2d 1260, 1263 (9th Cir. 1986) (citations omitted).

A district court finding that there is no imminent threat to the democratic process that justifies I-125, *see* Slip Op. at 12342, is precisely the type of mixed finding of fact and law to which *de novo* review should apply. Such a conclusion is critically dependent upon a proper assessment of the legal standards that govern the inquiry, including Supreme Court precedent that establishes what does and does not pose a threat to the democratic process for purposes of First Amendment analysis. The deferential "clearly erroneous" standard of Rule 52 should not be applied to such findings, because that would abdicate the duty of the Court of Appeals to insure that the law is properly and uniformly applied and that constitutional issues of overriding significance are correctly decided.

Here, the district court's findings were based on a critically flawed understanding of the governing legal principles. For example, the central premise of the district court's ruling was that, based on the testimony of plaintiff's expert, Professor Lopach, "there is no corruption or appearance of corruption in Montana ballot issue elections." CR 186 at 21; *see also id.* at 14. Professor Lopach and the district court, however, equated "corruption" with candidate-related financial improprieties. *See* RT 318 (ER 19), Testimony of Prof. Lopach ("when an election

official is bribed or when a legislator is bought off"); CR 186 ("buying or selling votes or tampering with election results"). In *Austin*, however, the Supreme Court specifically held that it was *unnecessary to address* whether the prevention of this type of *quid pro quo* financial corruption supported Michigan's ban on using corporate general treasury funds. 494 U.S. at 659-660. The ban, instead, was justified by the compelling state interest in preventing "*a different type of corruption* in the political arena: the corrosive and distorting effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public's support for the corporation's political ideas." *Id*. (emphasis added). *See also MCFL*, 479 U.S. at 258. Because they are based on an incorrect legal definition of "corruption," the district court's findings of a lack of harm to the political process in Montana clearly are not entitled to deference.

Similarly, the district court concluded that I-125 should be struck down because many factors influence the outcome of ballot elections in Montana and "neither money nor media advertising is the sole or even the single most important variable controlling election outcomes." CR 186 at 21. Again, this reasoning reflects legal error. There was no evidence before the Court in *Austin* that independent expenditures by corporations had been the sole or even the single most important variable in determining the outcome of Michigan elections.

The *Austin* Court held instead that it was appropriate to defer to the legislative judgment that the special benefits conferred by the corporate form "present the *potential* for distorting the political process", noting that the Court's past cases had afforded similar deference to Congress' judgment concerning the potential for undue influence presented by the use of the corporate structure. 494 U.S. at 661 (emphasis added) (citing *FEC v. National Right to Work Committee*, 459 U.S. at 209-210); *see also MCFL*, 479 U.S. at 257 (noting that traditional corporations raise "the *prospect* that resources amassed in the economic marketplace *may be used* to provide an unfair advantage in the political marketplace" (emphasis added). *Cf. Nixon v. Shrink Missouri Gov't PAC*, 120 S. Ct. 897, 908 (2000) (noting that the very fact that the public has voted in favor of a campaign reform initiative provides evidence of a public concern about the influence of money in politics).

Indeed, the evidence presented in this case concerning the distorting effects of corporate spending went far beyond the record before the Court in *Austin*. If evaluated under the proper legal standards, the record is more than sufficient to demonstrate the justifications for I-125's segregated fund requirement. Although space does not permit a full discussion of the facts, a few points are illustrative. Between 1982 and 1994, nearly three out of every four dollars spent on initiative campaigns in Montana came from corporations and their allied trade associations.

C.B. Pearson & Hilary Doyscher, *Big Money and Montana's Ballot Campaigns: A Study of Campaign Contributions to Montana's Ballot Elections from 1982 to 1994*, Ex. 602 at 1, 7. During that period, the largest five corporate contributions combined with the largest five trade association contributions accounted for nearly $2,000,000 in spending on ballot measures, a little less than half of all dollars raised for all ballot measures during that period. *Id*. at 12-13.[6] All of these latter contributions were spent to oppose various initiatives, and all of those initiatives failed. *Id.*

In several Montana initiative campaigns, the contributions of the corporate side have amounted to more than 90% -- sometimes more than 95% -- of *all* contributions from *both* sides of the initiative debate.[7] In fact, the total amount spent by 16 corporations or corporate trade associations on just one Montana

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[6] A total of approximately $4.7 million was raised for all ballot measure campaigns from 1982 through 1994. Ex. 602 at 12.

[7]

Initiative	Proponents' Contributions	Opponents' Contributions	Opponents % of Total
I-87 1980 (bottle bill)	$ 24,422	$575,794	95.9%
I-113 1988 (litter control)	$ 54,806	$493,339	90.0%
I-115 1990 (tobacco tax)	$ 43,654	$1,583,865	97.3%
I-122 1996 (clean water)	$460,252	$2,336,343	83.5%

Source: Ex. 506 (I-87), Ex. 602 Appendix C (I-113, I-115); Ex. 801 (I-122).

initiative in 1990 nearly equaled the total amount of campaign contributions made by 17,000 contributors to *all* candidates for statewide or state legislative office in Montana that year. RT 904 (ER 69) (testimony of Samantha Sanchez).

Spending in opposition to initiatives proposed by citizens' groups in Montana has been particularly overwhelming in assuring the defeat of such initiatives. The defeat of such initiatives is of particular concern in view of Montana's original purpose for adopting the initiative and referendum process: to provide a means for the people to legislate directly when the legislature is resistant to important reforms desired by citizens. An analysis of all initiative campaigns since 1982 in which two-thirds or more of the total spending was done on the "no" side (the side opposing enactment of the initiative) showed that such initiatives were defeated seven out of nine times. Ex. 742.[8]

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[8] Of course, many initiatives that appear on the ballot are not terribly controversial, and do not attract strong opposition. Further, when one side only slightly outspends the other, the result of the election is unlikely to have been dictated by spending. It is therefore uninformative to lump together all initiatives, whether or not they were the subject of one-sided spending campaigns, and merely calculate how often the highest-spending side was successful. Indeed, Professors David Magleby and Thomas Cronin – acknowledged by *plaintiffs'* experts to be the leading authorities in this area – have emphasized the importance of analyzing separately those initiatives in which one-sided spending occurred. David B. Magleby, DIRECT LEGISLATION: VOTING ON BALLOT PROPOSITIONS IN THE UNITED STATES 146-48 (1984); Cronin, DIRECT DEMOCRACY, at 107, 109-113. *Cf.* Slip Op. at 12334 (citing plaintiffs' figures which lump together all initiatives, regardless of whether spending was one-sided).

None of this evidence could be properly evaluated by the district court when it was laboring under an incorrect understanding of the legal standards that should have governed its inquiry.[9] The panel majority's deference to the district court's findings was improper under this Circuit's precedents, particularly in a constitutional case of this significance.

[9] Appellants also submit that, even if *Bellotti* controlled this case rather than *Austin*, the record would be more than adequate to demonstrate corporate dominance of the initiative process that justifies I-125's segregated fund requirement, and that the district court's findings to the contrary reflect clear error even if *de novo* review were not required.

CONCLUSION

For the foregoing reasons, the Montana Commissioner of Political Practices, the Secretary of State of Montana, and the League of Women Voters of Montana, *et al.*, all defendants in the case below, respectfully request that their petition for rehearing with suggestion for rehearing *en banc* be granted.

Respectfully submitted,

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