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SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF LOS ANGELES

DAVID SCOTT SMILEY, *et. al.*,

Plaintiffs,

vs.

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS, *et. al.*,

Defendants.

CASE NO. BC 254659

[Assigned to the Honorable Anthony J. Mohr, Dept. 309]

CLASS ACTION

PLAINTIFFS' REPLY TO DEFENDANT NEULEVEL'S OPPOSITION TO MOTION FOR PRELIMINARY INJUNCTION; DECLARATION OF PAUL TRAINA

Date: September 26, 2001
Time: 1:30 p.m.
Dept: 309

Complaint Filed: July 23, 2001

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I. INTRODUCTION

Defendants are engaged in a criminal act that must be stopped. This Court should not be misled to believe that this case is about regulation of the Internet -- it is not. Rather, this case is about the regulation of illegal lotteries and defendant's unlawful business practices. The <.biz> domain distribution scheme employed by defendant NeuLevel meets all the elements of a lottery including: (1) prize - the right to register a particular domain name; (2) chance - winning or losing depending on luck or fortune; and (3) consideration - payment of money for each submission. (Pen. Code, § 319.)

In addition, defendant completely misses the mark on its Supremacy Clause and Commerce Clause arguments. *First*, to succeed on a Supremacy Clause argument, defendant must challenge California's anti-lottery and unfair competition laws and establish that they conflict with federal statutes that are intended to occupy the same field. However, to defendant's demise, Plaintiffs are not seeking to enforce any Internet laws or regulations, only anti-lottery and unfair competition laws which are consistent with federal law in these fields. *Second*, it is well-settled that the mere fact that the application of a law may incidentally effect the Internet does not violate the dormant Commerce Clause. (*Ford Motor Co. v. Texas Dept. of Trans.* (5th Cir. 2001) 2001 U.S.App.LEXIS 19185.)

This Court should not be tricked into believing that the Department of Commerce ("DOC") entered into an agreement with defendant ICANN wherein they approved defendant's lottery scheme. The agreements between defendants ICANN and Neulevel, and the registrars and Neulevel, never explain defendants' lottery process. (See Decl. of Traina, Ex. A: Appendix J to Registry Agreement). In fact, noticeably absent from the "Registry TLD Start-Up Plan" provided by defendant to the DOC, is any indication that multiple submissions would be accepted from a registrant for a particular <.biz> domain name, the essence of this lottery scheme. Hence, the DOC could not, and did not approve defendant's lottery scheme. In fact, in a letter from the DOC, the agency explained that it would not participate in the TLD distribution process. (See Decl. of Traina, Ex. B.)

The real "evidence" shows a consistent scheme of deception by defendant, starting with the absence of information provided to the DOC and continuing on into this Court. Defendant's deception

must be stopped.

II. THE SUPREMACY CLAUSE IS INAPPLICABLE

Defendant engages in a historical diatribe of the Internet to convince this Court it is immune from the established federal and state laws which prohibit lotteries. Defendant deceptively spins a fictional tale in which it proffers endless mounds of so-called "evidence"—none of which expressly or impliedly, read separately, or taken as a whole, provides them with the immunity essential to its defense. Instead, defendant improperly paraphrases numerous documents and statutes in a desperate attempt to create an "inferential leap" of preemption. A closer look at defendant's "evidence" reveals that no governmental authority has decreed any federal or state statute preempted.

In order to prevail on the Supremacy Clause argument, defendant must show that Congress' command over lotteries, not the Internet, is explicitly stated in the federal law or implicitly contained in its structure and purpose. (*Jones v. Rath Packing Co.* (1977) 430 U.S. 519, 525 [51 L.Ed.2d 604, 97 S.Ct. 1305].) Here however, defendant's reliance on the Supremacy Clause as a defense to its illegal lottery fails for two controlling reasons: *first*, in forbidding the creation of, and participation in lotteries, Federal Statutes, 18 U.S.C. § 1301 and 18 U.S.C. § 1955, expressly authorizes state anti-lottery laws; and *second*, Defendant has failed to produce any evidence to show any federal law or statute *expressly or impliedly* preempts state anti-lottery laws.

A. Congress Expressly Forbids Lotteries

Congress enacted 18 U.S.C. § 1955 to expressly prohibit the creation of lotteries, which states in relevant part:

> "(a) Whoever conducts, finances, manages, supervises, directs, or owns all or part of an illegal gambling business shall be fined under this title or imprisoned not more than five years, or both.
>
> (b) As used in this section—
>
> (1) "illegal gambling business" means a gambling business which--
>
> (i) **is a violation of the law of a State** or political subdivision in which it is conducted; . . .
>
> (2) "gambling" includes but is not limited to pool-selling, bookmaking, maintaining slot machines, roulette wheels or dice tables, **and conducting lotteries**, policy, bolita or numbers games, or selling chances therein." [emphasis added].

To further illustrate its intent to prevent the creation and participation in lotteries, Congress also enacted 18 U.S.C. § 1301 that prohibits the transportation of lottery interests in interstate and foreign commerce.[1]

What is evident from these two statutes is that Congress intended to create a *national uniform plan* expressly prohibiting the creation of, and participation in, lotteries. California's anti-lottery law does not conflict with the laws enacted by Congress—it mirrors Congressional intent. Moreover, by enacting 18 U.S.C. § 1955, Congress specifically empowered individual States to enact laws to prohibit any "illegal gambling business," i.e. lotteries. (18 U.S.C. § 1955(b).) Defendant has provided *no evidence* that shows Congress intended to preempt its own federally created anti-lottery legislation—"the supreme law of the land."

B. California's Anti-lottery Statute Does Not Violate the Supremacy Clause

As analyzed above, California's anti-lottery statute does not violate the Supremacy Clause because, like 18 U.S.C. §§ 1995 & 1301, it expressly prohibits lotteries. Also, 18 U.S.C. § 1995 empowers States to enact anti-lottery legislation. Notwithstanding the overwhelming evidence that Congress intended to prevent lotteries, California's anti-lottery statute does not violate the Supremacy Clause because defendant has failed to illustrate that Penal Code § 319 conflicts with any federal statute or scheme expressly prohibiting this State's regulation of lotteries.

When applicability of a state statute is challenged under the Supremacy Clause, the Court must consider whether Congress intended to prohibit the states from regulating in such a manner. (*Pacific Legal Foundation v. State Energy Resources Conversation & Development Commission* (9th Cir 1981) 659 F.2d 903, 919 [no preemption of state statute regulating nuclear energy even though Congress had

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[1] "Whoever brings into the United States for the purpose of disposing of the same, or knowingly deposits with any express company or other common carrier for carriage, or *carries in interstate commerce or foreign commerce any paper, certificate, or instrument purporting to be or to represent a ticket, chance, share, or interest in or dependent upon the event of a lottery*, gift, enterprise, or similar, scheme, offering prizes dependent in whole or in part upon lot or chance, or any advertisement of, or list of the prizes drawn or awarded by means of, any such lottery, gift enterprise, or similar scheme; or, being engaged in the business of procuring for a person I State such a ticket, chance, share, or interest in a lottery, gift, enterprise or similar scheme conducted by another State . . ., knowingly transmits in interstate or foreign commerce information to be used for the purpose of procuring such a ticket, chance, share, or interest; or knowingly takes receives any such paper, certificate, instrument, advertisement, or list so brought, deposited, or transported, shall be fined under this title or imprisoned not more than two years, or both. [emphasis added].

enacted the Atomic Energy Act regulating nuclear power].) The Court must start with the assumption that the states' police powers were not to be superseded "unless that was the clear and manifest purpose of Congress." (*Ibid.*) "Congress's purpose is most clear, of course, when the federal statute at issue explicitly prohibits state regulation in the same field." (*Man Hing Ivory and Imports, Inc. v. Deukmejian* (9th Cir. 1983) 702 F.2d 760, 763.)

Despite federal involvement in the Internet, defendant can provide no evidence that Congress, the DOC, or any other federal agency or authority expressly or impliedly sought to preempt California's anti-lottery legislation. Rather, Congress has refused to create legislation that controls the Internet. (Decl. of Traina, Ex. G; *United States General Accounting Office* memorandum (July 7, 2000), p. 8 ["Although the U.S. government has supported and funded the development of the domain name system, Congress has not chosen to legislate specifically in this area nor has it designated an agency to be responsible for it."].)[2]

Defendant ICANN is nothing more than a private company with whom the federal government has contracted to manage the Internet.[3] Accordingly, the DOC intended that defendants be provided no legal immunities in order to insure "fair play" and to safeguard against "abuses of power." (See *Management of Internet Names and Addresses ("MINA")* 63 Fed.Reg. 31741, p. 14, ¶9, "Principles for a New System"["Legal challenges and lawsuits can be expected within the normal course of business for any enterprise and the new corporation should anticipate this reality"].)

Defendant ICANN itself understood the DOC's intent to provide it no legal immunities with regard to the distribution process of the new <.biz> TLDs and agreed to abide by all established laws by

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[2]Likewise, Defendants cannot reasonably argue that Penal Code section 319 is impliedly preempted because compliance with both the federal objectives and section 319 can occur. (See *Florida Lime & Avocado Growers, Inc. v. Paul* (1963) 373 U.S. 132, 142-143 [10 L.Ed.2d 248, 83 S.Ct. 1210].) As articulated in Plaintiffs' opening brief, defendants have reasonable, non-criminal alternatives to distributing the <.biz> domain names including, but not limited to, a "first-com first-serve basis", a competitive bidding process, or from randomly selecting domain name registrants from a pool of applications accepted without consideration. This being the case, Penal Code section 319 does not stand as an obstacle to the execution of the objectives of Congress, but merely the commercial interests of Defendants. (See *Hines v. Davidowitz* (1941) 312 U.S. 52, 67 [85 L.Ed. 581, 61 S.Ct. 399].)

[3]Defendant Nuelevel, and all registrars, are sub-contractors of ICANN, and therefore are subject to the same laws and regulations as ICANN.

promising to "engage in any other related *lawful activity* in . . . the development of policies for determining the circumstances under which new top-level domains are added to the DNS root system." (See Decl. of Traina, Ex. C; *Memorandum of Understanding ("MOU")*, § III(B)(i-iv)[emphasis added]).

Like defendant ICANN, defendant Nuelevel and the registrars also recognize their susceptibility to lawsuits arising from the <.biz> registration process. This acknowledgment is evident because the "registrars" are required to "refrain from engaging in any illegal, unfair, or deceptive trade practices." (See Decl. of Traina, Ex. D; *Proposed Unsponsored TLD Agreement*, Appendix F, p. 56). Furthermore, MINA specifically provides that "[N]othing in the domain name registration agreement or in the operation of the new corporation should limit the rights that can be asserted by a domain name registrant or trademark owner under national laws." (See *MINA*, 63 Fed.Reg. 31741 (1998), p. 21). Defendant realizes it is subject to the existing laws of this country—whether federal or state. There is simply no evidence to support defendant's tenuous position of preemption.

Defendant erroneously argues that California's state anti-lottery statute is invalid because it effectively regulates the Internet and the Federal Government. Defendant is wrong for several reasons. *First*, California's lottery legislation does not attempt to regulate the federal government or the Internet—only lotteries. The fact that defendant is conducting the lottery on the Internet does not provide it with absolute immunity from prosecution for illegal acts. *Second*, California's state anti-lottery legislation does not conflict with any federal "regulation in the same field," i.e., lotteries. (*Man Hing*, *supra*, 702 F.2d at p. 763). In fact, 18 U.S.C. § 1955, expressly empowers states to enact anti-lottery legislation like Penal Code § 319 to prevent games of chance. Hence, there simply is no conflict between federal and state law with regard to the regulation of lotteries.

Third, defendant has failed to provide evidence of any statute or regulation that expressly or impliedly prohibits state regulation of lotteries on the Internet. Defendant's reliance on *Man Hing*, *supra*, for the proposition that California's anti-lottery statute is unconstitutional is unavailing. In *Man Hing*, the court found the Endangered Species Act contained language that preempted state law. The act stated: "Any State law or regulation which applies with respect to . . .interstate or foreign commerce in, endangered species or threatened species is void . . ." (*Id.* at p. 763). Here, however, defendant fails to provide any evidence that remotely suggests preemption as found by the *Man Hing* court. The reason

for this is apparent: defendant simply has no evidence that any federal statute or scheme was intended to preempt California's anti-lottery laws.

Defendants' attempt to *"super-bootstrap"* 42 U.S.C. §§ 1870(c), 1862(a)(4), 1862(g), the Management of Internet Names and Addresses ("MINA") 63 Fed. Reg. 31741, and the Memorandum of Understanding between the DOC and ICANN ("MOU") for the proposition that the existing federal and state lottery laws are preempted is not convincing. *Not one of these statutes, regulations, or documents contain any language that provide defendant with immunity, or preempts any existing federal or state statute.* In fact, the opposite is true. As illustrated above, all defendants are completely aware that they must abide by all existing laws and refrain from any illegal, unfair or deceptive practices. Hence, defendant's Supremacy Clause defense is hopelessly defective and must fail.

III. THE COMMERCE CLAUSE IS INAPPLICABLE

Defendant argues that California's anti-lottery statute, Penal Code § 319, violates the dormant Commerce Clause. Defendant is wrong. By enacting 18 U.S.C. §§ 1955 and 1301, Congress has *expressly mandated* that federal and state prohibitions of lotteries do not restrict interstate commerce. (See *Pic-A-State PA, Inc. v. Commonwealth of Pennsylvania* (3rd Cir. 1994) 42 F.3d 175, 180; see generally *People v. Prevost* (1998) 60 Cal. App. 4th 1382, 1397).

In *Pic-A-State*, which is nearly identical to the instant facts, defendant Pic-A-State PA, Inc., was engaged in the distribution and transportation of lottery tickets in interstate commerce. (*Pic-A-State, supra*, 42 F.3d at p. 176). Although the defendant argued the Pennsylvania statute prohibiting lotteries was invalid because it impeded interstate commerce, the Court held the state statute valid because it complemented the federal statutes prohibiting the sale of lottery tickets, stating:

> "By amending 18 U.S.C. § 1301, Congress prohibited the interstate sale of lottery interests. Act 8 (the Pennsylvania Statute) complements the federal statute by prohibiting the sale of lottery interests within the borders of the Commonwealth of Pennsylvania. Accordingly, we conclude that Act 8 does not violate the dormant commerce clause." (*Id.* at p. 180).

Likewise, here, California's anti-lottery statute complements federal statutes 18 U.S.C. §§ 1955 and 1301, by expressly prohibiting the creation of, and participation in, lotteries. California's anti-lottery statute does not conflict with the federal statutes prohibiting the interstate sale of lottery tickets, *nor does*

defendant argue the existence of a conflict. (See *Pic-A-State, supra,* 42 F.3d at p. 180 citing *California v. Zook* (1949) 336 U.S. 725, 729 [93 L.Ed. 1005; 69 S.Ct. 841] [the Supreme Court specifically holding that state 'aiding' enforcement statutes are valid even when Congress has made a specified activity unlawful]). Because Congress has specifically prohibited the interstate sale of lottery interests by enacting 18 U.S.C. §§ 1955 and 1301—thereby empowering California to enact its own statute prohibiting lotteries—defendant's reliance on the dormant commerce clause is inapplicable and fatally flawed.

A. Regulation of Lotteries Does Not Violate the Commerce Clause

Defendant relies on *ACLU v. Johnson* (10th Cir. 1999) 194 F.3d 1149 and *American Libraries Association v. Pataki* (S.D.N.Y. 1997) 969 F.Supp. 160, for the proposition that states cannot regulate a lottery on the Internet. (Opp., pp. 12-14). Defendant's reliance on these cases is misplaced for several reasons: *first,* and most importantly, these cases did not contend with a federal statute that specifically proscribed the acts in question; *second,* the courts in these cases were concerned with "national uniformity" with regard to the Internet; and *third,* these cases are inapposite because they dealt with sexually explicit materials distributed over the Internet.

In *ACLU* and *Pataki, supra,* the courts were primarily concerned with subjecting the Internet to inconsistent state laws and grappled with the prospect that the Internet required a "national scheme of regulation." (See *ACLU, supra,* 194 F.3d at p. 1161-1162; *Pataki, supra,* 969 F.Supp. at p. 182). However, the concerns addressed in *ACLU* and *Pataki* are not present in the instant action.

Congress has already provided a "national uniform" scheme of regulation that expressly forbids lotteries by enacting 18 U.S.C. §§ 1955 and 1301. These federally created statutes not only prohibit the formation and participation in lotteries, *they specifically prohibit the sale of lottery interests in interstate commerce.* (See 18 U.S.C. § 1301; *Pic-A-State, supra,* 42 F.3d at p. 180).

The concerns addressed in *ACLU* and *Pataki*—dealing with inconsistent laws regarding individual standards on sexual tolerance, thereby making nationwide regulation impossible—simply do not exist in the present action. Defendant need not be concerned with inconsistencies of individual state laws because the federal government has already mandated a nationwide ban on lotteries in interstate commerce. Because California's anti-lottery law does not conflict with the federal statutes prohibiting lotteries—California's lottery law does not violate the commerce clause.

B. Anti-lottery Legislation Directly Regulates Lotteries--Not The Internet

As analyzed above, Congress has decreed, and the Courts have ruled, that federal and state lottery laws do not burden interstate commerce. (See *Pic-A-State, supra*, 42 F.3d at p. 180). Defendant need not construct multiple systems taking in to consideration the laws of all the individual states. The "national scheme" of *no lotteries* has already been established by Congress. Defendant *must* comply with the laws enacted by Congress, and those complementary laws enacted by the States, which expressly forbid lotteries. Therefore, Defendants' cannot hide behind the tenants of the commerce clause.

Accordingly, in *Ford Motor Co. v. Texas Dept. of Transportation* (5th Cir. 2001) 2001 U.S. App. LEXIS 19185, 4-5, a conflict arouse between Ford Motor Company, who attempted to market cars via their Internet web site, and a Texas statute that prohibited manufacturers from directly retailing motor vehicles to consumers without a Texas dealer's license. The Fifth Circuit found the Texas statute did not violate the dormant commerce clause and distinguished it from *Pataki, supra*, because it did not *directly regulate* Internet activities, stating:

> "Section 5.02C(c) serves as a prohibition on all forms of marketing and sales by manufacturers, not just those conducted via the Internet. In the absence of Congressional legislation, § 5.02C(c)'s *incidental regulation* of Internet activities does not violate the Commerce Clause." (*Ford Motor Co., supra*, 2001 U.S.App.LEXIS 19185 at pp. 22-23 [emphasis added].)

As illustrated above, the court in *Ford Motor Co.* focused on the distinction between legislation that "*directly regulates* Internet activities" versus those that only have an "*incidental*" effect on the Internet. (*Id.*). Here, Penal Code § 319 and 18 U.S.C. §§ 1955 and 1301, which prohibit lotteries, do not *"directly regulate"* Internet activities—but only serve to regulate lotteries. Moreover, Congress has not enacted legislation specifically precluding the Internet from any federal or state regulations. The mere fact that this country's anti-lottery legislation constitutes an "*incidental regulation*" of Internet activities does not violate the Commerce Clause. (See *Ford Motor Co., supra*, 2001 U.S.App.LEXIS 19185 at pp. 22-23.)

Defendant's blanket proposition that any law that incidentally affects the Internet violates the Commerce Clause is fallacious and overbroad. If defendant's contention were true, it would effectively invalidate every federal and state regulation—whether dealing with commerce or not. Such a broad legal theory is not supported by law and "would allow corporations or individuals to circumvent otherwise

constitutional state laws and regulations simply by connecting the transaction to the Internet." (*Ibid.*). The "application of this principle in circumstances like the instant case would lead to absurd results" and create an avalanche of litigation. (*Ibid.*).

Likewise, defendant's assertion that the burden of applying California's unfair competition law would be burdensome and a violation of the Commerce Clause is equally unavailing. Merely because enforcement of Section 17200 may impact defendant's illegal activity related to the Internet, does not mean that Section 17200 is regulating the Internet. (*Ford Motor Co., supra*, 2001 U.S.App. LEXIS 19185 at 22-23). Like the state and federal prohibitions against lotteries, Congress and every state in the Union, including the District of Columbia, has enacted legislation prohibiting acts of unfair competition. Moreover, the California Court of Appeal ruled recently that application of Section 17200 to a nation-wide class is proper. (*Wershba v. Apple Computer, Inc.* (2001) 89 Cal.App.4th 324, *aff'd* at *Wershba v. Apple Computer, Inc.*, (2001) 91 Cal.App.4th 224).

Hence, Section 17200 serves as a vehicle for a nation-wide class action and any "incidental" effect it may have on the Internet is not sufficient to deny its application to the case at bar.

IV. THE ANTI-LOTTERY LAWS APPLY TO DEFENDANT'S <BIZ> DISTRIBUTION SCHEME

In an effort to get around the tri-part analysis (i.e., consideration, chance and prize) which is universally applied to determine whether a particular scheme is a lottery, defendant, NeuLevel, alleges that the Court should look solely at the intent behind the lottery statute(s) in order to determine the legality of their own conduct.[4] (Opp., p. 16). According to defendant, the intent behind the lottery statute(s) combined with defendant's task of efficiently and equitably allocating the domain names creates an exception or exemption from the tri-part test. Neither the intent surrounding the lottery laws nor the task of efficiently allocating domain names creates such an exemption.

First, the intent and purpose of the anti-lottery laws is not limited to "protecting the poor" as alleged by defendant. (Opp., p. 16). The anti-lottery laws were designed to apply to all persons, rich

[4]Defendant's argument is based on "part" of an excerpt found in the *Cudd v. Aschenbrenner* case. (*Cudd v. Aschenbrenner* (1962) 233 Ore. 272.)

or poor, who have provided something of value with the hope of receiving something more valuable. (*State v. Bussiere* (1959) 155 Me. 331.) In *Bussiere*, the Court stated:

> . . . The source of all evil connected with lotteries or gambling is that of a person risking or hazarding something of value, however small, with the hope or opportunity of obtaining a larger sum by chance. (*Id.* at p. 331; *Cudd v. Aschenbrenner*, (1962) 233 Ore. 272 [emphasis added].)

Anti-lottery statutes were intended to apply regardless of the social economic status of the participants. (*Office of the Attorney General of the State of California*, (1981) 64 Op.AttyGen.Cal 629 [Found that recycling machines offering a random payout are considered a lottery]; *People ex rel. Lockyer v. Pacific Gaming Technologies*, (2000) 82 Cal.App.4th 699 [Telephone calling card vending machine was held to be an illegal gaming device where chance determined whether user received money in addition to the card; it was held immaterial that a user always received a card for the amount paid]; *Phoenix Suns Ltd. Partnership v. Abele (In re Harrell)* (D. Ariz. 1994) 1994 U.S.Dist. LEXIS 7188 [Attorney General notified the Phoenix Suns that distribution of Season Tickets under a lottery scheme would be in violation of Arizona Lottery laws].)

Next, and just as important, the legal authorities relied upon by defendant demonstrates that Courts do not apply a pure policy analysis when determining whether the scheme in question is an illegal lottery. The determination whether a practice is a lottery is always made by an analysis of the elements of consideration, chance and prize. The case of *Cudd v. Aschenbrenner* cited by defendant to demonstrate the policy of "protecting the poor" and that "we must consider the circumstances which spawned the lottery laws," held that the defendant was not engaged in a lottery because there was no consideration. (*Chudd, supra*, 233 Ore. at p. 279.) In *Cudd*, the Court stated that: "The crucial inquiry is: Did the participant part with any consideration." (*Id.* at p. 289.) Likewise, the Court in *Daub v. The New York State Liquor Authority*, (1965) 257 N.Y.S.2d. 655 and *Polonsky v. City of South Lake Tahoe*, (1981) 121 Cal.App.3d 464 cited by defendant as examples of cases which reject the "mechanical application of the anti-lottery law," found that defendant's scheme was not a lottery because the element of "chance" was absent and "consideration" was not provided by the Plaintiffs. (*Daub, supra*, 257 N.Y.S.2d at p. 655; *Polonksy, supra*, 121 Cal.App.3d at p. 464.) The cases relied upon by defendant

demonstrates that the decision regarding whether a particular scheme is a lottery revolves around the universal application of consideration, chance and prize.

Third, defendant attempts to label its distribution scheme as "mere processing incident" to avoid the application of the tri-part test is without merit. Defendant's argument is an effort to align their distribution scheme with the facts as stated in *Daub*. The defendant's scheme and the facts in *Daub* cannot be reconciled.

In *Daub*, the defendants establish a system for random selection of applicants who paid a fee in order to prioritize the persons who would be considered for a new lease for package liquor stores. (*Ibid.*) Each person who wanted a new lease was required to pay an application fee. *The applications would be randomly selected by the defendant for purposes of identifying the order from which each applicant would be later considered.* (*Ibid.*) Finding that the selection process was not a lottery, the Court found that the "element of chance as to the numerical order in which the applications are to be processed" was missing. In other words, all applications for the licenses were going to be processed and individually considered by the defendant, thereby eliminating the element of chance.

Defendant's distribution system for the <.biz> domain names is not the same as the "mere processing incident" set forth in *Daub*. The system established by defendant in this case is based upon "chance." In other words, you get the generic name of your choice if you were lucky enough to be chosen. Unlike *Daub*, the applicants can and have applied numerous times to increase their chance of success. Unlike *Daub*, here, no individual consideration will be given to the applicants in defendant's distribution process. Defendant cannot escape the application of the tri-part test simply because of the label they now have chosen.

V. PLAINTIFFS ARE ENTITLED TO EQUITABLE RELIEF

Defendant's allegation that it is entitled to continue the illegal scheme because Plaintiffs across the nation have participated in an "illegal lottery" is legally incorrect. In other words, defendant argues that because defendant has "duped" several million applicants into applying for a <.biz> domain name, the applicants are now barred from seeking equitable relief. (Opp., p. 16). A claim made pursuant to Business and Professions Code section 17200 does not allow this type of result.

As a matter of law, the doctrine of unclean hands does not apply to prevent the granting of a Preliminary Injunction in favor of Plaintiffs who are making a section 17200 claim. (*Kofsky v. Smart and Final Iris Company* (1955) 131 Cal.App.2d 530.) The rationale of allowing a section 17200 claim in the face of an individual Plaintiff, who may or may not have unclean hands, is based upon the Legislature's intent to prevent acts against the public interest. (*People v. James*, (1981) 122 Cal.App.3d. 25, 34.) The rationale as stated above, extends to those circumstances in which the alleged violation was committed by the entire class of persons who either unexpectedly or unknowingly violated the law. (*Ibid.*) Defendant's claim of unclean hands on behalf of either the individual Plaintiffs or the public as a whole has no merit.

VI. PLAINTIFFS HAVE ESTABLISHED ALL ELEMENTS OF AN ILLEGAL LOTTERY

A. A Domain Name Constitutes Property Within The Meaning Of Penal Code § 319

Defendant's argument that a domain name is not property belies the very reason that defendant maintains a lottery is necessary. Defendant argues that a lottery is necessary to "ensure equal access" by allocating a "scarce resource" to avoid "exploitation" by "well-heeled business entities" and to avoid a "land-rush demand" for this scarce commodity. (Opp., p. 1.) Defendant's very own description of why a lottery is necessary establishes that a domain name is property. Defendant attempts to escape from the obvious conclusion that a domain name is property by citing several out of state and federal cases that truly do not deal with the fundamental issue: What is property? In order to answer this question, one need not look any further than the boundaries of the State of California.

California case law and statutory authority have consistently defined "property" as "something that one has the exclusive right to possess and use." (*People v. Kwok* (1998) 63 Cal.App.4th 1236.) Further, Civil Code section 654 defines "property" as the ownership of a thing is the right of one or more persons to possess and use it to the exclusion of others. "In this Code, the thing of which there may be ownership is called property."

The most complete definition, however, (which is consistent with California's definition of "property") is found in *Black's Law Dictionary* (5th Ed., 1979):

"That which is peculiar or proper to any person; that which belongs exclusively to one.

. . .(citations omitted) The word is also commonly used to denote everything which is the subject of ownership, corporeal or incorporeal, tangible or intangible, visible or invisible, real or personal; everything that has an exchangeable value. . . Term includes not only ownership and possession but the right of use and enjoyment for lawful purposes. (citation omitted)"

A 1938 California Court of Appeal decision squarely defined "property" within the meaning of Penal Code section 319. In *Settles v. Superior Court* (1938) 29 Cal.App.2d.Supp. 781, the State prosecuted two employees of an establishment for operating an illegal lottery. The defendants argued that the "prize" won by the lottery was not "property" as used within the meaning of Penal Code section 319. The defendants claimed that the "prize" was merely the right to play another game free of charge. As such, the right to play, the defendants argued, did not constitute property within the meaning of the statute. The Court of Appeal disagreed.

The Court of Appeal held that the term "property", as used by the legislature in Penal Code section 319, should be used in its most general sense.[5] *Settles* relied in part on the case of *Ponsonby v. Sacramento Fruit Lands Company* (1930) 210 Cal.229, wherein the California Supreme Court classified the term property as *nomen generalissimum*. *Nomen generalissimum* means a "name of the most general kind; a name of the most general meaning. (See Black's Law Dictionary (5th Ed.1979).) The *Settles* Court concluded that the right to intangible, incorporeal right to replay another game constituted "property" within the meaning of the Penal Code. In short, the inescapable conclusion is that anything, no matter what shape or form, invisible, intangible, or otherwise, that can be used to the exclusion of another is "property" as that term is defined by the Code of Civil Procedure, Civil Code and the Penal Code. Therefore, the query is simple: Is a domain name something that can be used by one person to the exclusion of all others? The undeniable answer is yes. At the risk of stating the obvious, the entire purpose of the registry process is to allow the successful entity who obtains a domain name to use it to the exclusion of all others. The registration side of the current domain name system architecture is arranged hierarchically to ensure that each domain name is unique—exclusive. Hence, the lucrative side

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[5] The *Settles* Court utilized, in part, the definition of property contained in Penal Code section 7. The Court recognized that the definition of property contained in Penal Code section 7 provided examples of the term property, i.e. money, goods, chattels, etc., and noted that the definition of "property" is not exclusive of anything else properly coming within the terms defined. Penal Code section 7 was amended in 1905 to conform with the definitions of "property" contained in the Code of Civil Procedure and the Civil Code. Therefore, any interpretation of the Code of Civil Procedure and the Civil Code applies with equal force to the *Penal Code*.

of a lottery—convince the applicants to purchase many non-refundable applications to increase their chance to obtain exclusive right to use a domain name. The more you buy, the better chances you have to win. The exact reason California has outlawed lotteries since the 1849 when the original Constitution of the Sate of California was adopted.

The only California decision cited by Defendant is *Hotel Employees and Rest. Employees Int'l Union v. Davis* (1999) 21 Cal.4th 585, 592. *Hotel Employees* does not stand for the proposition that domain names are not property as defendant contends. (Opp., p. 18.) The *Hotel Employees* case dealt with the conflict between the California Constitution and Proposition 5's authorization of casino gambling. Nowhere does *Hotel Employees* state—nor even intimate—that "[b]ecause domain names are not property, a system allocating domain names cannot be a lottery."

Further, defendant cites *Kremen v. Cohen*, (N.D. Cal. 2000) 99 F.Supp. 2d 1168, as authority for its proposition that a domain name is not property. However, *Kremen* is an action by a former owner of a domain name <sex.com> who obtained the registration from defendant Network Solutions, Inc. (NSI). The Plaintiff alleged that co-defendant Cohen wrongfully obtained the domain name by writing a fraudulent letter on Plaintiff's letter head to NSI stating that the Plaintiff abandoned the domain name. As a result of the letter, NSI registered the domain name <sex.com> in co-defendant Cohen's name. Procedurally, the *Kremen* decision concerns a motion for summary judgment brought by defendant NSI as to plaintiff's claims for breach of contract, breach of intended third party beneficiary contract, conspiracy to convert property, conversion to bailee, breach of fiduciary duty and negligent misrepresentation. The pertinent discussion pertains to the conversion causes of action.

Defendant cites *Kremen* for the proposition that "domain names are not protected property and cannot be the subject of a conversion action." (Opp., p. 19.) In fact, the argument asserted by defendant NSI was not that a domain name was not "property" but that it was "intangible property" not subject to cause of action for conversion. The *Kremen* court did not find that a domain name was not "property." Instead, the *Kremen* court merely found that a domain name was neither "tangible property" or "intangible property represented by documents" capable of being subject for a cause of action for conversion. The *Kremen* Court, citing Witkin, *Torts* §613, found that valuable intangible property such as "goodwill of business, trade secrets, a newspaper route, or a laundry list of customers" are not subject

to conversion."

The United States District Court order in *Kremen v. Steven Michael Cohen* is persuasive. The District Court's order states:

> Defendants, relying on *Kremen v. Cohen*, 99F.Supp.2d 1169 (N.D.Cal. 2000), do argue in their cross-motion for summary judgment that a domain names is not a form of intangible personal property. This argument, however, is without merit as this Court has already recognized that a domain name is a form of intangible property. *Kremen*, 99 F.Supp.2d at 1173 ("NSI contends that a domain name is a form of intangible property. . . The Court concurs."); *see also*, Cal.Civ.Code §§655, 654; *Yuba River Power Co. v. Nevada Irrigation Dist.*, 207 Cal. 521, 523 (1929) (stating that property includes "everything which one person can own and transfer to another. It extends to every species of right and interest capable of being enjoyed as such upon which it is practicable to place a money value."); *McCord v. Plotnick*, 108 Cal.App.2d 392, 395 (1952) ("In a court of equity 'if that which complainant has acquired fairly at substantial cost may be sold fairly at substantial profit and to the disadvantage of complainant cannot be heard to say that it is too fugitive or evanescent to be regarded as property.") (See Decl. of Charles Carreon and District Court Order attached to his Decl. as Exhibit "A".)

Thus, the argument that domain names are not property has no merit. Moreover, the fact that valuable property such as trademarks or domain names are not subject to conversion does not mean that they do not constitute "property." For example, good will is not property subject to conversion. However, for almost forty years good will has been uniformly categorized as "property". (*Haldeman v. Haldeman*, (1962) 202 Cal.App.2d 498.)

The Defendant also cites *Lockheed Martin Corp. v. Network Solutions, Inc.* (9th Cir. 1999) 194 F.3d 980 and *Network Solutions, Inc. v. Umbro Int'l*, (2000) 259 Va. 759 as authority for its proposition that domain names are not property. Once again, these cases are entirely impertinent. Interestingly, the Defendant in *Kremen* relied heavily upon *Lockheed Martin Corp.* and *Network Solutions, Inc.* to support its position regarding the classification of a domain names as property . The *Kremen* Court found these cases to be inapplicable as to the proper classification of a domain name. The *Kremen* Court succinctly summarized the *Lockheed Martin Corp.* case as follows:

> "In *Lockheed*, Plaintiff Lockheed Martin registered a service mark in the phrase "Skunk Works." Lockheed sued NSI for trademark infringement, arguing that NSI diluted its service mark by permitting third parties to register variations of the phrase "skunk Works." The Court held that NSI's function did not subject it to liability for contributory infringement of a trademark because it merely provides a service, not a product. Thus unlike the present situation, in *Lockheed* the focus was on NSI's role, rather than the proper classification of a domain name." (*Kremen, supra*, 99 F.Supp. at p. 1173, fn1.)

In *Umbro*, the issue was whether a domain name could be subject to garnishment. The Supreme Court recognized that a judgment creditor could only proceed with garnishment proceedings if "there is a liability" on a third person to the judgment debtor. (*Umbro, supra,* 259 Va. at p. 768.) The Virginia Supreme Court found that the "domain name registration" is the product of a contract for services between a registrar and registrant. (*Id.*. at p.770.) In fact, the court in *Umbro* recognized in its analysis that a domain name could be considered property in that Congress passed the Anticybersquatting Consumer Protection Act ("ACPA") which authorizes an *in rem* civil action against a domain name. The Court observed that since the legislation supports an *in rem* proceeding, it could be argued that a domain name is property. However, the Court's determination did not turn on the classification of a domain name as property. The Court stated:

> "Irrespective of how a domain name is classified, we agree with Umbro that a domain name registrant acquires the contractual right to use a unique domain name for a specified period of time." (*Ibid.*)

The Court concluded that for purposes of a garnishment proceeding, a domain name is inextricably bound to the services provided by the registrar, and therefore, it is not subject to garnishment since it is not a "liability" owed by the third person to the judgment debtor. (*Ibid.*) The Court did not, contrary to defendant's assertion, determine whether a domain name is "property".

A registered domain name is clearly "property" as that term has been defined by California law. An entity with a registered domain name obtains exclusive use of the domain name for a specified period of time. (*Ibid.*) Further, it is a valuable right as established by the defendant's admitted purpose for a lottery. Defendant admits that a lottery is necessary to avoid a "land rush" demand for domain names. It is illogical to argue that there would be a land rush for something that is not valuable. In fact, Congress recognized the valuable nature of domain names so much so that it passed the ACPA. Therefore, since a domain name is something of value that is used by someone to the exclusion of others, domain names clearly fall within the meaning of "property" as used in Penal Code section 319.

It is a primary rule of construction that courts are bound to give effect to statutes according to the usual, ordinary import of the language employed in framing them. (*Benson v. Superior Court* (1963) 214 Cal.App.2d 551, 558.) Defendant's distortion of the term "property" does not comport with

California law. Like the *Settles* decision, wherein the court found that the prize--the right to play one more game--was "property" as used in the Penal Code, the inescapable conclusion is that a domain name, *which is used to the exclusion of all others in the world,* constitutes property.

B. Plaintiffs Have Established The Element Of Chance

Defendant's contention that the element of "chance" does not exist under their distribution scheme because of the remote possibility that only one applicant may have submitted applications for a particular domain name is without merit. (Opp., p. 20.) According to defendant, and assuming the above facts, the right to a particular domain name will be automatically given to the sole applicant, therefore eliminating the need for a "randomized selection" and thereby eliminating the "chance" requirement. Defendant's argument misconstrues the basic definition of "chance" and ignores their own scheme which was established for the purpose of handling a "land rush" of applicants seeking the same generic name.

"Chance" means that winning and losing depend on luck and fortune more than judgment and skill. (*Finster v. Keller* (1971) 18 Cal.App.3d 836, 844-845.) Whether the element of "chance" exists is not determined in hindsight by the operator of the game. "Chance" exists where applicants, at the time of paying valuable consideration for the "chance" understood or expected that the prize is to be distributed or disposed of by lot or "chance." (*Niccoli v. McClelland* (1937) 21 Cal.App.2d Supp. 759.) Moreover, a game is not regarded as one of skill merely because that element enters into the result in some degree, or is one of chance solely because chance is a factor in producing the result. (*People v. Settles* (1938) 29 Cal.App.2d.Supp. 781.) The test of the character of a game or scheme as one of chance or skill is, which of these factors is dominant in determining the result? (*Ibid.*)

From the perspective of either the defendant or the Plaintiffs, the distribution system established is predominately based on chance. Defendant has admitted that the system it established was as a direct result of the "land rush" of generic domain name applicants. Defendant's agreement with the registrars did not limit the number of applications for the same domain name. NueLevel's registrars advertise that the system created by NueLevel is a "lottery," and the more applications submitted the better the "chances" are of receiving the domain name the applicant selected. To argue that skill is the dominant factor because you could pick an "obscure" name is akin to changing the rules of the game in midstream. If skill was the predominant factor, as alleged by defendant, the domain names could rationally be

distributed on a first come first serve basis. The expectation by defendant and the basis for the distribution system established was based on chance.

From the perspective of the Plaintiffs the rationale is the same. Plaintiffs are participating in a system created by defendant. Plaintiffs seek generic domain names which will attract customers to their businesses. Plaintiffs, consumers and businesses alike apply for the generic names and are admittedly never told whether others have applied for the same name. The number of applicants which have applied for the same domain name is a veritable mystery which was intentionally created by defendant to increase the number of applications for the "land rush" of generic domain names. The dominant factor, whether viewed from the perspective of the defendant or the Plaintiffs, is based on "chance."

C. The Element Of Consideration Has Been Established By The Plaintiffs

Defendant's allegation that Plaintiffs have not paid consideration because defendant only received a $2.00 application fee which may or may not cover their costs is irrelevant. The Supreme Court of California has addressed the issue of consideration in conjunction with Penal Code section 319 and found that the question of consideration is determined from the standpoint of the ticket holder. (*California Gas Retailers v. Regal Petroleum Corp.* (1958) 50 Cal.2d 844.) The Court in *California Gas Retailers* stated:

> It would again appear that, in view of the plain provisions of section 319 of the Penal Code, in order to constitute consideration within the definition of a lottery there must be a valuable consideration paid, or promised to be paid by the ticket holder. (*Id.* at p. 789; also citing *People v. Carpenter* (1956) 141 Cal.App.2d 884.)

The Supreme Court also found that absent a "gratuitous distribution of property" courts throughout the country have found that the lottery laws are violated. (*Ibid.*)

It is said in 34 American Jurisprudence 650:

> . . .that no sooner is the term "lottery" defined by a court, than ingenuity evolves some scheme within the mischief discussed, although not quite within the letter of the definition given; but an examination of the many cases on the subject will show that it is very difficult, if not impossible, for the most ingenious and subtle mind to devise any scheme or plan, short of a gratuitous distribution of property, which has not been held by the courts of this country to be in violation of the lottery laws... *California Gas Retailers* at 844 [emphasis added].

In the face of the Supreme Court's decision, Defendant argues that the "fee" they receive from

their lottery does not cover some of their costs of administering the intellectual claim procedure, thus, no consideration has been given. Defendant cites the one page opinion in *Polonsky v. City of South Lake Tahoe, supra,* 121 Cal.App.3d 464 in support of its position. First, no analysis was done by the Court in *Polonsky* regarding the issue of consideration. The decision is one page in total and cites no legal authority or basis for its decision. In fact, the Supreme Court's decision in *California Gas Retailers* regarding the issue of consideration is never even mentioned. Given the limited scope of *Polonsky*, the Court should follow the long standing black letter law and its corresponding policy which was established by the California Supreme Court.

VII. ON BALANCE, ALL FACTORS WEIGH IN FAVOR OF A PRELIMINARY INJUNCTION

A. An Injunction Would Preserve The Status Quo

First and foremost, the issuance of a preliminary injunction will maintain the status quo. It has been sixteen years since a new top level domain name has been introduced. There is no compelling reason why <.biz> cannot wait to be introduced at the conclusion of this litigation. In fact, defendant NeuLevel's own web page, notifies prospective applicants that the October 1, 2001 date is "subject to change." (Decl. of Traina, Ex. E.)

On the other hand, the Plaintiffs will suffer grave injury if the <.biz> domain names are distributed under the lottery scheme. Plaintiffs, by defendant's own account have spent millions of dollars in application fees. Plaintiffs will undoubtably spend millions establishing web sites with their new respective domain names. How could this Court repair the damage to all of the internet users world-wide (including Plaintiffs), if preliminary injunction is issued and Plaintiffs later prevail? If the Court allows the lottery to go forward, and the Plaintiffs prevail, the court would have to declare that the distribution of the names was illegal. The names domain names would have to be re-deposited with a new registry to be re-distributed legally. The damages to those plaintiffs who received the domain name, consumers and business that relied on the domain name is immeasurable.

B. The Plaintiffs Success On The Merits Favors An Injunction

Plaintiffs have conclusively established that the defendant has engaged in an illegal lottery. The

overwhelming evidence easily surpasses the threshold showing of "a substantial likelihood of prevailing on the merits". "[T]he more likely it is that plaintiffs will ultimately prevail, the less severe must be the harm that they allege will occur if the injunction does not issue. This is especially true when the requested injunction maintains, rather than alters, the status quo." (*King v. Meese* (1987) 43 Cal.3d 1217, 1227.) "[I]f the party seeking the injunction can make a sufficiently strong showing of likelihood of success on the merits, the trial court has discretion to issue the injunction *notwithstanding that party's inability to show that the balance of harms tips in his favor*. [Citation.]" (*Common Cause v. Board of Supervisors* (1989) 49 Cal.3d 432, 447 [emphasis added].) The foregoing direction from the Supreme Court has particular application in this matter. The evidence establishes that the defendant has engaged in illegal conduct. The defendant should be enjoined on that ground alone. However, defendant's conduct is combined with Plaintiffs substantial injury that can not be undone if the Court does not enjoin the defendant's lottery. This is particularly in light of the fact that defendant's prospective harm is imaginary and self-inflicted.

C. The Court Should Not Consider Defendant's Alleged Harm As Defendant Has Unclean Hands

Defendant's plea that the lottery system is the only "fair" distribution method and that it will be harmed by the issuance of an injunction is unavailing. The defendant preaches that the need and justification for the lottery is to protect businesses big and small; to provide equal access for all of the "David" companies who are so often trampled by the "Goliath" monopolies in the ruthless internet world. However, all the NeuLevel lottery scheme does is enable David and Goliath to buy rocks (applications) at the same price. Of course, the Goliath monopolies will have much more money to buy the applications than David. Thus, once again, David has one rock with a sling against the vast arsenal of Goliath.

The real question is: who really benefits from the fight between David and Goliath? The one selling the rocks–Defendant Neulevel. This scenario is the exact reason why California outlawed lotteries from the very first day this state was admitted into the Union. California does not want the Davids of the world to plunk down five dollars for a lottery ticket (application) with the hope of winning the big prize (a domain name).

Defendant NeuLevel claims that the lottery is necessary to prevent a "land rush". Who created the "land rush"? Defendant NeuLevel. How? Defendant's own words:

> "Neulevel itself spent millions of dollars in marketing and advertising to aggressively promote the October 1 launch date. In the past sixty days. . .NeuLevel's executives have appeared on radio and television on numerous ocassions.. . . .The registrars, many of whom are defendants in this case, have also spent millions of dollars and made countless promotional efforts concerning the October 1 launch. . . ." (Opp., p.28.)

If there was going to be such a "land rush", why did Defendant NeuLevel and the registrars have to spend millions of dollars aggressively marketing and advertising the launch date? Defendant NeuLevel created, promoted, incited, and profited off of the fight between David and Goliath. Defendant NeuLevel is just like the bookie who spent countless dollars setting up his global telephone network and on the eve of his first big betting event he is arrested by the police. He proclaims: "What do you mean your shutting down my illegal gambling operation! You can't down shut it down! I spent too much money getting it organized!" The answer is plane and simple, Defendant NeuLevel's expenditures on an illegal lottery can not be considered in whether an injunction should issue.

The issuance of a preliminary injunction maintains the status quo; protects plaintiffs from irreparable harm; and does not prejudice the defendant at all.

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VIII. CONCLUSION

WHEREFORE, Plaintiffs respectfully request that the Court grant its Motion for a Preliminary Injunction.

Respectfully Submitted,

DATED: September 21, 2001

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